

CSR and the Supply Chain: The Case of the Global Retail Supply Chains Managed by the Hudson's Bay Company (HBC)

Canada

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Executive Summary

Corporate Social Responsibility (CSR) within the supply chain is an issue that has been discussed extensively within the Canadian economy. Canadians understand and support the economic benefits resulting from the trend towards freer trade and the sourcing of goods from overseas. At the same time, Canadians do not want to be seen as supporting economies and suppliers who insist on using CSR practices, particularly labour practices, that fail to adhere to International Labour Organization (ILO) and United Nations (UN) minimum standards.

Canadian consumers have demanded that their retailers carefully select and audit suppliers to ensure that they adhere to global standards of conduct within the supply chains that they use. Retailers such as the Hudson's Bay Company (HBC) have responded to these demands with enthusiasm. Indeed, in addition to CSR policies focused on the elimination of suppliers with unacceptable labour practices, or "sweatshops" from within the supply chain, the Hudson's Bay Company's definition of social responsibility includes environmental responsibility, such as energy efficiency and waste reduction, efficient transportation practices, and efficient practices related to building and operating retail stores.

For HBC however, it is the principles of corporate social responsibility that translate into the procedures and policies for managing global supply chains and avoiding the exploitation of workers from other economies.

The HBC goes through considerable lengths to ensure that products sold to Canadians come from "socially responsible" suppliers and economies or those that adhere to, or at least are willing to work towards adhering to generally accepted socially responsible practices and labor standards.

HBC has set up a Social Responsibility Program and an Ethical Sourcing Program that include an in-house Code of Vendor Conduct with stringent vendor prioritization and conduct verification policies.¹ In this way, HBC seeks to ensure that it only does business with suppliers that support and align with its own social responsibility goals. In the process, it is helping to promote business practices within its supply chains which reflect an acceptable definition of CSR.

Introduction

Corporate social responsibility within the supply chain is an issue that has been discussed extensively within the Canadian economy. The issue is very much related to the rapid globalization of supply chains in Canada, particularly in the retail sector. Canadians understand and support the economic benefits resulting from the trend towards freer trade and the sourcing of goods from foreign countries. At the same time, Canadians do not want to be seen as supporting economies and suppliers who insist on using CSR practices, especially relative to labour, that fail to adhere to International Labour Organization (ILO) and United Nations (UN) minimum standards. As a result, Canadian consumers have demanded that their retailers carefully select and audit suppliers to ensure that they adhere to such global standards of conduct within the supply chains that they use.

This case study relates the efforts being made within the Canadian economy to incorporate the principles of corporate social responsibility into the procedures and policies that manage global supply chains. It uses the case of a very well-known large Canadian company, the Hudson's Bay Company (HBC), to illustrate the lengths to which all Canadian retailers go to ensure that products sold to Canadians come from "socially responsible" suppliers and economies, those that

¹ 2005 Social Responsibility Report of the Hudson Bay Company. Website: <http://www.HBC.com>.

adhere to, or at least are willing to work towards adhering to generally accepted socially responsible practices and labour standards.

The case first presents Hudson Bay Company as a company firmly focused on ensuring CSR at all levels of its supply chain. It goes on to outline the Canadian context within which Canadian retailers, such as HBC, set up and operate global supply chains, with emphasis on the CSR practices of those supply chains. By necessity, the practices used in the Canadian economy have to be aligned with global practices negotiated under the UN or ILO umbrella since Canada is usually a signatory, and often one of the founding members of these organizations.

There are broad CSR issues discussed in Canada. The case examines those that are of concern to Canadians within the supply chain and summarizes the mechanisms used by Canadian industry, both domestic and global initiatives, to support the desired social responsibility goals. At the core of these initiatives is also the rights of individual economies to enact standards and labour laws that meet specific local needs that are, hopefully, consistent with the international standards.

The appendices to the report provide links to web sites containing information about CSR and the supply chain, and some detailed information on important global initiatives from economies outside of APEC.

Case Study: Hudson's Bay Company's Ethical Sourcing Program

Founded in 1670, the Hudson's Bay Company (HBC) is Canada's oldest diversified general merchandise retailer, operating in department store (the Bay), mass merchandise (Zellers), specialty (Home Outfitters and Designer Depot) and discount (Fields) retail formats.

With over 550 stores and nearly 70,000 associates located in every province in Canada, HBC provides Canadians with stylish, quality merchandise at great value, through retail banners focused on exceptional customer service.

HBC is a Canadian retail leader in corporate social responsibility. (Fourth Annual HBC CSR Report can be found at Website: <http://www.HBC.com>).

Canadian companies in general, and Hudson Bay Company in particular, are reacting to the Canadian's desire for effective CSR within the supply chain. Canadians generally support the Responsible Trading Guidelines of the Retail Council of Canada (governing all Canadian retailers), and the programs implemented by Hudson's Bay Company as part of its activities within its own global supply chains.

Social responsibility, as defined by HBC, goes beyond the concept of ethical sourcing and also includes environmental responsibility, such as energy efficiency and waste reduction in day to day operations, transportation practices, and practices related to building and operating retail stores.

HBC operates within a CSR environment legislated by the government of Canada, as well as by the retail association's supply chain initiatives which are described in more detail in the succeeding section of the case.

CSR Developments in Canada

Canadians refer to supply chain operations that fail to use acceptable practices as “sweatshops”. A sweatshop is most often described as a workplace in which workers are employed for long hours at low wages and under unhealthy or oppressive conditions. The U.S. General Accounting Office has developed a working definition of a sweatshop that is widely accepted in the Canadian economy as:

“an employer that violates more than one federal or state labour, industrial homework, occupational safety and health, workers' compensation, or industry registration law”

The term sweatshop was derived from the English word *sweater*. The term was first used in the mid 19th century to describe an employer or middleman who paid very low wages for long, monotonous work. The word *sweatshop* described a subcontracting system in which the middlemen earned profits from the margin between the amount they received for a contract and the amount they paid to the workers. The margin was said to be “sweated” from the workers because they received minimal wages for excessive hours worked in often unsanitary conditions.

In the 1880s, this type of working conditions was widespread in all economies currently described as “developed”. The phenomenon was initially supported by a large number of migrant workers from eastern and southern Europe desperately looking for work and willing to work for very low wages under almost any working condition. The practices were perpetuated at the turn of the century, and during the 1930s (the Great Depression), when terrible economic conditions made very difficult working conditions, even abuse of workers, a daily reality – a fact that is conveniently overlooked by many stakeholders in what are now more “developed” economies. By the middle of the 20th century, a growing social conscience for the plight of workers resulted in legislation to eradicate or control the existence of “sweatshops” in most of these developed countries.

Canadians realize that improving labour standards and eliminating supply chain operations that can be described as “sweatshops” is a journey that requires some time. According to the Encyclopedia Britannica, five main factors have contributed to the control of sweatshops in the 20th century:

- the growth of social idealism,
- pressure of the trade unions,
- extension of the business franchise,
- greater economies of scale of factory production, and
- the acceptance of modern labour practices with increased interest in human relations within industry.

The reality is that sweatshop conditions continue to exist in a number of APEC economies today, usually illegally or as part of the underground economies. They can be especially prevalent in less developed economies where certain “lower” socio-economic conditions tend to be more common, including:

- A large unskilled and unorganized workforce (which may include children) is readily available.
- A workforce is desperate for work.
- There are questionable management practices that are used to take advantage of this workforce.
- A state or governing body is possibly ignorant of the situation, incapable of rectifying it, or lacking in resources, capability or willingness to intervene.

It is clear that poverty and economic weakness are the root causes of the sweatshop phenomenon. Under such conditions, workers, and maybe even some governments, feel that they have to accept whatever conditions are given to them because the alternatives, (perhaps starvation and disease) are considered less appetizing.

Arbitrary employment practices are also a driving factor for workers accepting their working conditions. The fear of losing their only income-generating opportunity is a great motivating factor in maintaining silence and bearing the work load.

HBC's Social Responsibility Program

HBC is among a large group of Canadian retailers that aggressively drive social responsibility standards and have actively participated in the Retail Council of Canada Responsible Trading Guidelines.²

However, a closer look at the industry CSR trading guidelines reveal that they only ask retailers to use “reasonable” efforts to require their suppliers to provide decent, legal and humane working conditions at the manufacturing stage. They are also asked to use “reasonable” efforts to require their contractors to include these guidelines in their contracts.

This language is necessary because the Retail Council is an association, not a regulatory body. It would be inappropriate for the Council to require adherence to anything. In addition, the Council represents a wide range of retailers, from very small to very large. It would be difficult for the association to require from small retailers the same level of effort required from large ones who obviously have much more resources to use in addressing issues related to CSR in the supply chain. Finally, the Council can only really be active in the domestic Canadian economy. Addressing issues outside of Canada would be outside of its mandate.

For these and other reasons, HBC's own CSR program is much more rigorous than those suggested by the Retail Council's Responsible Trading Guidelines. The program is backed up by first, a rigorous verification procedure, and second, by a process by which suppliers are asked to make improvements on CSR within a certain timeframe.

HBC believes that social responsibility really encompasses all aspects of interactions with HBC stakeholders including employees, customers and the environment within which it operates. These interactions are a reflection of the values embedded in the culture of a retailer like HBC.

Arguably Canada's oldest and first company, HBC has a history spanning more than 370 years. It helped build the Canadian economy, particularly in the early years when Canada as an economy did not even exist. For this reason, the CSR culture of HBC goes beyond the company and includes a commitment to the various communities where it operates.

HBC's social responsibilities are very diverse and include a charitable foundation dedicated to improving the lives of Canadians by working with local and national organizations to invest in three key areas: a) building healthy families, b) creating strong communities, and c) inspiring Canadians to become more socially responsible.

The HBC believes that effective social responsibility begins at home, thus it invests in local hospitals, oncology centers, the Canadian Red Cross Disaster Relief Fund and Women's Shelters as part of its HBC foundation initiative. It also invests in programs for employees including those that ensure that employees are treated with respect and in a courteous and fair manner at all times.

² Responsible Trading Guidelines. Website: <http://www.retailcouncil.org>.

This commitment to CSR extends to areas outside the company and over 500 locations in Canada with nearly 70,000 employees. The company actively supports the volunteer efforts of its employees who actively participate in community and fund-raising efforts to help needy families within the communities served by HBC.

Under environmental responsibility, HBC has developed a comprehensive strategy to become more energy efficient, both within its stores and within the supply chain. They have done this by installing sensitive energy-demand controls and high-efficiency motors within heating, ventilation and air-conditioning plants. New stores are being designed to be 25% more energy-efficient than what is required by existing building codes. Such codes are viewed as only minimum standards and HBC knows that it can do substantially better by capitalizing on state-of-the-art technology to control and limit energy use.

The company's environmental response strategy has been very successful in reducing electricity use in retail operations by more than 100 MW and natural gas consumption by almost 10 million m³. This represents annual greenhouse gas emission reductions of about 50 megatons or the equivalent of removing 10,000 cars from the road each year.

Within the supply chain, environmental policies have resulted in the purchase of high-efficiency supply-chain equipment, and include utilizing rail-based Intermodal services in high-density corridors to help reduce fuel consumption and therefore greenhouse gas emissions. These broad CSR efforts are ongoing.

HBC has implemented its global reporting initiative, a commitment to identify and report on a large number of CSR indicators in their yearly CSR report (See Website: <http://www.HBC.com>). This initiative covers more than 32 economic and environmental performance indicators that are to be tracked year after year, and include indicators on labor practices, human rights and societal contribution.

HBC's Ethical Sourcing Program

HBC's Ethical Sourcing Program is defined as its commitment to being socially responsible in terms of the programs and policies that govern the sourcing of products sold through HBC.³ Because HBC has thousands of partners inside and outside Canada, HBC feels that it can make a significant impact on ethical sourcing issues if it works with merchandise vendors and manufacturers around the world, to ensure that its merchandise sourcing policies comply with international labor and human rights standards.

The goal of the social compliance program is to ensure that all HBC brands have been produced under humane conditions and protect the integrity of HBC's private brands. They do this through education and collaboration to ensure that meaningful progress can be realized in CSR within the supply chain.

The ethical sourcing program encompasses three basic principles.⁴

1. educating and training of HBC buyers, vendors and manufacturers on the Code of Vendor Conduct and audit process as a core element of HBC's auditing and compliance programs;
2. improving the quality and transparency of dialogue with external stakeholders; and

³ "Taking Care of Our Home." 2005 HBC Social Responsibility Report: 35. Website: <http://www.HBC.com>.

⁴ *Op. cit.*, 36.

3. leveraging international relationships to seek common programs that enhance the efficiency and effectiveness of social compliance within the global retail supply chain.

HBC realizes that it will be much less effective acting alone than if it were to act in concert with partners and other recent retailers to observe effective CSR within the supply chain. Its efforts start with education and training of HBC buyers, vendors and manufacturers about the code of conduct and the way the verification processes will be implemented. Such training helps suppliers, vendors and HBC associates to understand policies and procedures. For example, HBC introduced an intranet online learning course in 2005, which over 400 associates have completed so far. It is important that buyers and vendors are accountable for the factories they use for sourcing products.

A second principle involves removing secret practices and making everything transparent to external stakeholders. After all, “If you have nothing to hide, than you shouldn't have to hide anything.”

Finally, CSR within the supply chain is a global issue by virtue of globalization and free trade. As a result, effective CSR is highly dependent on establishing links and partnerships with other institutions, associations and companies with similar CSR goals. For example, the 2005 CSR report indicated that HBC:

... attends the annual Intertek Conference on social compliance, which provides an opportunity to collaborate with retailers, consumer brand companies and other stakeholders on the issues and challenges facing the industry in relation to social compliance. This... allows leaders in CSR to share ideas and experiences related to the implementation and performance measurements of ethical sourcing programs and their impact on the supply chain. One of the key challenges in the area of collaboration is achieving co-operation within the industry to address non-compliance.... HBC has taken the initiative to develop research and projects with Canadian Business for Social Responsibility (CBSR) to find effective methods for Canadian retailers/brands to establish a framework of collaboration within Canada. HBC continued working with the Fair Factory Clearinghouse (FFC) to advance international collaboration on programs and audit sharing.

Any CSR initiative is only as strong as its weakest link — usually those willing to gloss over poor CSR practices in the name of profit or rapid development. It is only through a concerted effort by all governments, all retailers and all suppliers that poor CSR practices in the supply chain will be eradicated throughout the world. HBC is committed to work with any and all its global partners and competitors to improve practices in the supply chain.

The ethical sourcing program at HBC is made up of two specific initiatives, a social compliance program and the HBC Code of Vendor Conduct. These initiatives are backed by an independent compliance and monitoring program which helps ensure that HBC's purchasing power is a force for positive social change in the economies that manufacture the products that it sells to Canada. HBC believes that working for ethical practices within their supply chains is of fundamental importance, and that it is a responsibility shared across the company: from the Board of directors, to the CEO, through senior management in their Social Compliance department who oversee the program and manage the day-to-day responsibilities, and right through to the merchants and sourcing teams who buy products in many economies around the world. HBC sees ethical sourcing, as “the bedrock of their business operations”.

HBC's social compliance program attempts to ensure that the products being sold in HBC stores are produced in conditions that respect the human rights principles as reflected by the United

Nations such as those of the *United Nations Global Compact* dialogue,⁵ and those of the International Labor Organization and its *International Labour Standards*.⁶

These standards address issues like:

- forced or child labor within the supply chain,
- respect for the right of employees to free association and collective bargaining, where applicable,
- humane treatment of workers,
- protection of the health and safety of workers, and
- avoidance of undisclosed trans-shipments (used by certain unscrupulous suppliers specifically to avoid ethical sourcing practices and codes of conducts).

HBC expects their vendors to share these ethical standards. It distributes a “Social Compliance Starter Kit: Policy and Procedures” to all existing and new vendors which contains information about HBC’s policies, the social compliance process, registration information and its Code of Vendor Conduct.

HBC requires all domestic and direct import vendors to participate in HBC’s Social Compliance program. Through HBC’s Global Sourcing department, facilities that manufacture the company’s merchandise are audited regularly by third party auditors to ensure compliance with the Code of Vendor Conduct. HBC’s Social Compliance team meets regularly with vendors to inspect their factory, list compliance issues, formulate corrective action plans and re-audit schedules. These meetings ensure improved social compliance monitoring on a regular basis.

*HBC’s Code of Vendor Conduct*⁷

The HBC Code of Vendor Conduct (CVC) is at the heart of HBC efforts towards CSR within the supply chain. HBC reports that it fully intends to conduct its business in a socially responsible manner and it is “determined to build business relationships with its business partners and their employees based on the highest ethical principles of trust, teamwork, honesty, and respect for the rights and dignity of others.”

They require business partners and their employees to endorse a set of ethical standards compatible with their own. They encourage and favour those suppliers and vendors who fully conform to standards of business practices that are consistent with the HBC principles. They are committed to engage only those business partners who demonstrate a commitment to contribute to the improvement of community working conditions and strive to meet the requirements stated in the CVC.

In many respects, the CVC goes beyond the basic requirements mandated by the ILO and the UN. HBC seeks to go further with rigorous verification and mandated remedial activities and re-verification of a list of requirements that Canadians in general support within the supply chain. (See **Appendix 1**).

⁵ Website: http://www.unglobalcompact.org/Issues/supply_chain_management/index.html.

⁶ Website: <http://www.ilo.org/public/english/standards/norm/index.htm>.

⁷ Vendor Code of Conduct. Website: <http://www.HBC.com>.

HBC's Vendor Prioritization and Conduct Verification Policies

HBC realizes that there are limits to its ability to affect the local policies and practices of its vendors. As mentioned before, HBC is a relatively small global player, and Canada is a relatively small economy and therefore may not have as much “pull” in terms of demanding changes in local practices as other, much larger global players. At the same time, HBC has hundreds of suppliers from all around the world including more than 580 suppliers in the Asia Pacific region as shown in **Table 1**.⁸ For this reason, HBC characterizes vendors in terms of degree of trading activity undertaken with them. It then establishes a prioritization sequence for frequency of verification, in terms of doing further business with those vendors and verifying compliance with codes of conduct.

The idea behind the prioritization is that, if one company deals regularly with a vendor, the company is more likely be able to demand and make an impact on the CSR practices used from the regular vendor than with a vendor which deals with the company once a year for a small order. The categories of vendors based on yearly volumes and the nature of the vendor relationship is as follows:

- Priority A vendors are those given high priority: top 200 `suppliers based on volume of sales, perceived risk and factory location
- Priority B vendors are new suppliers without an established track record, and all new vendors are carefully evaluated on social compliance criteria
- Priority C vendors are all existing suppliers that are not new or among the top 200 suppliers within a supply chain.

HBC then conducts its verification program, according to these established priorities. For example, in 2004, HBC conducted verification among 369 vendors and 491 factories throughout its supply chain. For 2005, this number had grown to 455 vendors and 634 factories, as shown in **Table 2**.⁹

Table 1:
Number of Factories by Region

REGION	
Asia	586
Central America	1
Europe	4
Middle East	7
North America	36
Total	634

Table 2:
Audits Completed by Vendor Priority*

	2004		2005	
	Vendors	Factories	Vendors	Factories
Priority A	114	199	100*	330
Priority B	168	187	207	241
Priority C	87	105	148	63
Total	369	491	455	634

As part of its verification process, HBC uses a three strike policy, meaning that a particular vendor or factory is given a number of chances to fix deficiencies, or otherwise improve on those areas that are not currently in compliance with the CVC. The purpose of the policy is to build a strong business relationship with key suppliers, as well as with factories that want to keep the HBC business. This includes being willing to fully disclose factory locations, pay for their audit, and actively participate in the compliance program. If a supplier breaches any of the above conditions more than three times in a fiscal year, the supplier may be suspended or may be barred from doing further business with HBC for a minimum of two years. In 2005 for example, 42

⁸ “Taking Care of Our Home,” *2005 HBC Social Responsibility Report*: 39. Website: <http://www.HBC.com>.

⁹ Ibid.

* When the purchase order list from vendors for 2005 was finalized at the end of the year, only 100 of the top vendors were audited because of a lag in determining how many total orders each vendor fulfilled. Going forward, we will ensure that the top 200 vendors from the previous years are audited. “Taking Care of Our Home” *2005 HBC Social Responsibility Report*: 39. Website: <http://www.HBC.com>.

factories received one strike and five factories received two strikes as part of the verification process.

Similarly, new factories are audited for compliance with this policy and are either approved or not approved based on the results of compliance audits. This policy ensures that suppliers being added to the supply chain are in full compliance with the CSR policies of HBC, and verifies that existing suppliers continue to adhere to the policies. Repeat offenders are subject to more frequent audits, and in the case of continued non-compliance, are eventually removed from the approved suppliers list. The following table presents the results of the vendor compliance and monitoring program from 2003 to 2005.

Table 3:
Results of Vendor Compliance and Monitoring Program Results: 2003-2005

Factories	2003	2004	2005
Approved	395 or 90%	474 or 07%	605 or 95%
Not Approved	46 or 10%	17 or 3%	29 or 5%

Source: 2005 HBC Social Responsibility Report entitled "Taking Care of Our Home." 39
Website: <http://www.HBC.com>.

The audit procedure is very comprehensive. The factory audits are performed by two independent firms so that buyers and local partners would not know in advance the timing of the audit, or affect the outcome of the audit. Audits are conducted over one or two days and consist of:

- an interview with the factory manager about any special conditions at the factory
- interviews with selected factory employees about their treatment
- a tour of the facility
- a complete review of employee documentation, such as wage and payroll reports, time cards, contract, personal files
- a closing meeting with the factory manager to review the findings and where applicable, develop a corrective action plan.

The audit reports are sent back to HBC and reviewed by the social compliance team, who assigns the final grade and reviews the findings with the particular suppliers. There is a three-level grading system. The audit grade received is associated with the audit schedule, and has a direct impact on the factory's production schedule with HBC.

As shown in **Table 4**, factories that are rated "subject to improvement", or "zero tolerance", are subject to a written corrective action plan and reviewed actively by the HBC purchasing group to determine, if and when, orders can be placed. HBC usually works with individual factories to determine the timeframe and degree of correction that is required. Because of the diversity of economies it deals with, corrective action plans tend to be unique to each circumstance, and usually depend on the nature of the action required and the reputation and track record of the factory or supplier involved. HBC negotiates with each factory and seeks a steady progress towards full compliance – which is typically rewarded with additional orders. Failure to show progress results in termination, or being prevented from receiving additional orders until the concerns have been addressed and re-audited.

**Table 4:
Audit Reports Review System and Schedule**

Audit Grades	Re-Audit Schedule	Production Schedule
Approved for Production	Facility will be re-audited in 1-2 years	Factory may proceed with production
Subject to improvement	Facility will be issued a CAP and re-audited within 6 months	Production may continue, but there may be delay or cancellation due to results of re-audit
Zero Tolerance	Facility will be issued a CAP and re-audited within 2 months	Production will be postponed or not accepted

Source: Please see page 38 of the 2005 HBC Social Responsibility Report entitled "Taking Care of Our Home." Website: <http://www.HBC.com>.

In its Social Responsibility report for 2005, HBC noted many positive changes in factories that have been subjected to its compliance audits. However, the report admitted that long-term solutions have been slow in coming and a real challenge. HBC also suggested that purchase order size is the most significant obstacle in addressing factory labor standards. This is because factories receiving HBC orders representing only a small fraction of its factory output, tend not to have sufficient motivation to change practices, even when CSR is seen to be an important issue. HBC cannot act alone to improve CSR practices within the supply chain but must increasingly do so in concert with other larger retailers, local NGOs and government who need to support its efforts and require similar CSR compliant practices at the local level.

For this reason, HBC reports that in 2005, the social compliance team participated in meetings and joint audit initiative with local groups in the Asia Pacific region, such as the Asia Monitor Resource Center, the Hong Kong Christian Industrial Committee, and local university researchers from the East China University, to discuss regional challenges and social compliance and human rights issues. In Canada, HBC met with the Maquila Solidarity Network, religious groups and Play Fair at the Olympics to discuss its CSR program and policies. These discussions have led to a greater collaboration and understanding of the issues facing Canadian retailers in their social compliance efforts.

HBC also reports that facing challenges to its ability to encourage social change at a faster pace and collaboration with local NGOs would be helpful in implementing more effective mediation programs that might substantially improve CSR practices within the supply chain at the local level.

General Issues Related to Ethical Sourcing of Clothing and Apparel

For years, Canadians and Canadian retailers and wholesalers have worried about the impact of supply chain globalization on their own social responsibility, and by association, on the business practices of their suppliers from developing economies. Most Canadian products that are sourced outside of Canada tend to be related to clothing and apparel. For this reason, this section of the paper examines the CSR issues that Canadians care about within the supply chain for clothing and apparel.

Generally, Canadians support the goals of a number of global trading initiatives such as those of the *United Nations Global Compact* and the *International Labour Standards*¹⁰. Canadians refer to CSR issues within the supply chain using the term "ethical trading." Ethical trading initiatives

¹⁰ Website: <http://www.ilo.org/public/english/standards/norm/index.htm>.

seek to ensure that sourcing and business trading partners of corporations active in Canada meet the needs and expectations of Canadians in terms of social responsibility, not only in Canada, but also around the world.

Reflecting on the importance of the issue for Canadian retailers, the Retail Council of Canada suggests an implementation plan for Responsible Trading Guidelines (**Box 1**) which states that:

1. The Responsible Trading Guidelines (RTG) shall form part of any agreement the retailer enters into with its suppliers.
2. The retailer shall evaluate its suppliers by assessing their observance of the RTG.
3. The retailer shall assign responsibility for the implementation of the RTG to a responsible member of management.
4. Employees to whom the RTG applies shall be informed of it through the posting of the code in a prominent place in the local languages spoken by the employees and managers.
5. Employees to whom the RTG applies shall be provided with a confidential means of reporting violations of the RTG to the retailer and shall not be disciplined, dismissed or discriminated against for providing information about the observance of the guidelines.

Box 1:

The Responsible Trading Guidelines, Retail Council of Canada

- **Laws and Workplace Regulations:** The laws and regulations of the countries where goods are made shall be complied with.
- **Forced Labour:** Forced labour shall not be used, whether in the form of prison labour, indentured labour, and bonded labour, or otherwise.
- **Child Labour:** No person shall be employed under the age of 14, under the age interfering with compulsory schooling, or under the minimum age established by law, whichever is greater.
- **Harassment or Abuse:** Corporal punishment and other forms of coercion, abuse or harassment, whether psychological, sexual or physical, shall be prohibited.
- **Discrimination:** Discrimination in hiring or any other terms or conditions of work, other than *bona fide* occupational requirements allowed by law, based on race, colour, national origin, religion, disability, gender, sexual orientation, marital status, or political opinion, shall be prohibited.
- **Freedom of Association:** Employees shall be permitted to exercise lawful rights of free association.
- **Hours of Work:** The laws on working hours of the countries where goods are made shall be complied with and employees shall be entitled to at least one day off in every seven-day period, except as required to meet urgent business needs.
- **Health and Safety:** Conditions in all work and residential facilities shall be safe, clean, and consistent with all applicable laws and regulations regarding safety and health.
- **Wages and Benefits:** Employees shall be paid the higher of the minimum wage required by the laws of the countries where goods are made or the prevailing local industry wage and shall be entitled to all legally mandated benefits. Deductions from wages, not provided for by the laws of the countries where goods are made, shall not be permitted without the express permission of the employee.

The RTG itself was spearheaded by the Retail Council of Canada to assist its members in defining a consistent approach for the Canadian retail sector in the Canadian economy. The Retail Council of Canada is serious about CSR and the supply chain and devotes a portion of its web site to the issue.¹¹

¹¹ Responsible Trading Guidelines. Website: <http://www.retailcouncil.org>. See Appendix 2 for information on apparel related fair labor practice references.

CSR within the supply chain is actively discussed in the Canadian media. The issue came to the forefront in February 2001, when the Ethical Trading Action Group (ETAG) launched a disclosure campaign proposing that the government amend Regulations of the *Textile Labelling Act in Canada* to require disclosure of the addresses of manufacturing sites on labels of apparel sold in Canada. Unlike other disclosure proposals which limited their scope to domestic supply chains, ETAG wanted to find out about manufacturing locations worldwide, not just those in Canada. In making this request, ETAG members—a broad coalition including religious groups, labour groups, non-government organizations (NGOs), and other socially minded agencies, sought to facilitate verification of the labour standards employed at manufacturing sites around the world, particularly for clothing, shoes and other such apparel sold in the Canadian economy.

The ensuing Canadian media coverage made it clear that ensuring effective CSR within the supply chain is a major challenge for many Canadian retailers. The CSR efforts of Canadian retailers in themselves, provide no absolute guarantees that there are socially responsible practices within the supply chain. That is because large retailers, such as the Hudson's Bay Company, source products from thousands of locations and hundreds of manufacturers every year. For example, HBC sources products from almost 1,000 vendors representing 3,000 to 5,000 factories in 16 economies. It is difficult to imagine how HBC can be fully aware of all of the labour issues that such a supply chain would create, day in and day out.

Similarly, experts in supply chain management have documented the path taken by individual pieces of apparel from manufacturers to retailers and final containers. They confirm that the Canadian economy tends to have complex supply chains encompassing tens of thousands of items manufactured in hundreds of locations around the world. A well known author on the subject of clothing supply chains, talks about following the supply chain for a particular sweater “spanning 5 countries and 29,000 miles, a path that he characterizes as the normal pattern...”¹² This complexity makes it very difficult for any retailer, even the largest, with all of the resources they can muster, to really know and control the practices used in thousands of such supply chain patterns for tens of thousands of apparel products. Yet, this is what Canadians expect.

Compliance with overall local production codes and labour standards is usually the way the apparel industry attempts to control supply chains. Most industries and many large firms establish, require and enforce codes of conduct and other procedures for manufacturing facilities within their supply chains, including those facilities located in offshore economies.

Small firms can have an even more difficult time. Because they are small and possess fewer resources, they generally manage their supply chains through agents, wholesalers and other middlemen. Small importers and retailers rely on the business and CSR practices of agents and middlemen for their apparel purchases and imports. This greatly complicates supply chain monitoring because such firms have to rely on the good faith and practices of others, often located in other economies and subjected to local laws and labour practices. The agents or middlemen usually represent several manufacturers, each with multiple locations. The ability to hide or transfer production between plants at a moment's notice (what is called trans-shipment), makes verification particularly problematic and increases the difficulties of policing based on agreed standards and practices.

Small retailers find it very difficult to determine where their supplies come from. At the same time, they often lack the time and resources needed to verify the performance of every agent and importer they use to access suppliers. In some cases, these firms may be unwittingly using agents and middlemen willing to use operations that are actually sweatshops.

¹² Birnbaums Global Guide to Winning the Great Garment War (Paperback): 13.

The Global Apparel Market, and the Use of Agents and Middlemen

Since the turn of the century, the world has witnessed rapidly improving and socially responsible working conditions in the apparel industry. However, socially responsible working conditions have not improved as rapidly in all economies. For example, the lower levels of development and the widespread poverty that exist in many economies contribute to conditions under which poor labour standards can exist.

Many economies lack the capacity to effectively enforce labour laws that are otherwise acceptable to most trading partners. For example, one needs a structural ability to enforce standards in general before trying to address labour standards. Policies may instead stress the importance of gainful employment for the population and not working conditions. In many of these economies, a key question is whether there exists a sufficient capacity to address the complex issues that, in many ways, help support poor CSR practices. Purchasers of apparel in some economies also contribute to poor practices when they are willing to turn a blind eye to substandard practices in order to source cheaper product. Such practices taint the industry and support behaviours and practices that many Canadians find offensive.

It is also possible that unscrupulous manufacturers will willingly send their goods to other economies, through middlemen, to circumvent quotas, as well as to disguise the fact that one or more of their garments are made under questionable conditions. Hence, some may simply find it safer to produce apparel without regard to labour standards and to rely on subterfuge to sell the products in Canada than to produce the apparel in a more costly, albeit more ethical, means.

The global apparel industry is a highly competitive environment with hundred of thousands of suppliers and tens of thousands of retailers. These conditions can be extremely challenging for many economies and suppliers, and may actually create pressures to employ the kind of substandard labour standards that Canadians are concerned about. This is an operating reality that will not be solved by Canadians alone. As long as economies are willing to condone unfair labour practices in the name of industrial development, Canadians and their apparel manufacturers will simply have to be vigilant and avoid situations that they find unacceptable.

With so many suppliers chasing so relatively few purchasers, and with competitiveness dependent on providing the highest quality at the lowest possible cost, there is never a shortage of producers willing to make garments for less. Low prices do have their limits however, and the overall production costs, including macro costs and indirect costs, such as the cost of appropriate labour standards and CSR, need to be factored into pricing and purchasing decisions. Market conditions in some economies may not always support effective CSR, and charging an insufficiently high price almost guarantees that working conditions remain substandard, that is, manufacturers do not have sufficient resources to improve working conditions and guarantee effective CSR within the supply chain.

Moreover, the supply chain is subject to seasonal variations and has perhaps as many permutations as there are types of apparel. This is particularly true in Canada where winter apparel is substantially different and may have to be sourced differently from summer apparel. There are also long lead times for such apparel, with orders typically needing to be finalized six or seven months ahead of the selling season. This means that winter apparel needs to be ordered in mid-summer in order to arrive on the shelves ahead of the winter season.

One can only imagine the variety and number of permutations of the supply chains used by individual retailers and manufacturers. Under conditions of quota changes, seasonal changes, the number of types of apparel, the use of intermediaries or avoidance of their use, direct sourcing or

avoidance of direct sourcing, rules of origin, etc., it is no wonder that CSR within the supply chain becomes a challenge for many economies.

The Role of Apparel-Exporting Economies

Around the world, several organizations and programs have been working to improve working conditions. Indeed, there are prominent examples of organizations and programs dedicated to the implementation of socially responsible standards in the apparel industry (See **Appendix 3**).

Many large retailers require minimum production standards, including labour standards within the supply chain equation. This requires a number of trips to the manufacturing location and a number of test verifications to make sure an effective relationship is set up based on all of the aspects of supply chain management, including quality, price and CSR. The existence of effective legislations and regulations governing CSR in the exporting economy is an important enabler of CSR within that economy.

This is really a question of host economy government policy and administrative capacity, and the degree of government involvement in the issue of CSR in the supply chain. Should the governments of importing economies focus on policies in exporting economies in terms of government accountability, competitive behaviour, trade initiatives, accurate information and verification of CSR in the supply chain?

Socio-political issues in the host economy are often at the center of the issue of labour standards in the apparel industry. They relate to the human impact of the use and promotion of CSR, from the social responsibility factors in Canada that are driving our desire to do something about the issue, to factors in the economies that produce apparel. The socio-political dimension is a relatively important aspect and encompasses a number of very contentious questions:

- **Should CSR in the supply chains consider impacts on local workforce when the economy or operations become stigmatized because of the existence of sweatshop conditions, and the fact that those conditions may or may not be improved considering the existing economic conditions or level of development?**

Employees losing their jobs (or not having a job in the first place) because their local host economy employer is not willing or able to adhere to labour practices and standards acceptable to Canadians is really a difficult issue for a socially minded Canadian retailer. Issues such as foreign aid, local labour standards and the need to better educate the workforce are raised to explain that it is not really the job of an importing economy's retailers to solve the domestic need for socially responsible policies and procedures within the host economy.

Yet, many retailers care about the conditions that result when a Canadian manufacturer or retailer stops dealing with a particular location. They care about the relationships they have built up over time and the expense of having to set up new relationships. This level of caring explains why manufacturing locations found not to be in compliance with guidelines and codes of conducts are often given several chances to improve and to meet the standards. However, if that location is not able to provide the required elements of price, quality and on time delivery, it cannot be relied upon by Canadians, who expect these things when they buy apparel from Canadian retailers.

Some Canadians believe on moral grounds that we have to support employees in developing economies, even when the particular manufacturing locations fail to meet our standards. Such stakeholders believe we must "work with them" to improve standards. Even if you believe this to be true, questions such as *How* and *How long* should you be willing to work at it is a very

contentious issue in Canada. The same stakeholders often blame retailers in the media when examples of poor practice are uncovered.

- **Is it the responsibility of the importing economy's government to impose conditions on an offshore economy in exchange for market access, or is self determination an absolutely overarching principle?**

Many Canadians argue that as a socially responsible economy, we need to exert political pressure on all governments to adopt the types of minimum standards that Canadians view as “right” and as “fair.” This would include ensuring CSR within the supply chain. Yet, it is only when we speak about our own domestic practices that we really have complete control of this issue. Governments in other economies can, and have in the past chosen their own paths for improvements. Our only choice is to “not deal” with those who fundamentally refuse to believe in what we think is right. This is a double-edged sword. Is it ever feasible or even desirable to try and impose the use of Canadian standards on other jurisdictions?

Most Canadians believe that social responsibility involves at least adhering to local government standards, on the assumption that those standards are deemed to be globally acceptable, and not too far removed from our own expectations. This is usually a valid assumption within the APEC region.

- **Is there a reputation and/or image benefit to particular economy/manufacturers/suppliers in undertaking labour standards reviews and reforms?**

Many Canadians believe that there are a few issues, such as the wish to eradicate slave and child labour, on which there is broad consensus, and which has a significant impact on the reputation of the particular economy or supplier. Strong stakeholder pressure from consumer groups and the global economy are focused on relatively high-profile issues, such as child labour, rather than on the broader standards mandated by the ILO. Some will argue that there are degrees of CSR within the supply chain that affect the reputation of the host economy.

Yet, it is the full and complete adherence to ILO standards that is broadly thought to represent the desired direction for fair labour standards in the apparel industry. Canadian industry stakeholders are already doing their part to address the issue by means of their codes of conducts and the efforts they make at enforcing them. Canadian retailers report that they avoid certain economies, because they appear to be unwilling to support the types of operations and CSR to which Canadian companies have committed. Other economies are preferred because they are developing or have established very rigorous processes that support their CSR activity. As a result, it is an important aspect of the policy development of each economy to focus on mechanisms and policies that are useful and supportive of the CSR and the supply chain

Socially minded companies gravitate to socially responsible codes and work diligently to abide by them. Industry minded social groups support socially responsible codes even if they do not immediately achieve all of their goals. Governments conscious of their reputation balance the needs for action on CSR against the undesirable impacts of increased regulation and standard requirements on the economy.

It is therefore the emergence of codes of conduct and the willingness of suppliers to adhere to them which is seen as the most important indicator of effective CSR, and the driver of a CSR-minded reputation. It is difficult to force a recalcitrant supply chain stakeholder (industry, government, or supplier) into doing what is right in every case. The voluntary codes work best because they are voluntary.

Conclusions

It is clear from the above discussions that one cannot easily enforce socio-political aspects of a policy that runs counter to the desire or capacity of the local market participants and the local community to address the issue of CSR in the supply chain – even when it runs counter to those of the global community. We are therefore dependent on the proper understanding of the issues surrounding CSR and the supply-chain within each economy, and on the willingness of government and industry participants to voluntarily work towards complete adherence to widely accepted standards. This is why APEC initiatives such as the ones that led to this report are very important.

The best way to ensure CSR within the supply chain is to have consistent and concerted effort by all economies, all suppliers and all purchasers to practice effective CSR within the supply chain. This will tend to reward those suppliers using effective and generally accepted practices, and not those suppliers that repeatedly refuse to improve practices to a more satisfactory level.

At the turn-of-the-century, many developed nations struggled to ensure effective CSR in their domestic supply chain. With concerted effort and a combination of information, legislations and regulations that are enforced, those economies were able to largely eradicate poor CSR practices. This served to greatly improve the working conditions in their respective economies. With the advent of globalization and freer trade, the issue of CSR within the supply chain arose again as it revealed trading partners who did not, or could not afford to follow globally approved methodologies and practices to ensure CSR within the supply chain.

Canada continues to support CSR efforts within the Canadian government, industry associations and individual participants working together to define standards that are seen as minimum, and verify the existence of those minimum standards within the operations. In most cases, organizations use codes of conduct, with independent verification. Codes of conduct are seen by many as an effective way to inform consumers of the efforts being made to ensure fair labour standards in various industries, most notably apparel. Because they outline in relative detail the agreed upon standards that signatories will follow, they allow for more transparent verification and reporting.

However, because they are quite new, there are concerns that over time stakeholders will begin to criticize them as not stringent enough. Other stakeholders complain that the codes are not being managed closely enough by the industry and that verification may not always be effective. While it is true that we may never be able to satisfy all stakeholders with any initiative, a multitude of criticisms of this type tends to reduce the perceived value of a code. This has led to a proliferation of codes and a resulting dilution of the number of apparel industry participants that subscribe to any one code. This may eventually lead to confusion, as consumers compare and contrast the various codes governing the production of the apparel they want.

We can jointly contribute to a solution by continuing to work together, enacting laws domestically and implementing and enforcing codes internationally that will ensure that those employing unfair CSR practices are penalized while those employing fair practices are rewarded. We can also encourage others to do so and contribute to international initiatives in meaningful and effective ways. In the end, all of the parties concerned need to confront and correct questionable business practices. Only then will the benefit be felt by those who need it most.

Appendix 1 Code of Vendor Requirements

- **Legal Expectations:** All business partners and their employees must comply with all contract provisions, legal requirements and standards of their industry under local, regional and national laws and regulations of the countries in which the business partners are doing business. Should the legal requirements and the standards of the industry conflict, business partners and their employees must comply with the higher standard in the country in which the products are manufactured. Nothing in this Code is to be construed as encouraging, authorizing or condoning any action by any company or individual that breaches any applicable law or regulation, directly or otherwise. By extension, the provisions of this Code are not to be read as creating or implying meanings beyond those specifically explained in this document.
- **No Forced Labour:** Business Partners must maintain employment on a voluntary basis respecting the right of employees to decide to work or not. Business Partners shall not use forced labour, whether in the form of prison labour, indentured labour, bonded labour or otherwise in the manufacture or in their contracting, subcontracting or other relationships for the manufacture of their products.
- **No Child Labour:** The use of child labour is not permissible. Workers can be no less than age 15 (or 14 where the law of the country of manufacture allows), or the age at which compulsory schooling has ended, whichever is greater. In situations involving hazardous working conditions, we require that workers are at least 18 years of age. HBC supports the development of legitimate workplace apprenticeship programs for the educational benefit of younger people as long as they are not being exploited or given jobs that are dangerous to the child's health or safety. No child or younger person of compulsory school age should be employed during school hours and the combined time spent on school, transportation, and at work cannot exceed 10 hours a day.
- **No Harassment or Abuse:** HBC requires that every employee shall be treated with respect and dignity. No employee shall be subject to any physical, sexual, psychological or verbal harassment or abuse including the use of corporal punishment.
- **Freedom of Association and Collective Bargaining:** Management practices must respect the right of employees to free association and collective bargaining where applicable.
- **No Discrimination:** HBC recognizes and respects the cultural differences found in the world. They favour Business Partners who ensure that no employee shall be subject to any discrimination in employment, including hiring, salary, benefits, advancement, discipline, termination or retirement, on the basis of gender, race, religion, age (other than normal hiring or retirement limitations), disability, sexual orientation, nationality, political opinion, union participation, social or ethnic origin or membership in any legal organization. Employment decisions will be made on the basis of knowledge, skill, efficiency and ability to do the job and meet its requirements.
- **Health and Safety:** HBC will only utilize Business Partners who provide safe and healthy work environments for their employees. Factories producing HBC merchandise shall provide adequate first aid supplies, fire exits and safety equipment, well-lit workstations, clean restrooms and ensure that all are well maintained and in good working order. Worker housing, where provided by the Business Partner, must meet a reasonable standard of health and safety.
- **Wages and Benefits:** HBC will seek Business Partners who share our commitment to the betterment of wage and benefit levels that address the basic needs of workers and their families so far as possible and appropriate in light of national economic conditions. Business Partners are required to pay the higher of, the prevailing industry wage, the minimum wage, or a wage that results in a decent living. Business partners shall provide all legally mandated benefits.
- **Hours of Work/Overtime:** Business Partners shall maintain reasonable employee work hours in compliance with local standards and applicable national laws of the countries in which Business Partners are doing business. In the absence of exceptional circumstances, HBC will favour Business Partners who utilize less than a sixty-hour work-week and not those who, on a regularly scheduled basis, require employees to work in excess of a sixty-hour work-week. Where this is not established at a lower level by local laws, HBC defines a standard work week to be not more than 48 hours and considers all hours in excess of this amount to be overtime, whether mandatory or not. Business

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Partners are required to compensate employees for overtime hours including such premium rates as are legally required in the country of manufacture, or in those countries where such laws do not exist, at a rate at least equal to their regular hourly compensation rate. Unless exceptional circumstances exist, employees should be permitted at least one day off in every seven-day period, and leave privileges.

- **Resolution of Disputes:** Business Partners should incorporate a dispute resolution process as part of their management practices to allow employees to voice workplace grievances without the fear of reprisal.
- **Environmental Requirements:** HBC will favour Business Partners who conduct their business using progressive environmental practices and take active steps to preserve and protect the well-being of the environment. All Business Partners must adhere to all applicable environmental laws and regulations regarding protection and preservation of the environment in their country.
- **Transshipment:** Vendors will comply with applicable customs importing laws, and in particular, will establish and maintain programs and documentation to support country-of-origin production verification, to prevent illegal trans shipping of merchandise.

Source: Website: <http://www.HBC.com/HBC/socialresponsibility/sourcing/conduct>.

Appendix 2

Apparel-related Fair Labour Standard Resources Print and Web References

Print References

Birnbaum, David, *Birnbaum's Global Guide to Winning the Great Garment War* (Hong Kong: Third Horizon Press, 2000).

Web References

Business for Social Responsibility (BSR)

(Website: <http://www.bsr.org>)

Retail Council of Canada's Responsible Trading Guidelines

This site provides a wide range of information, including responsible trading guidelines in its archive section. (Website: <http://www.retailcouncil.org>)

Canadian Apparel Federation

This site provides labour-related information. (Website: <http://www.apparel.ca>)

Supporting European Initiatives on Monitoring and Verification of Codes of Conduct in the Garment and Sportswear Industries (SOMO)

The resource list contains documents on multi-stakeholder initiatives concerning this project as well as audit reports, discussion papers, and reports on labour standards. For a look at national initiatives, use (www.somo.nl/monitoring/project/fo-character.htm). For a look at the SOMO resource list, use (Website: <http://www.somo.nl/monitoring/resource.htm#sw>).

The Workers' Rights Consortium (WRC)

The WRC is a non-profit organization created by college and university students, administrators, and independent labor rights experts to help enforce manufacturing codes of conduct adopted by colleges and universities. (Website: <http://www.workersrights.org>)

The Fair Labor Association (FLA)

The FLA is a non-profit organization combining the efforts of industry, non-government organizations (NGOs), colleges, and universities to promote adherence to international labor standards and improve working conditions worldwide. (Website: <http://www.fairlabor.org>)

Clean Clothes Campaign (CCC)

The CCC is a coalition of trade unions and NGOs, including development, consumers, solidarity, and fair trade organizations. It is active in 11 European economies and embraces nearly 300 organizations. (Website: <http://www.cleanclothes.org/campaign.htm>)

Social Accountability International (SAI)

SAI describes itself as working "to improve workplaces and combat sweatshops through the expansion and further development of the international workplace standard SA8000 and the associated S8000 verification system." (Website: <http://www.sa-intl.org>)

TransFair Canada

Transfair describes itself as "Canada's only independent certification organization for fair trade in coffee, tea, cocoa, and sugar. (Website: <http://www.transfair.ca>)

Appendix 3 Selected Initiatives that Focus on CSR and the Supply Chain

Clean Clothes Campaign's Code of Labour Practices. This European-based Code of Labour Practices sets forth minimum standards for wages, working time, and working conditions and provides for observance of all of the core standards of the ILO, including Conventions 29, 87, 98, 100, 105, 111 and 138. They are minimum standards meant to apply throughout the industry and in all economies. The code is not a trade protectionist measure. It is not meant to be used as a means to close the markets of some economies at the expense of workers in other economies.

Ethical Trading Initiative (United Kingdom). The Ethical Trading Initiative (ETI) brings together companies, unions, and NGOs to identify and promote good practices in the implementation of codes of conduct, including monitoring and independent verification. Companies such as Anchor Seafoods, Body Shop, Chiquita, Levis, NEXT, Marks and Spencer, Safeway stores, Brooke Bond Tea, Tetley Tea, and Twinings are members. The ETI has developed a multi-sectoral Base Code based on ILO standards. It includes provisions for a living wage, freedom of association, and security of employment. ETI members are currently participating in four pilot projects, testing various models of code verification. Details of the initiative can be found at www.ethicaltrade.org.

Fair Wear Foundation (Netherlands). The Clean Clothes Campaign (CCC) was successful in bringing together Dutch NGOs, labour centrals, and associations of apparel retailers and manufacturers in a five-year process of negotiations for an industry-wide code of conduct that has provisions for independent monitoring and certification. This became the Fair Wear Foundation. Unions, NGOs, retailers, and manufacturers are represented on a Fair Wear Foundation committee that will hire external monitors, evaluate their reports, and certify apparel companies and their supplier factories. This is an example of a type of verification arrangement. In the Netherlands, agreement has been reached on a voluntary code that includes strong provisions on freedom of association, hours of work, and a living wage. The Fair Wear Foundation will ensure that the codes are being applied fairly and will certify compliance. More information about the Fair Weather Foundation can be found on the organization's web site at <http://www.fairwear.org>.

FairTrade Labelling Organization. The FairTrade Labelling Organization (FLO) is a non-profit, membership-based association of National Initiatives (17 members worldwide) which promote fair trade labelling in their national markets. They do this by lobbying governments for support; negotiating with importers and retailers; and running education programs with the aim of supporting marginalized producers on the road to sustainable development.

The label identifies FairTrade products so that consumers will buy them, giving FairTrade producers access to international markets on fair terms. FairTrade products do not currently include apparel, but the concepts used in FairTrade could be adapted to apply to it. Information about the FairTrade initiative can be found at website: <http://www.fairtrade.net>.

FLO is the only certification system in the world where producers do not pay for their certification. The consumer pays for the FairTrade system. Traders pass on to consumers the higher FairTrade price and the premium that is paid to producers for FairTrade products. The National Initiative in the economy where the products are sold charges the licensee a fee for using the FairTrade label. This pays for all of FLO's certification and monitoring costs and for the National Initiatives marketing expenses. Including the cost of the system in the retail price makes FairTrade labelling sustainable.

CSR in Chilean Fresh Fruit Supply Chain

Chile

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Executive Summary

In an emerging economy such as Chile, fruit exports play an important role in economic development. However, the working conditions of small fruit producers and exporters are now largely determined by their buyers and ultimately by the end customers, mainly those in northern economies, who have in the past few years demanded more sustainably sourced products for consumption. Thus, in order to secure a piece of these lucrative developed economy markets, Chilean fruit producers and exporters have found it necessary to “green up” as part of the supply chain of larger retailers.

This case focuses on the achievements of a capacity-building program called ChileGAP (Good Agriculture Practices). ChileGap aims to strengthen the social and environmental performance of agricultural practices in Chile in order to satisfy the social and environmental requirements of buyers. Such fundamental change of business mindset does not take place quickly or easily. Challenges and problems have had to be faced and overcome with the assistance of public and private initiatives.

Introduction

The onset and rise of Corporate Social Responsibility (CSR) has left few economies or business sectors untouched. Indeed, CSR has been widely credited for helping generate sustainable development or what is also known as the “win-win” situation, where all parties or stakeholders benefit. It is thus apparent that CSR has a huge appeal to business, governments and society as a whole.

Indeed Chile, the subject of this case, has not been exempt from this new concept of doing business. With the growth and development of CSR in more developed economies in the northern hemisphere, partly in response to the new ethical demands of the so called “green” and “social” consumers, it would be good business sense for a natural resource export oriented economy such as Chile to get in on the act and produce its exports in a more socially responsible manner.

This case focuses specifically on one such export sector, Chilean fresh fruit production, which has adopted a proactive stance towards CSR. This involved implementing an integrated CSR business strategy to make exports more competitive, while at the same time contributing to sustainable development. However, despite the proactive actions they have taken, Chilean fruit producers, to a certain extent, have also been driven to green their production and become more socially responsible by the demands imposed by consumers in the prosperous and socially conscientious economies of the northern hemisphere. Indeed, it is the economies in Europe, North America and Japan that have increasingly demanded higher standards. Their insistence that commodities be ethically produced has had a knock-on effect on exporting economies such as Chile.

The groundbreaking dimension of the case relates to the integration of CSR elements into the business practices of the enterprises. Aside from being a concept that is most relevant to developed economies, CSR has also been mainly relevant to multinational enterprises and other large companies. In fact, one of the main criticisms levelled by academics and non-governmental organizations (NGOs), is the SMEs lack of awareness or commitment to CSR. Considering that SMEs account for the vast majority of companies and the largest source of employment in Chile and in the rest of the world, the failure to include SMEs as part of this new sustainable business practice would come in the way of achieving the CSR goal of providing benefits on a large scale.

A multi-stakeholder initiative to integrate CSR practices into Chilean SMEs in the fruit sector not only resulted in more socially responsible business practices but also gave the SMEs a

competitive business advantage. This transformation began with a voluntary social and environmental initiative undertaken by the Chilean fruit sector.

In Chile, SMEs in the fresh fruit sector have been driven towards corporate responsibility as a result of both societal and international market expectations. Producers are conscious that to remain competitive and be able to integrate themselves into the major global supply chains, they need to adopt higher standards of corporate responsibility. In some cases, supplying large supermarkets can only be done by producing fruit in a socially responsible manner and having these practices independently verified.

Given Chile's importance as an exporter of fresh fruit accounting for 48.5% of exports from the southern hemisphere, high standards of CSR are essential to the industry's development and competitiveness. The pressure coming from external markets, government, consumers and civil society is largely believed to have forced companies into increasing their standards. This has been accepted by the sector because of fear that failure to do so would put its reputation at risk.

For a greater number of SMEs seeking to enter international supply chains, social and environmental conditions are challenges which increasingly must be met in order to gain market access. However, while compliance is a competitive issue since suppliers can lose contracts through non-compliance, meeting social and environmental standards alone is not enough to win and retain customers. Some industries are, nevertheless, responding to this perceived constraint by establishing their own standards as a way of actively building a competitive advantage in terms of social and environmental standards, rather than continuing to see the matter as one of compliance for market access.

The favorable location and temperate climate conditions are natural advantages for the development of the fruit industry in Chile. But it is the public and private efforts which have made Chile one of the main exporters of fruit in the world.

The government of Chile has invested heavily in researching: a) the main potential international markets, b) their specific demands and c) sanitary standards required to access these markets. As a result of this investment from the government, and with the cooperation of private organizations a number of programs have been established specifically for this industry. Buenas Prácticas Agrícolas - BPA (Good Agricultural Practices - GAP) and in particular, ChileGAP are two of the programs that are working to find ways of enhancing sustainability in the fresh fruits supply chain.

Nevertheless, greening the production of fruit and also meeting large multi-national buyers' social requirements in terms of labour working conditions have, by no means, been a smooth or a rapid transition for the Chilean fruit sector. The typical business practices of Chilean SMEs over the past several decades could be considered as not fully socially responsible. Thus, efforts at changing mindsets and business practices came up against certain obstacles and significant challenges for the Chilean fruit sector SMEs. However, with the assistance of public and privately financed initiatives business leaders have been able to address these issues.

Good Agricultural Practices and the Chilean Association of Exporters (ASOEX)

The association has put in place a policy of going beyond market compliance as a means to improve the competence of producers. It developed the concept of ChileGAP early on, following the first established agreements made by EurepGAP.

ASOEX has established Chilean standards governing key social and environmental aspects of the production process of Chilean fruit. The standard, ChileGAP, provides both short and potential long-term advantages. In the short term, it can be more readily aligned to the particular characteristics of the Chilean fruit sector in contrast to the more generalized, global standards historically preferred, and largely controlled by international buyers in Europe and North America. Furthermore, certification through ChileGAP has proved to be cheaper to Chilean producers than alternative international certification processes. In the long term, ASOEX wishes to use ChileGAP to differentiate Chilean fruit in the highly competitive fruit export market. Thus the association participated in the creation of the ChileGAP certification and has continued working with the producers to build their competency so that they can be certified. There are more than 4000 fruit producers participating in programs on good agricultural practices in Chile, about 1500 are working with technical assistance from ASOEX.

Before the establishment of ChileGAP, the agricultural producers of Chile had to comply with the standards of the European market and of a number of supermarket chains in the United States. This made the export process more complex. The problem for the Chilean producers was that they did not know if their products would arrive in the United States or in Europe, and if they went to the United States which of the various possible buyers would receive them. To facilitate the export process, ASOEX started its Good Agricultural Practices program which is known today as ChileGAP. The European and North American markets certify that the ChileGAP's standards meet their own level of standards.

ChileGAP focuses on three specific aspects: environmental issues, hygiene and phytosanitary standards, and the safety of employees. The program has not only resulted in a greater number of products grown but it also provides a guarantee that consumers would receive high-quality goods. The ASOEX staff made sure that participating companies understood ChileGAP's standards. They visited producers and help them implement improvements in production, minimize the use of pesticides and improve the quality of life of employees.

In order to be certified by ChileGAP, producers have to prove that they abide by the three aspects of the GAP. Many independent international verification companies certify the Chilean producers.

There are some costs related to the implementation of sustainable practices for the company which include the staff employed to supervise the process and the continuation of the ChileGAP process. Although there are no short-term economic benefits resulting from this process, ASOEX hopes that participation in ChileGAP will increase the exports of Chilean goods to primary markets. Given the international acceptance of ChileGAP, the agricultural producers have a greater guarantee that they will be able to sell their products to more profitable markets.

At the same time, through a multi-stakeholder initiative, ASOEX has been working together with a Chilean corporate responsibility research, consulting and non-profit center known as Vincular, with financial support from the Inter-American Development Bank (IDB). The consortium is developing a project to adopt a CSR management system for SMEs in the fruit exporting sector. The project also involves two other productive sectors from the Chilean economy, the wine industry and the manufacturing industry. The CSR model developed in the project is based on an industry-wide vision, and is in accordance with the ISO 26000 process, GRI indicators for SMEs and other relevant international standards on social responsibility.

Chilean Fresh Fruit Production

The Chilean fruit sector has around 14,000 producers mainly located in the central valley zone and accounting for 64% of the economy's total fruit production. The fruit sector generates direct full time employment of around 128,000 workers and close to 300,000 temporary workers, and indirect employment such as that of transport.

In 2006, there were 7,000 registered fruit exporters from 4000 in 2004. However, only 19 companies with sales volumes of over 2.2 million boxes each accounted for around 55% of the fruit exports.

Chile exports a wide range of fruit products but the most important are table grapes, followed by green and red apples. Other fruits exported are kiwi fruit, plums, nectarines and peaches and other emerging produce such as avocado. The Chilean fruit sector takes advantage of its southern hemisphere location which makes it possible to supply the demand for these fruits during the times when they are out of season in the northern economies. The total exports grew from 224,062,000 boxes in 2004-2005 to 230,828,000 boxes in 2005-2006.

The main markets for Chilean fruit exports are shown in **Table 1**. The leading destinations based on volume exported are the USA and Canada representing 37.8% of the total exports, followed by Europe with 30.6%. Significantly smaller volumes are exported to Latin America, the Far East and the Middle East.

Table 1:
Volume (in tons) of Fresh Fruit Exports by Season, by Region

Products	USA Canada	Europe	Far East	Middle East	Latin America	Season 2005/06	Season 2004/05	Var. % 2006/2005
Grapes	469.974	195.114	73.537	6.280	64.836	809.741	754.292	7,4
Red Apples	78.566	176.107	60.676	74.110	201.953	591.412	503.741	17,4
Avocado	65.662	21.288	642	0	1.146	88.738	143.940	-38,4
Kiwi Fruit	24.883	91.667	14.049	2.360	13.294	146.253	133.933	9,2
Green Apples	13.980	69.983	3.831	10.367	26.272	124.433	132.548	-6,1
Pears	20.561	50.682	1.031	4.708	37.653	114.635	115.940	-1,1
Plums	29.319	24.314	11.932	1.430	12.944	79.939	97.379	-17,9
Peaches	32.062	3.368	162	0	13.105	48.697	57.763	-15,7
Nectarines	24.869	8.070	4.671	64	6.844	44.518	62.860	-29,2
Lemons	15.378	76	15.353	0	5	30.812	35.607	-13,5
Oranges	2.469	6.321	9.774	0	836	19.400	22.313	-13,1
Clementines*	14.484	7.760	740	157	693	23.834	21.443	-10,0
Cherries	11.229	3.885	5.109	32	2.191	22.446	13.907	61,4
Blueberries	12.031	2.613	389	0	32	15.065	11.336	32,9
Nuts	0	5.857	103	0	2.339	8.299	7.697	7,8
Asian Pears	4.873	349	138	16	1.169	6.545	7.857	-16,7
Raspberries	4.163	153	19	0	7	4.342	4.976	-12,7
Almonds	0	2.144	117	17	1.662	3.940	4.754	-17,1
Apricot	1.954	179	4	0	661	2.798	2.951	-5,2
Cherimoyas	310	1	10	0	10	331	361	-8,3
Others	2.809	2.006	739	31	1.001	6.586	8.186	-19,6
Season 2005/06	829.576	671.937	203.026	99.572	388.653	2.192.764		2,3
Season 2004/05	864.233	676.766	171.796	86.987	344.002		2.143.784	
Part. % 2005/06	37,8	30,6	9,3	4,5	17,7	100,0		
Var.% 2006/2005	-4,0	-0,7	18,2	14,5	13,0	2,3		

Source: ASOEX based on information from Chilean Agricultural and Farming Government Agency.

A market analysis shows that the USA is the main destination for Chilean fruit exports and that Holland receives the bulk of exports since it is the first point of entry and distribution in Europe. Despite the USA's current position as principal destination for fruit exports, the European Union has been gaining ground as an export destination mainly due to the recent strength of the euro and lower import taxes from the Free Trade Agreement (FTA) with Chile. The Latin American and Far East markets have also been targeted for expanding export sales.

It can be argued that the Chilean fruit exports industry has enjoyed a continued success which can be attributed to its effort to meet specific demands from the market. Hence the increasing global trend in consuming fruits that are ethically and responsibly produced and also taste better, has coincided with the GAP program and the Chilean government's Clean Production Agreements, that an increasing number of producers comply with. This highlights the advantage of going beyond the merely practical business considerations and arriving at a win-win situation, which satisfies both the enterprise's desire for profit and the demands of the market for social accountability. Socially responsible behavior has been led by ethical consumers in northern hemisphere economies, and these demands have had a direct impact on Chilean fruit production methods.

Despite the fundamental changes in business practice that has developed among Chilean fruit producers, some major challenges remain.

Social and Environmental Problems in Fruit Production

For the fruit producing sector, the main social problems are related to quality of work life and the environmental impacts.

Environmental Aspects

Various environmental authority reports and those by the Organization for Economic Cooperation and Development (OECD) and the United Nation's Economic Commission for Latin America and the Caribbean report, "An Evaluation of Environmental Performance – Chile," indicate that contamination of water from improper use of pesticides and fertilizers has been the main negative environmental impact of fruit production.

A secondary impact of agricultural production is the degradation of agricultural soil due to poor agricultural practices or ways of tilling the land. This often resulted in considerable soil erosion and made the soil infertile. Likewise, the use of salt water for irrigation and intensive production techniques has caused salination of the soil, which consequently makes it less productive.

Social Aspects

Work life quality, particularly that of temporary harvest workers, is by far the main social concern for the fruit sector. The main problems that arise are related to the existence of legal contracts and compliance with workers welfare benefits. They include lack of sub-contractor legal contracts, excessive work hours well over the legal maximum and the general lack of human resource infrastructure.

However, it should be pointed out that the export oriented fruit producers tend to perform better in these potential pitfalls since many of them already comply with GAP, which ensures that environmental and social standards are met in the workplace. Nevertheless, the social and environmental problems confronting fruit production highlight the need for a more responsible business model, especially because the sector's main export market in the north is raising the "ethical bar" for the purchase and consumption of primary sourced products.

Profile of ASOEX

The Association of Chilean Exporters A.G. (ASOEX initials in Spanish) is a trade organization founded in 1935 by a group of fresh fruit and vegetable exporters who shared a common goal to open up new markets and improve competitiveness for their partners.

The importance of ASOEX is shown by the fact that its 90 members account for 90% of the total Chilean fresh fruit exports and over 50% of total fresh fruit production. The signing of various free trade agreements has allowed Chilean fruits to be exported to new and previously unimaginable markets where these products are now renowned for their quality, safety and competitive prices.

One of ASOEX's main differentiation strategies is to place emphasis on its GAP program, the only such initiative in the world with a national focus. This program permits Chilean producers and exporters to comply with international norms and legislation on food safety, environmental protection and CSR via the verification of technical protocols developed by the ChileGAP program. ChileGAP has also been approved recently by EureGAP, the European body that manages the most advanced verification system of these concerns. As a result Chilean producers and exporters have gained more competitive edge by offering trustworthy products. The system likewise helps reduce industry wide certification costs, thereby placing all stakeholders in a win-win situation in terms of sustainability.

Good Agricultural Practices (GAP)

Towards the end of the 1990s after the mad cow disease epidemic and debates about genetically modified foods, public debate about food origin in Europe became more commonplace. The risks that this situation posed to Chile's exporters were among the main drivers in creating the concept of GAP.

Likewise, higher levels of public concern for social and environmental impacts of agriculture production along with the communication revolution of internet, electronic mail, mobile phones and digital cameras which can expose unethical offenders, have acted as strong drivers in the creation of GAP.

These factors sometimes known as "the triple bottom line - people, planet and profit" recognize the importance that major corporations and multinational supply bases place on mechanisms that would ensure responsible agricultural practices that respect food safety, the environment, workers welfare and the welfare of animals. Good Agricultural Practices, which are understood by producers the world over, deliver clearly defined outcomes in these areas (EurepGAP, 2007).

EurepGAP

One of the best known international initiatives based on Good Agricultural Practices is the EurepGAP. It began in 1997 as an initiative by retailers belonging to the Euro-Retailer Produce Working Group (EUREP). British retailers in conjunction with supermarkets in continental Europe were the driving forces for this initiative. They reacted to the growing concern of the

consumers with product safety, environmental and labour standards and decided to take more responsibility for what happened in the supply chain. Likewise, the development of common certification standards were also in the interest of many producers. Those with contractual relations with several retailers complained that they had to undergo multiple audits using different criteria every year. Given this, EUREP started to work on harmonized standards and procedures for the development of Good Agricultural Practices in conventional agriculture.

ChileGAP

The requirements imposed by international markets regarding compliance with certain standards for the application of Good Agricultural Practices resulted in a complex situation arising from the different points of view on GAP that have been established by the various markets. Hence, Chilean exporters and producers were confronted with levels of requirements which were inconsistent, even contradictory in certain cases. In many cases more than one certification must be obtained for the same property or packaging plant, resulting in an increase in costs for the producers.

Faced with this situation, in August 2003, the Chilean Exporters Association (ASOEX), with technical support from the Fruit Development Foundation (FDF), deemed as urgent and necessary the implementation in Chile of an overall program aimed at defining a uniform procedure for meeting all the requirements of the principal international purchasers of Chilean fruit.

This is the main reason for ChileGAP's conception, the implementation of which will enable the Chilean fruit industry to cope with varying requirements of international markets, through a single audit and certification.

The implementation of the program has already been widely recognized in Chile's main international markets, with formal equivalencies having already been secured in Europe and the United States of America.

The objectives of ChileGAP include responding to worldwide food safety requirements and reducing the risk of contamination in Chilean exports of fresh fruit, taking into consideration compliance with practices relating to CSR and overall crop management. This set of measures helps strengthen Chile's reputation as one of the world's principal producers of fruits that are internationally recognized for their safety and uniformity.

ChileGAP certification is accepted today as equivalent to EurepGAP in the European market. Similarly, in May 2005, an agreement was signed with Davis Fresh Technologies (Prosafe) to place ChileGAP on an equal footing with certification of safety for the US markets, a recognition which went into effect in October 2005.

ChileGAP is the first program in the world which has developed a uniform procedure for Europe and the USA that is implemented at all levels of an economy's fruit growing industry. It is the only non-European system of standards that has received accreditation from EurepGAP.

Verification of compliance with Good Agricultural Practices established by ChileGAP is carried out by internationally accredited independent certifying organizations. The certification system upon which they rely is updated continually in accordance with international industry demands, making it an effective tool for guaranteeing the safety of fruit and the excellence of the Chilean industry's production and post harvest processes.

Producers and exporters work together to administer ChileGAP. Their central mission is to promote and develop this program and comply with plans to improve it, thereby facilitating long-term relationships between suppliers and distributors. They have, among other mechanisms, a free of charge online technical information system with different levels of access and confidentiality, which could be accessed by producers and exporters for information on the technical and historical background of the degree of implementation existing in their properties. Buyers can likewise obtain information on the certification status of their suppliers (Website: www.chilegap.com).

At present, ASOEX is leading a much-needed “Initiative for Worldwide Unification of GAP standards”, with the goal of unifying criteria, procedures and requirements imposed on the various destination markets of Chilean fruit, thus facilitating marketing, avoiding duplication of efforts and helping to reduce the industry costs.

Integration of Good Practices/CSR into Supply Chain

As described previously, transforming production and making the supply chain of the fruit sector conform to international social and ethical responsibility standards has been imposed, to a large extent, upon the Chilean fruit sector by international market conditions. Exporting principally to northern economies in Europe and North America has raised social responsibility standards among producers of consumer product serving these developed economies, and has trickled down to the Chilean fruit sector as well. In these economies, the general public have gradually become more socially aware of consumer product ethics and with their purchasing power they can easily sway producers to follow more sustainable processes. Hence, there was a need for a program such as ChileGAP to strengthen practices in the exporting sector.

As a way of integrating GAP into the supply chain, the large exporting companies have assisted their fresh fruit suppliers in implementing GAP standards and going through the certification process.

The agriculture producers can also obtain co-financing for consulting on the implementation and certification of the GAP through CORFO instruments such as those of FOCAL which help SMEs to obtain ISO and GAP certifications for the agricultural industry. Other CORFO financing includes programs such as the “Programa de Desarrollo de Proveedores” (PDP) or Supplier Development Program which is aimed at improving the competence of productive chains and strengthening relationships between the larger firm participating in the PDP and its smaller suppliers. These retailers reap the benefits of the development program by achieving market stability and know-how, whereas the larger participating company attains a consistently higher quality supply.

The other CORFO co-financed program is the “Proyectos Asociativos de Fomento” (PROFO) or Project Partnerships for Business Development which essentially helps create and develop new business, which due to its nature and size, would be better carried out by forming new business partnerships that are larger in capacity and competitiveness.

The integration of GAP via the supply chain has proven to be a win-win situation for all stakeholders of the supply chain. On the part of exporters, they are able to comply with their clients’ demands (i.e. European and North American supermarkets/buyers), while simultaneously strengthening supplier relationships and assuring product quality, thereby making their fruit

produce more competitive in more demanding markets. By eliminating pesticide use and lowering rate of work related accidents, producers are able to reduce their production costs significantly. The consumers for their part enjoy the benefits of ethically produced and safer product.

It should be pointed out that in terms of CSR, ASOEX has been proactive in promoting the concept and its benefits to SMEs and large companies, and in some cases these SMEs supply exporting firms.

Challenges/Problems Faced and How These were Dealt with

Cultural Factors

Arguably the biggest challenge to the implementation of the GAP program has been the resulting culture shock when the CSR concept was first brought to the attention of SMEs and fruit producers. Participating SMEs had no prior knowledge of CSR and how it works. They were also initially wary about the seeming lack of immediate economic returns from what could be a significant financial and time investment in CSR which was still a vague and uncertified concept. The five SMEs which attended the agriculture sector meeting and met with the consultant to share sustainability information aired their distrust and suspicion of the new concept.

Another culture-related problem that was witnessed during the implementation of the ChileGAP program was a misunderstanding of CSR and confusing it with corporate philanthropy. Indeed such a mistake can be forgiven in a society such as Chile's, where historically the landowners have taken a paternalistic stance with their workers and local community. More specifically, it opened opportunities to improve management of the business through more rigorous data collection, imposition of controls and the adherence to procedures. All these have made possible better control of the production system and generation of financial savings through a more efficient use of resources, more commonly known as economic efficiency gains.

This misconception was addressed by further training and dialogue through the CORFO co-financed programs. In time, the SMEs also saw the business case take effect within their companies which, in turn, helped change their mindset from a philanthropic outlook to a CSR orientation. Chilean fruit growers and exporters however were not accustomed to being held accountable for the social conditions nor the working conditions of their workers which they had traditionally overlooked. Thus the program implied a radical change in their day to day operations.

Another serious challenge was how to change the behavior of the workers themselves and conform to the requirements of the GAP program especially in terms of health (e.g. personal hygiene) and safety issue (e.g. use of new equipment). Personal hygiene concerns included regular washing of hands, not smoking and others. The GAP program requires producers to train and certify that their workers observe socially and environmentally responsible practices. Workers who were required to take training courses in GAP included tractor drivers and those working directly with pesticides.

View to the Future with ChileGAP

One issue which will have to be confronted in the future is how to harmonize (or mutually recognize as equivalent). ChileGAP standards and international standards such as those of ISO 26000 on Social Responsibility, Global Compact, the GRI and more sector specific initiatives like EureGAP and Prosafe. Another contemporary issue which will have to be tackled is raising the program level to meet the increasingly demanding social and environmental standards of large international retailers. Large supermarket retailers such as Wal-Mart, Tesco's and Marks & Spencers are constantly demanding enhanced evidence of social and environmental responsibility from their suppliers.

Recently, the emphasis has been placed on the specific working conditions of those involved in production, and not just on the health and safety aspects. Tesco, Marks & Spencers, Sainsbury, Waitrose and an array of other UK import retailers participate in an initiative called Sedex or the Suppliers Ethical Data Exchange, a web-based system for companies to input data on labour standards at their production sites. The Sedex system has been designed to allow companies that are in an existing trading relationship to share this information, thus saving time and money lost in duplicated information. As a result, companies are better able to drive and demonstrate improvements. In fact, Sedex, along with Ethical Trading Initiative and Temporary Labour Working Group, resulted from the demand of consumers from mainly northern economies to be provided information on detailed labour practices from their suppliers. This development will undoubtedly be in the minds of fruit producers from emerging economies like Chile in the near future.

Conclusions

Sector specific social responsibility initiatives such as ChileGAP have broken new ground and achieved significant results. Given the importance of SMEs in Chile's economy, the resulting employment generation and promulgation of good practices in the global food supply chain have contributed substantially to a more sustainable development model.

Although the pilot project encountered birth pains and other unforeseen difficulties, the project team has been able to address many of the obstacles, particularly those related to cultural factors that have inhibited the willingness to change. It is hoped that ChileGAP will progress even further by addressing the problems that confronted its initial adoption. The vision is for SMEs in the fresh fruit export sector in Chile to play an even more active role in running businesses that are socially and environmentally sustainable, and which are cognizant of the emergent social and ethical responsibility of their main clients, the large northern economy-based buyers and retailers.

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CSR and the Supply Chain in Changyu Pioneer Wine Co. Ltd

Case Study:
China

China

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The case was developed with the cooperation of Changyu Pioneer Wine Co. Ltd solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

The concept of Corporate Social Responsibility (CSR) is just unfolding in China. Enterprises are at different stages of understanding and implementation of CSR. Some have been releasing their CSR reports annually, though many still have misunderstanding about CSR due to various reasons. In this case study, Changyu Pioneer Wine Co. Ltd is an enterprise with a well-established brand in the domestic and international markets. The company is now at the stage of rapid growth and emerging as a leading player in the wine industry in China. In Changyu's whole supply chain, vintage grape planters, sales agencies, foreign importers and exporters constitute the critical parts. Hence, Changyu faces key challenges in its relationship with these stakeholders as the company implements its corporate social responsibility initiatives.

Understanding the critical importance of these relationships, Changyu formulated its internationalization strategy and adopted measures to guarantee vintage grape planters' benefits, which included providing free technical support of experts and entering into purchasing contracts with vintage grape planters. These measures not only protected the planters' benefits but also secured the supply of quality vintage grapes to the company.

Changyu likewise organized its whole production process in accordance with international practices and commonly accepted regulations (e.g. SA8000). The benefits of suppliers, agencies, customers, local community and environment were taken into consideration in everything, from the purchase of raw materials to production and from packaging to selling. With the establishment and operation of its four brand chateaus, Changyu completed its strategic layout for internationalization and gained increasing recognition at home and abroad.

The implementation of CSR helped Changyu generate not only economic but also social benefits both domestically and internationally.

Introduction

As an enterprise with more than a hundred years of history, Changyu Pioneer Wine Co. Ltd is now the number one company in the wine industry in China. With sales income of US \$475 million in 2006, the company also ranked 14th in the world.¹ Throughout Changyu's history, the company has encountered various hardships and opportunities such as several changes in ownership and reforms of shareholders.

In all of these changes, Changyu has assumed its social responsibilities and has established favorable relationships with its suppliers, customers, the local community and government. One of the critical factors and biggest challenge for the success of the company is establishing and maintaining good relationship with its domestic and foreign suppliers. This is where the vintage planters and foreign importers and exporters play the key role. With economic globalization, domestic enterprises are facing competition both at home and abroad. For companies which do business globally, CSR implementation is becoming more and more important.

¹ Interview with Mr Zhou Hongjiang, General Manager of Changyu Pioneer Wine Co. Ltd

Overview of CSR in China

At present, Chinese enterprises, especially non-state-owned enterprises, are generally at the preliminary stage of growth and do not have a profound recognition of the concept of CSR and its importance. Under this scenario, it takes a long time for Chinese enterprises to incorporate CSR into the management of their businesses. Some enterprises which have no CSR mechanism in place focus on quick successes and instant benefits and in the process, exploit resources excessively, pollute the environment, evade taxes, cheat in financial affairs, default on wages and ignore security.

Problems concerning CSR in some labor-intensive enterprises are even more remarkable. Some employers do not sign employment contracts with employees which makes the fundamental rights of employees insecure. Some provide very poor working conditions and no safety measures, which sometimes cause the poisoning or even the death of employees. Many force their employees to work overtime with little or no extra pay in violation of the labor law. These kinds of behavior really harm the harmony between employers and employees, enterprises and consumers, enterprises and investors, and enterprises and the natural environment.

The problems of these enterprises in carrying out their social responsibilities brought not only social problems but also posed challenges from international competition. This is because with economic globalization, the concept of CSR has become very popular in Europe and North America. Hence, the enterprises most affected by the problem of CSR in China are those engaged in international businesses. Some enterprises which did not meet the requirements of SA8000 failed in their bid to become suppliers to the international market. Thus, CSR has directly influenced business opportunities for Chinese enterprises.

The China Enterprise Confederation, the only organization representing Chinese employers, has advocated that enterprises join the United Nations Global Compact and make an effort to become good corporate citizens. A consensus has emerged that in order to realize the goal of a harmonious society, it is now time for China to establish a system of incentives and penalties that would encourage enterprises to implement their social responsibilities with government guidance, legal guarantee, social supervision and self-regulation.

The manner and extent by which enterprises implement their CSR will vary for different enterprises with different resources and going through different stages of enterprise growth. In the **stage of gestation** and struggle for subsistence when enterprises have limited resources, enterprises should begin building up the ideals of CSR and abiding by the legal regulations. In the **stage of rapid growth** when enterprises greatly increase their strength, they should take CSR into consideration from the strategic perspective of the enterprise and take care of the benefits of all stakeholders. In the **mature stage** when they have accumulated substantial resources and capacity, enterprises should assume their social responsibilities more actively, not only from the legal perspective but also from the moral perspective, including resource saving, community responsibilities, public welfare and beneficence.

In general, the evaluation on CSR is done from two levels. The basic level CSR requires compliance with law and international labor regulations; the higher level CSR includes moral responsibilities. Although implementing CSR can mean additional cost for the enterprise, it however helps establish the enterprise's social image, improve the credibility of its products and services, and in the final analysis, bring higher rewards to the enterprise.

Reasons for the Lack of CSR in Chinese Enterprises

In China, enterprises fail to assume their corporate social responsibilities because of the following reasons:

- 1. Focusing on the short-term profits and ignoring long-term social responsibilities.** In the transformation process of the Chinese economy, enterprises have likewise been transformed into independent economic entities. Under the pressure of severe domestic and international competition, enterprises have to make themselves stronger and bigger first and enhance their capacity to manage risk in order not to be eliminated. This inevitably leads to the enterprise's ignorance of their social responsibilities such that some enterprises even build up themselves at the cost of these responsibilities. At the same time, although government no longer interferes with their business operations, enterprises still have the burden of providing some public services—a condition that is a carryover from a long history of planned economy. Thus the reluctance and passivity of enterprises in providing those services, together with the lack of regular government administration, also resulted in the lack of CSR among some enterprises.
- 2. No rigid restriction on enterprises' lack of CSR.** With the reform and opening policy, China has made great achievement in reforming the economic and political systems but still has to complete and strengthen the legal system. The penalty imposed on enterprises for not fulfilling their CSR is not heavy enough to serve as a warning and restriction. This encourages enterprises to focus only on the maximum profits at the cost of stakeholders since the profits they gain from bad business practices is far bigger than the penalty that might be imposed on them. This causes a strong sense of unfairness among the “good” enterprises, and discourages them from sustaining their social responsibilities.
- 3. Lack of supervision and restriction within enterprise.** The economic reforms in China have brought about profound changes in enterprise ownership. Except for a small number of very large companies, most enterprises have been transformed into non-state-owned companies where the status of employees has been weakened and the gap between employees and the management team has become increasingly bigger. The Workers Union does not have much say in protecting workers benefits. This encourages many company owners and managers to ignore the rights and benefits of employees in their desire to maximize company profits. The implementation of CSR is also not supervised by any organization.
- 4. Lack of impetus in implementing CSR.** China's reform and opening policy started at a low economic level. At the level of both the economy and enterprise, the focus was primarily on economic benefits which had indeed contributed to the economic development at that time. However this has also formed the mechanism for an inefficient pattern of economic development that emphasizes immediate benefits and misleads people's concept of development. For instance, the quantity was given priority over the quality of economic increase, economic increase was regarded as equal to the increase in wealth, more emphasis was placed on economic development than on social development, and natural resources were exploited. All these concepts have deeply influenced enterprises and resulted in their lack of motivation to fulfill their social responsibilities.

Importance of CSR and the Case Study

From the global perspective, the CSR movement is a general trend that nothing can impede. In the long run, the fulfillment of CSR is not only beneficial to an economy and society as a whole but also to an enterprise. CSR helps enterprises establish people-centered concepts and encourages them to care about public services and environmental protection for enterprise sustainability. It helps enterprises to transform themselves from low labor-cost competitive advantage to brand competitiveness both in the domestic and international markets. It also helps an enterprise to win more loyal customers with its good image, to retain intellectuals and avoid lawsuits with better working environment, and to improve the management of the enterprise and gain more opportunities in the global market.

The case study helps identify the enterprises that best fulfill their social responsibilities while earning profits and set good examples for others to follow. In 2006, China Central Television (CCTV) held the first session of Social Responsibility Investigation of the Enterprises in China after completing telephone interviews with 980 enterprises and collecting data on 500 enterprises. As a result, 20 were chosen as the best enterprises in fulfilling their social responsibilities. This study has made us understand Chinese enterprises' level of awareness and contributions to CSR and the problems that they faced in fulfilling their social responsibilities. The results of the study motivated more enterprises to actively assume their social responsibilities and contribute more to the creation of a harmonious society.

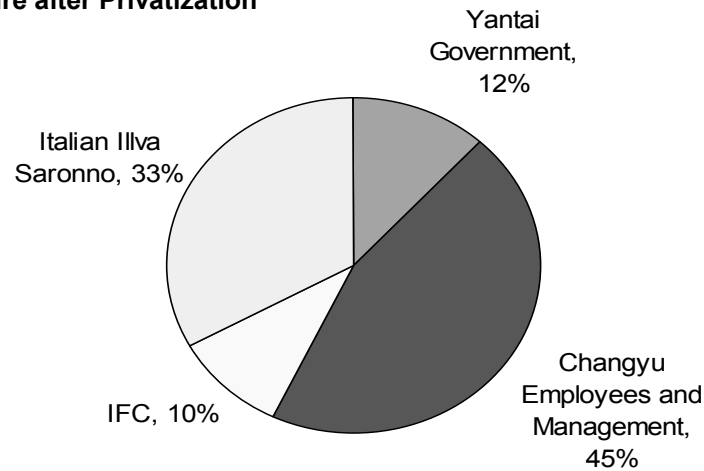
Yantai Changyu Group Company Limited

Yantai Changyu Group Company Limited is a major corporation operating a wide variety of business interests. It currently has major holdings in a public company and a subsidiary, and owns four wholly-invested subsidiaries and its own branch. Initially focused on the production of wine and related products, the company has vigorously expanded into other areas including the development of health care wines and Chinese herbs, the processing of liquor and alcohol, import and export, packaging, machinery and manufacturing of glass products.

Although the history of grape planting and wine making in China dates back to the Han Dynasty (206 BC-220 AD), the industrialized production of wine was started by Changyu. Due to the foresight and wisdom of its founder, Mr Chang Bishi, a patriotic overseas Chinese, the development of China's national wine industry over the past century has been recorded for posterity.

Changyu Group (holding) was historically 100% owned by the Yantai government after 1949. It was privatized via a two stage process in 2004 through an Employee and Management Buyout (EMBO) of 45% of the Group and the sale of an additional 43% stake in the Group to foreign investors, in two separate tranches of 33% and 10% each. The shareholding structure of Changyu Group after privatization is illustrated in **Figure 1**.

**Figure 1:
Shareholding Structure after Privatization**



Source: Report of Shareholder Changing of Changyu, 2005²

At the beginning of the 21st century, Changyu was China's leading winery and Asia's largest wine operation, with an annual production of 120,000 tons,³ and a well-established domestic market. Throughout that century, generations of Changyu employees labored with painstaking devotion to produce wine products that were immensely popular both at home and abroad.

In recognition of its great contribution to the development of global wine-making, Yantai City where Changyu's wine originated, is the only city in China to be honored with the title, "International Vine and Wine City." This honor comes from the painstaking endeavor of generations of Changyu employees, using elaborate yet intricate methods that ensure Changyu wine products are enjoyed throughout the world.

In cultivating premium wine, the Changyu people are also cultivating their own unique wine culture. "Loyalty, devotion, quality and performance" is regarded as the spirit behind Changyu. This unified spirit is the driving force behind Changyu's unswerving and persistent progress. Changyu epitomizes the maxim that companies do not make people, people make companies.

Despite their sharp competitive edge, the people of Changyu never allow complacency to creep into their work ethic. The new millennium presents not only wide opportunities but also new challenges for the company as it continues to strive to create the best products in the world and achieve progress.

Products and Services of Changyu

In the domestic wine industry, Changyu ranks first in all major economic indexes. Changyu's goal is to become one of the top ten in the international wine industry by 2008. In August 2006, *Newsweek* and *Interbrand* jointly appraised the "top 20 Chinese brands" and Changyu ranked the sixteenth. In October 2006 *Forbes* (Asia Edition) appraised 200 best enterprises with global sales of not more than US\$1 billion, and Changyu made it to the list because of the vigor and reputation of its brand, steadily increasing profit modes, excellent management team and capacity in expanding its global market.

In 2007, China had over 500 wineries in operation, with the top 10 producing around 10-12 million liters of wine annually. Cabernet Sauvignon was the most popular grape wine accounting for 40% of

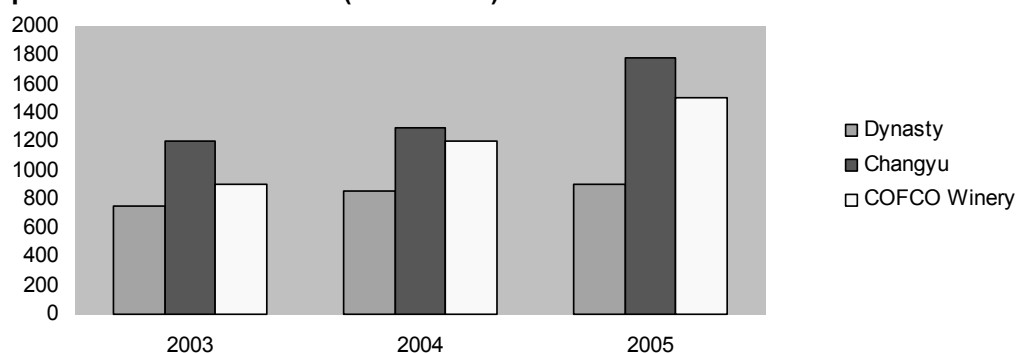
² Report of Shareholders Changing of Changyu 2005.

³ 2006 Changyu's Annual Report.

the market in 2003. Merlot and Cabernet Franc each shared around 10% of the market. The low-end, middle-end and high-end wine segments made up respective market shares of 50%, 40% and 10%. The profit margin of low and middle end wine segments stood at only 11% while that of high end wine ranged from 30% to 50%.

According to the China Alcoholic Drinks Industry Association, four domestic wineries represented 51.49% of total Chinese wine production in 2006. The top three were Changyu, Great Wall, and Dynasty (**Figure 2**).

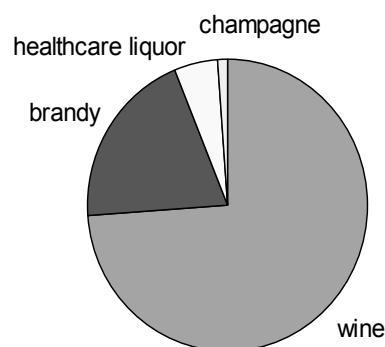
Figure 2:
Comparison of Sales Revenue (In RMB mn)



Source: Sinolink Securities, Dec. 2006

Changyu's product structure (**Figure 3**) and revenues indicate that wine is the company's main product and the biggest source of its revenues (**Table 1**).

Figure 3:
Changyu's Product Structure



Source: Sionlink Securities, Dec. 2006

Table 1:
Revenue by Product Category (2004-2006, in RMB mn)

	2004	2005	2006
Wine	923.97	1,340.21	1,631.07
Brandy	300.90	363.42	395.17
Health Liquor	98.09	80.78	97.54
Champagne	15.47	19.98	21.47

Source: Changyu's Financial Report (2004-2006)

As a wine company with a hundred years of history Changyu assumes the responsibility of promoting and popularizing wine culture in China. In 2002, Changyu pioneered the establishment of the first domestic tourist destination in the wine industry which can receive 300,000 tourists a year. It is the only 4-A rated tourist spot in the country.

Changyu has over 30 subsidiaries around China and every year, a group of consumer opinion leaders are chosen to experience the wine culture tour of Changyu. Consumers who attended the first wine culture tour at Castle Chateau in Yantai found everything new and fresh and their experience strengthened their loyalty to Changyu. Later, the company organized the visit of consumer media representatives to the ice wine base in Liaoning, where they could observe how the ice grapes were picked, compressed and processed. All these activities intended to increase consumer awareness of Changyu wine which could lead to an increase in sales by millions Yuan.

Ordering wines in barrels is an individualized service Changyu provides. In the Chinese wine market, the level of competition is increasing and the consumption is becoming more individualized. While Changyu provides personalized services for consumers, it also promotes the consumption of wine in traditional channels like restaurants. Changyu established a top-class membership club and catered to orders by barrels. Shortly after taking this measure, Changyu received orders for over 1000 barrels of wine from many famous individuals and organizations such as CCTV, which contributed a lot to the brand image and marketing of Changyu's wine products.

Based on the analysis of different income levels, cultural background and preferences of consumers, Changyu further differentiated the wine market for high-class consumers and put more effort on increasing buyer's value. This helped Changyu avoid price competition.

In their product series Changyu increased individualized services. Changyu also formed partnerships with famous domestic brands, such as People's Great Hall and Diaoyutai, which took full advantage of the "wine for national banquet" channel and thus strengthened Changyu's image as a top wine brand.

International Strategic Cooperation of Changyu

Changyu faces global competition even without going abroad because of the increasing globalization which made possible the entry of various kinds of foreign wine in China. For any industry or enterprise, China deserves careful study because of its huge market potential. As part of an international supply chain Changyu has to actively participate in the competition in the international market. In carrying out its internationalization strategy Changyu has undertaken the following:

1. Internationalization of ownership system and capital investment. In the current share structure of Changyu, Italian Illva Saronno Corporation holds 33%, International Finance Corporation 10%, Yantai SASAC and Yuhua Corporation composed of Changyu employees holds 45%. This kind of ownership structure greatly motivated all parties and brought together the shareholders' vast experience in operating the brand and managing its capital in the international market. With 400 years of history, Illva has a sales network in 150 economies and abundant international marketing experience. International Finance Corporation of World Bank also holds shares in over 60 private enterprises and has very rich experience in international management of capitals.

2. Internationalization of talents. In recent years, Changyu has been involved in running schools together with Tongji University and Jiangnan University, and also sent its vintage engineers and other technicians to study abroad. Changyu has a national technical center, the only one in the industry, which has an R&D team of over 100 people.

Changyu also had regular communication with first-class wine companies abroad. They invited vintage experts and grape planting experts from many European and American economies such as Australia, France, and Italy. At the beginning of 2006, Changyu met the international standard for classifying the quality of wines, which is based not only on production year of grape, place of production and age of grape trees, but also on other aspects such as techniques of vintage production, oak barrel storage and technical level of vintage engineers.

Apart from training the technical staff, Changyu also emphasized the training and recruitment of marketing talent. It enrolled some local staff in overseas economies, and thereby increased its international market share by making full use of the staff's understanding of the local market. The company retained Australian wine experts as senior advisors and conducted over 300 sessions of training in wine culture and knowledge for leading consumers in China. In 2006 Changyu invited Mr Kelly, school director of the University of Pennsylvania, as its senior advisor for international marketing. This greatly helped Changyu's global marketing efforts.

3. Improvement of Changyu's marketing network in three aspects. The first aspect is addressing the China market. A precondition for Changyu's globalization was to do well in the domestic market, and this required high-quality products, a strong core business model and a solid market position. In the domestic market, Changyu had 1500 marketing personnel and about 3000 agents who were all well-educated and responsible for both marketing and management. Changyu began marketing its wine abroad and at the same time introducing foreign wine to meet the needs of China's consumers through Pioneer International Wine Corporation which was established to sell wines from around the world.

The second aspect of the strategy was expanding exports. Changyu chose and developed the best agents in order to increase export sales. In 2006, exports reached RMB30 million, which though relatively small, was an encouraging trend. TXB Corporation of Germany, one of the largest wine agents in Europe ordered 240,000 bottles of Changyu Cabernet wine- the biggest order of Chinese wine exported to Europe in recent years.

4. Establishment of four professional wine chateaus. The Castle Chateau built in Yantai a few years ago is the first professional wine chateau in China. Its wine products have been warmly welcomed since they first appeared in the market.

Chateau Changyu Afip Global is jointly invested by investors from America, China, Italy, France and Portugal. It is a wine chateau integrating vintage, tourism, entertainment and training on wine knowledge which was opened for business in June 2007. The chateau is positioned as the new leader of international wine chateaus and it is technically supported by OIV (*Organizacion Internationale de la Vigne et du Vin*). It is positioned for top political and business activities with Beijing as the focus of marketing. The Olympic Games in Beijing in 2008 will be a good opportunity for the entry of Changyu's products in the international market.

Changyu cooperated with Canadian Aurose in setting up the world's largest ice wine base in Liaoning, which released new products in December 2006. They organized local and foreign wine experts for wine tasting of the new products side by side with foreign ice wine. The experts found Changyu's ice wine to be of high quality.

Currently the combined annual output of ice wine from Austria, Canada and Germany totals 1000 tons. The same volume can be produced by Changyu alone; hence the ice wine of Changyu will create a great impact on the world's ice wine market. China will become the major supplier of ice wine in the world market together with Canada and Germany. Ice wine will be one of the key products of Changyu to expand its world market for wine.

Changyu also jointly built wine castles in distinguished foreign vintage grape planting area. It built Changyu Kely Chateau in New Zealand which marketed its products to Oceania and China. The two kinds of products sold domestically are positioned particularly for golf clubs with over one million high-income members.

Changyu's internationalization strategy follows two principles. The first is keeping its own brand. It maintains both an independent brand and jointly-owned brand. Its independent brand of Changyu Cabernet has successfully entered the European and American markets. Its jointly-owned brand, Changyu-Kely, serves the Oceania market with New Zealand as the center. Through cooperation with these strategic partners, Changyu has improved the quality of its products, increased the influence of its brand in the world and met the requirements of CSR according to international standards.

Key Challenges Concerning CSR and the Supply Chain in Changyu

Changyu recognizes that CSR is a voluntary activity that a company has to undertake to have sustainable growth, and that CSR covers compliance, consumer protection, environmental preservation, labor, human rights, contribution to community and local development - all of which go beyond pure financial performance measures. The current high level of attention to CSR is mainly attributed to the globalization of business and the occurrence of company bankruptcies due to unethical practices. The company anticipated that the social requirements placed on business enterprises would increase further due to various large-scale changes in the business environment.

The objective of Changyu's CSR activities is for the company to carry out business activities and at the same time fulfill its responsibility to contribute to the sustainable development of society. The company believes that CSR activities will help raise its corporate value and will ultimately support the sustainable mutual growth of its suppliers and its own business. The company's resolve to adhere to CSR is faced with a number of challenges:

- 1. Challenge of keeping good relationship with the company's suppliers.** As a wine producer, Changyu must ensure the quality of the raw materials, particularly grapes. Therefore, Changyu established four chateaus in different cities in China, which provide good quality raw materials for the production of wine and job opportunities for the local labor. It is very important that Changyu maintains good relations with the local government and communities. Changyu adopts the policy of being open, fair, honest to its sales agencies and customers so that they can all contribute to Changyu's good image and by so doing, gain benefits from their efforts.

The special feature of wine demands high quality vintage grapes which can only be ensured through the proper mode of planting and growing. There is a surplus production of vintage grape in China but high-quality grapes are in short supply. This is because China produces

about 300,000 tons of wine a year. Since 1.5 mu* of vintage grape can produce one ton of wine, it would need a maximum of 600,000 mu to provide the vintage grape materials needed for the total wine output of 300,000 tons. However the area planted to vintage grape has now exceeded 750,000 mu, implying that there will be a large surplus of vintage grapes under normal climatic conditions. Such situation will undoubtedly affect the vintage grape planters.

When natural disasters, plant diseases and insect infestation strike however, vintage grape will be in short supply. To address this potential situation, Changyu developed a grape planting base and invested a large sum of money in developing the Shelongzhu base which put 80,000 mu under cultivation.

Changyu also imported oak barrels, mainly from France, for storage to maintain the high quality of wine. High quality oak barrels are usually sourced abroad. Without the support of these foreign oak barrel suppliers, it would be difficult for the company to keep their products in good storage and maintain their high quality.

- 2. Challenge of maintaining good relationships with the company's sales agencies.** The products of the company are mainly sold through its China-wide network of sales agencies and foreign agencies. For domestic selling, Changyu must provide the right product to the sales agencies according to the market segments served, help sales agencies increase investment in advertisement, and encourage sales agencies by giving more favorable contract terms. For overseas sales, apart from maintaining the high quality of the products, the company must meet the needs of the international market to satisfy some commonly accepted standards, for example those of SA8000, which has had a great impact on many enterprises in China. SA8000 is used by purchasers worldwide to measure how well a supplier has implemented its CSR. It has consequently become a new standard to measure a supplier's credibility and reliability.

Efforts of Changyu in Fulfilling CSR

Changyu's efforts in developing relationships with its suppliers and customers to enhance brand recognition and quality image need to be seen in the context of the company's overall commitment to CSR. Changyu earns customer satisfaction and confidence by developing and offering beneficial and reliable products and services and by paying careful attention to safety. It supplies products and services of value, based on an understanding of customer needs and expectations so that it will be highly regarded by society. The company also maintains and improves the quality and safety of products and services to win customer satisfaction and confidence, and responds and provides adequate information to customers with sincerity.

Changyu strives to develop creative technologies and works actively to break ground in new business areas for the future prosperity of society. It maximizes customer satisfaction and develops unique technologies that contribute to the enjoyment of high-quality life. Changyu promotes fair, transparent, and free competition among corporations and ensures that its relationships and dealings with government agencies and political bodies are of a normal and proper nature. It enhances general awareness of the observance of related laws within the company. It builds and maintains control systems for proper entertainment and gift-giving.

* Mu is the Chinese unit of area. It is equivalent to one-sixth of an acre.

Changyu delivers accurate and sufficient corporate information in a timely, clear, and appropriate manner while enhancing the transparency of its corporate activities. It discloses adequate and timely information to stakeholders and promotes two-way communication with them. Changyu respects the customs and cultures of all regions and economies and manages its activities in a way that contributes to community development. It promotes corporate activities based on respect for local cultures and mutual trust. It continues to be interested in the activities of local business partners to fulfill their CSR and support their efforts to improve. As a good corporate citizen, it fully recognizes that it is a key member of society and actively engages in philanthropy and other activities of social benefits. Changyu promotes social contributions that respect the interests and support the progress of all stakeholders, including local communities.

Changyu respects human rights in workplaces and promotes respect for human rights and equal opportunities among all business partners, including those overseas. It respects each employee's individuality and creates work environments where all its employees can fully demonstrate their abilities and carry out their jobs with enthusiasm. It supports employee's efforts to plan and prepare for their future and develop their skills. It endeavors to create an equitable work environment for a variety of talents to be fully demonstrated.

Changyu also continuously strives to innovate and generate superior products of high quality through improvements made in its supply chain:

Huge Investments in Developing Grape Planting Base

Huge investment has been made in developing grape planting base to satisfy the demand for raw materials in the production of high quality wine. In the last few years, the sales of Changyu Cabernet has skyrocketed to several hundred million RMB from about RMB50 million, and it is estimated that the sales of Changyu castle wine will increase steadily in the next 12 years.

The market demand for such high-quality vintage grape as Shelongzhu will greatly increase with the increase in sales of Changyu Cabernet wine and Changyu chateau wine. In 2004, Changyu declared that RMB300 million would be invested in three years, of which RMB5 million would go to breed selection and technical development; RMB5 million to improving technical skills of grape planters; and RMB20 million to increasing the scale of Shelongzhu grape planting in Yantai. At present, the planting of Shelongzhu grape accounts for about 70% of the total production in China. With the RMB30 million input, Shelongzhu grape planting will be further expanded and thus satisfy the increasing demand for Cabernet wine from high-quality vintage grape.

According to experts, the increase in Shelongzhu grape planting by Changyu can give the company a competitive edge upstream, and at the same time support the brand recognition and quality reputation of Changyu Cabernet. In the "fighting for cabernet" in 2005, Changyu gained the support of academic and major media sectors although some competitors imitated Cabernet by taking advantage of legal flaws. Instead of taking legal measures, Changyu strengthened its market position by ensuring the high quality of raw materials with better results.

Provision of Technical Support and Formation of Close Relationships with Grape Planters

Changyu has 80,000 mu of vintage grape planting base composed of 200 units with thousands of planters and workers. Changyu has taken various measures to guarantee grape planters benefits.

- 1. Protection agreements were signed with planters to ensure planters' profits.** Changyu signed contracts with all planters in the grape base and promised "protection price for general grape and higher price for high-quality grape." Protection price means that planters' profits from planting grapes are 1.5 times more than the profits they can gain if they grow grains. High-quality grapes are examined by professionals and are priced higher. This makes the planters confident to plant high-quality grapes without worrying about marketing their grapes and earning profits. In 2005, the average income from planting grapes in Yantai reached RMB8000 per mu.

The mode of "base plus planter" followed quality-oriented production policy. Changyu purchases grapes from these planters at a price not lower than protection price and higher than the market price, and pays planters by Spring Festival every year. This forms a relatively close, steady supply circle.

- 2. Grape planting bases are classified into different classes and the top classes are awarded prizes.** Besides a good sum of prize money, planters receive materials on the latest planting techniques and protection against plant diseases and insect pests. Every planter has been given a brochure on *Principles of Assessment of Planting Base* and the Standards for Classification, which assesses each plant according to its geographical position, scale, breed of the grape and planting management.

Because of its many years of experience in the construction and management of planting base, the quality of grapes in Changyu's planting base has been improving. For example, in early 2005 when there was more rain than normal, Changyu still managed to produce high quality grapes in increased volume.

- 3. The technicians from Changyu grape planting base complied with the company's requirement on the management of vintage grape with no public hazard.** The technicians tracked the planting in all aspects throughout the process from growing to fertilizing, from output control to pesticide usage. They were always ready to help whenever problems occurred in planting. In order to improve planters' working efficiency, Changyu asked farming machine experts to design small machines appropriate for planting use. Hence, weeds-cutting, fertilizing and pesticides spraying have been mechanized.
- 4. Each technician is allocated an area within the 80,000mu planting base which he has to manage.** The technician needs to choose over 10 grape gardens to manage for the supply of high-quality grapes. The assessment of the technician's performance is directly related to the quality of vintage grape, its output, average sugar rate and volume of rotten grapes in his area of assignment. A meeting is held every Monday so that technicians can review the previous week's operations, find solutions to difficult problems and plan the work for the following week. Every technician must work with planters four days a week and planters have to certify to the work that the technicians have done for the week.

Establishment of Other Grape Planting Bases in China and Outside of China as a Supplement to Yantai Base

The world demand for vintage grape is steadily increasing. In order to produce high-quality wine of various tastes and flavors, Changyu established its own wine companies or partnered with foreign companies in Hebei, Shanxi and Beijing. In central and western China, Changyu partnered with local farmers to establish 20,000 mu of grape planting base.

Changyu's increasing Yantai vintage base can hardly meet the needs of the market. As a corporation which aims to be among the top 20 wine producers in the world, Changyu believes that its growth relies heavily on the performance of its vintage grape base and that the planters are just as important as the company's market share. Throughout the process of grape planting and harvesting, executive directors of Changyu often visit the planters to listen to their ideas, plans, complaints and suggestions about vintage planting. Changyu's No.1 workshop was directly connected with the vintage grape base. Most of the technicians in Changyu provide free technical assistance to the planters from time to time.

The development of vintage grape base has made a large group of planters prosperous, especially those in central and western part of China, and has increased the pace of local economic development as well. Planters not only earned profits but also improved their technical skills which contributed to Changyu's competitiveness.

In 2006, Changyu's products accounted for 20% of the wine market in China and Changyu became the number one brand in the wine industry. Since 2002, Changyu had experienced high growth rate in sales, profits and taxes. In 2003, it had sales income of RMB2 billion and profits of RMB430 million or an increase of about 15% compared with 2002. In 2004 the two economic indexes further increased by 20%.

According to the strategic plan, Changyu will increase its sale of wine to over 100,000 tons in two or three years with sales income of RMB5 billion and profits of RMB1 billion. To make Changyu a world-class brand has always been the dream of all employees but this also signifies greater responsibility for all people of Changyu. With the expanding scale of operations, the vintage grape base has become one of the critical factors in realizing their dream. The technicians are exploiting new methods of planting grapes and improving the mode of "base plus planters." This has helped build a closer and more solid relationship between planters and the corporation. Planters gained more profits, the local economy improved and Changyu guaranteed its supply of high-quality vintage grapes.

Setting of High Requirement for its Suppliers of Barrels, Bottles, Packaging and Other Materials

Exporters of oak barrel and building materials must meet the CSR requirements according to international standard before they can be suppliers to Changyu. The manufacturers of wine bottles and package must implement their social responsibilities before they can be considered as suppliers by Changyu. They must have a good reputation in the marketplace; they must manufacture their products in resources-saving and environment-friendly way; and they must be just to their own suppliers. The final selection of suppliers is made through open, fair and just public bidding process.

Integration of CSR into Changyu's Cultural Construction

Since 1997, Changyu has been conducting a tour exhibition of one hundred years of wine culture in the major cities in China which includes a review of the history of wine industry in China, the present situation and prospects of the wine industry, and relevant information on wine. This was done through a combination of exhibits, special topic forum on TV, and articles in newspapers and magazines.

Changyu put up a wine museum, opened its historical wine cellar to the public, and displayed Changyu's particular culture through famous paintings and archive materials of historical importance. The company built wine castles by integrating grape planting, vintage, entertainment and tourism,

which added new dimensions to Changyu wine culture. They pushed the globalization of the corporation by participating in various domestic and international conferences on wine and consulting foreign experts, thus providing Changyu the most advanced technology and concept in vintage wine production and marketing in the world.

They also sacrificed a lot to foster the domestic market for wine, signifying its corporate culture as the leader in the industry. Although it takes time and means cost, it benefits the healthy development of the industry as a whole.

Changyu has institutionalized CSR in its relationship with its employees, suppliers, sales agencies and other stakeholders. The top management team puts more emphasis on CSR and attaches strategic importance to CSR. The company combines CSR with its internal management system and makes it a compulsory part of the company's achievement when the final assessment is carried out.

The company maintains good relationships with suppliers, sales agencies, customers, local governments and communities. Taking into consideration the nature of Chinese enterprises. Changyu develops its own evaluation system for CSR implementation.

Changyu hires and retains the most suitable employees at the lowest cost and best efficiency, including not only highly technical talents but also skilled workers. By increasing the power of the workers union, consumers association and other NGOs, the company promotes CSR not only within the company but also in the whole society.

Finally, the company increases its investment in environmental protection and voluntarily accepts the supervision of mass media and other concerned government organizations.

Conclusion

The Changyu case leads to a number of important conclusions about the concept and current stage of development of CSR in China. It also illustrates some important examples of the benefits of good CSR practices.

1. In the short term, the implementation of CSR may increase the running cost of a company as it strives to meet higher standards concerning labor, environment and other production aspects. Thus it may reduce a company's competitiveness for a period of time. As such, CSR can also be regarded as a non-tariff barrier by some exporting enterprises. This helps explain the lack of attention given to CSR by some enterprises (including Changyu before the restructuring was conducted in the company) in China.
2. In the long term however, the implementation of CSR brings both economic and social benefits to an enterprise. It helps an enterprise improve its brand image thus gaining more trade partners and giving the company more chances to succeed. It can help an enterprise attract and retain talent and consequently increase its competitiveness. It promotes sustainable development of society as a whole, which benefits the healthy development of the enterprise itself. This may well explain Changyu's achievements.
3. Problems created from the lack of socially responsible practices, external requirements and worldwide efforts to promote CSR are pressing Chinese corporations to place more emphasis and invest more resources in their social responsibilities. As a global company, Changyu has

recognized the importance of CSR and has met the key challenges throughout its supply chain by maintaining harmonious relationships with the vintage grape planters and its sales agencies at home and abroad. In assuming its social responsibilities, Changyu has made great achievement both socially and economically. Best practices concerning CSR in a company and the development of the company can form a virtuous cycle which mutually benefits each other. This is the most valuable learning about the Changyu case which can be shared with other companies.

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**Greening the
Supply Chain and Beyond:
The Case of
Asia Pacific Resources Holdings
International (APRIL)**

Indonesia

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The case was developed with the cooperation of APRIL– RAPP solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

This case is about the behavior of Asia Pacific Resources Holdings International (APRIL), a company which main production arm-RAPP - is in Riau Province, Indonesia. Contrary to the perception in the global market that majority of the Indonesian companies are ignorant or choose to ignore corporate social responsibility (CSR) RAPP as a part of APRIL is one of the few corporations in Indonesia which has made CSR an integral part of its business strategy and has regarded stakeholder engagement as a serious concern.

As a major producer of fiber, pulp and paper, APRIL believes that it has a fundamental role in developing ways to meet the world's growing demand for its products and at the same time integrating sustainability in its operations, as a seller in the global supply chain and as a buyer of raw materials.

The market and business review of pulp and paper indicates very good prospects. Nevertheless, APRIL is conscious of increasing customer awareness and concern with sustainability issues. APRIL recognizes that in markets where a commitment to environmental responsibility is fostered at the government level, customers want to be assured that relevant external standards are practiced by their suppliers. APRIL's commitment to sustainability and adherence to standards will differentiate the company and provide it a competitive edge.

APRIL also regards as a key challenge the general perception of overseas buyers that Indonesian business players act irresponsibly towards the environment. Therefore the company is very serious in greening the supply chain through various initiatives like protecting High Conservation Value Forest (HCVF) and developing the Mosaic Plantation Concept (MPC). Another challenge is the insistence of some buyers that the suppliers should have the Forest Stewardship Council certification which APRIL cannot have because it is automatically disqualified since its plantations were mostly developed after 1994. APRIL is addressing this by pursuing some initiatives, besides earning the national LEI certification on Sustainable Forest Management.

On the other hand, since APRIL believes that sustainability is key to its long term profitability, it has also imposed strict requirements on its suppliers to ensure that the supply chain is untainted. For example, it imposes the Pulpwood Legal Tracking system and works against illegal logging. Beyond that, APRIL also implements in other areas a number of CSR projects like the Integrated Farming System, SME Development, and social, infrastructure and educational programs.

The APRIL case demonstrates that the application of the Triple Bottom Line concept in the industry by managing forest resources into sustainable plantations that harmonize commercial, social and environmental development needs is a winning strategy.

Introduction

Involvement in a global supply chain opens new opportunities for business, but at the same time imposes new challenges to meet international standards and rules. In particular, growing pressures on corporate social responsibility (CSR) issues – whereby business activities are scrutinized by various stakeholders – has become a very real challenge, so much so that some CSR aspects have been viewed as non-tariff barriers by some local suppliers. However, the practice of CSR throughout the global supply chain is considered inevitable and all players have to be prepared for its adoption.

Indonesia is an economy which is perceived as not being too concerned with intellectual property rights, labor practices, environment protection and having one of the lowest scores in the Corruption Perception Index (CPI) of the Transparency International. In other words, there is a perception in the global market that majority of Indonesian companies are ignorant or choose to ignore the CSR elements.

For this reason, APRIL (Asia Pacific Resources Holdings International), a company whose production arm -RAPP (Riau Andalan Pulp and Paper) - is in Riau Province, Indonesia, was deliberately chosen as the subject of the case study. Unlike typical Indonesian companies, APRIL is a player in the global supply chain, and one of the few corporations in Indonesia where CSR is an integral part of the business strategy and stakeholder engagement is taken seriously.

In the global supply chain APRIL is a seller of pulp and paper and at the same time a buyer of raw materials for its products. From the perspective of APRIL both as a buyer and seller, greening the supply chain is of utmost importance to ensure sustainability in the industry. Thus, APRIL has been very serious in greening the supply chain and has even established its own standards, as a means of building its competitive advantage. APRIL has also pursued CSR initiatives in other areas, some of which take into consideration the local and cultural aspects of the surrounding community.

The case of APRIL captures the responsible behavior of the company in doing its business as part of a global market where the customers are increasingly concerned that the products they buy should be produced in an environmentally responsible manner. Since APRIL believes that sustainability is key to its long term profitability, it has imposed strict requirements on its suppliers to ensure that its supply chain is untainted. The lessons learned which are shared through the case, hopefully will contribute to a pool of learning which other players in the APEC economies can draw upon.

APRIL Profile

APRIL is Indonesia's leading producer of fiber, pulp and paper. It has forestry and mill operations in Riau province, central Sumatra. As a signatory to the UN Global Compact, APRIL embraces its responsibility to the communities within its sphere of influence. The company uses the influence that the scale of its operations has built up to promote development and advance sustainable growth in the areas where it operates. This has been done largely through the company contributions to the economy and the creation of employment opportunities.

APRIL's presence in Riau continues to be one of the reasons why people in search of a better life are attracted to Riau. As a leading economic force and major employer in Riau, APRIL provides livelihood to about 100,000 of the population. A study conducted by the University of Indonesia reported that in 2004, APRIL operations generated a total income of IDR 184.1 billion or USD 17 million for the local community, through direct and indirect employment.

APRIL embraces the sustainable development concept, and firmly believes that commercial, environmental and social imperatives must coexist. Its vision statement is:

To be one of the largest, best managed, most profitable and sustainable pulp and paper companies in the world, and be a preferred supplier to our customers and the preferred company to our people.

The APRIL Group comprises of:

- PT Riau Andalan Pulp and Paper (RAPP or Riaupulp), which has been operating since 1995 one of the largest pulp mills in the world in Riau, Sumatra, with a design capacity of

two million tons per year on a 1,750 hectares site, with fiber drawn primarily from government granted concessions.

- PT Riau Andalan Kertas (Riaupaper) which operates a 350,000 ton per year uncoated wood free paper machine.
- Asia Pacific Enterprises LTD (APEL) and APRIL Fine Paper Trading (AFPT), which markets the Group's pulp products and paper products, respectively

In 2006 APRIL had 3,713 Indonesian employees, 70% of them had been with the company for six or more years. Since the safety of employees is a key priority for APRIL, several initiatives have been implemented to maintain a culture of safety in its fiber plantations and within the mills. Since 2005, APRIL has obtained certification for its Occupational Health and Safety (OHSAS) Management System according to OHSAS 18001:1999 Standard. As a company which truly cares for its human capital, APRIL instills an instinctive belief in 'the APRIL way' of doing things and provides everyone of its people opportunity to develop themselves.

In 2005, APRIL established the Learning Institute (ALI) to take care of company-wide human resource development. Its mission is to ensure that the company attracts, trains and retains world-class employees and that the culture and competence of the organization support the sustainability, improvement and growth of APRIL. The ALI has adopted a Faculty Organization Model to reinforce its belief in self-empowerment and in quality rather than hierarchy. ALI development programs are designed to address one or more of the essential competencies required to enhance individual as well as organizational performance as reflected in the three APRIL Cultural Pillars (Customer Focus, Performance-driven and Proactive Teamwork), as well as in the 4Cs (Competence, Commitment, Character, Complementarity) and 4Es (Energy, Energize, Edge, Execution) models.

APRIL also realized that an intrinsic element of a sustainable business is a commitment to continual improvement, and as it has grown and developed, there has been a need to formalize its approach. To institutionalize continual improvement in APRIL, a new Business Continuous Improvement Department (BCID) was created in mid 2005 to effect sustainable continual improvement mindset through a standardized and formalized APRIL Improvement Management System (AIMS).

Under the AIMS philosophy, staff thinking and practice are expected to shift towards measurable and sustainable improvements. With support from the BCID team, the AIMS approach is being introduced company-wide. Following their training, individuals and groups of employees have proposed improvement ideas and projects. Approved ideas and projects are carried out and management gives appropriate recognition to successful proponents of these ideas. To support the embedding process, benchmarking among and within departments is undertaken and additional tools are provided.

Further, as a business operating in a sector with multi-stakeholders who might wish to know more about or even challenge what it does, APRIL has adopted the accessibility and transparency approach. Its "Open Door" policy allows all the stakeholders to observe the company operations and other initiatives first hand. The company also believes in understanding and learning the interests and concerns of its stakeholders, hence it regularly conducts dialogues with different stakeholders in various forms, including sending its own people around the world to meet with stakeholders. APRIL welcomes opportunities for constructive feedback and collaboration with interested stakeholders on issues of mutual interest. Engaging stakeholders at all levels has been the company policy right from the start.

Market and Business Review

Overview

Asia which includes China; India; Japan; and Indonesia, has 56% of the world's population and a market size exceeding that of the US or Europe. It is estimated that by 2020, Asia alone will require an additional 100 million cubic meters of fiber annually. In order to satisfy this demand, 3.5 million hectares of fast growing plantation will be needed. This provides an opportunity for Indonesian fiber producers, applying internationally recognized and certified forest management practices, to command a significant share of the potential market. As one of the major producers, APRIL markets to 56 economies. The Asia Pacific region is its largest market for both its pulp and paper products and Europe is its major market for paper. Japan is an important market accounting for about 15% share of APRIL's total paper sales.

Pulp Business Review

Asia's continuing economic rise has led to the growth in paper consumption, which in turn has driven an increase in demand for Kraft pulp in recent years. With its strategically located manufacturing bases, APRIL is well positioned to take advantage of this high-growth segment. Coupled with an increasing industry appetite for sustainable supplies of BAKP (Bleached Acacia Kraft Pulp), as well as a favorable foreign exchange rate, its pulp sales grew by 15.6%, with market pulp volume increasing to 1.65 million tons in 2005 from 1.62 million tons in 2004.

Asia accounted for more than 80% of APRIL's sales volume in 2005, a marked increase from the 75% share of Asian sales in 2004. More notably, the company successfully grew the key markets of China and Korea, capturing significantly increased market shares in both countries: more than 20% in China and about 30% in Korea. The operations in Riau generated pulp production volume exceeding 1.9 million tons. Some 1.65 million tons were sold to APRIL's customers as market pulp and the remaining volume was used for the company's own paper production.

In 2004 and 2005, APRIL made significant headway in developing the market for acacia pulp, which increased its sales by 35% in 2005 alone. The expansion of the market was being helped by the growth of the digital print market which increased demand for higher resolution and quality color printing. With its unique fiber morphology, acacia pulp exhibits superior surface qualities compared to other hardwood pulp, making it an ideal raw material for printing paper. Acacia is now also recognized as one of the best choices for tissue as it is softer than other fibers.

The market for pulp continued to see major structural changes in 2004 to 2005. Older mills in the Northern Hemisphere increasingly failed to compete with the more cost-effective manufacturers in Asia and South America. While cost competitiveness is a key deciding factor, APRIL is increasingly conscious of customer awareness and concern with sustainability issues. APRIL recognizes that in markets where a commitment to environmental responsibility is fostered at the government level, customers want to be assured of relevant external standards practiced by their suppliers. Hence the company believes that its commitment to sustainability, and the standards it adheres to, will provide a point of differentiation and competitive edge to its business operations.

Paper Business Review

Propelled by sustained GDP growth across the region and increased consumption in China and India, Asia also played a significant role in advancing the paper business. It is predicted that

within 10 years Asia, including Japan, will be as big a market as the US and Europe combined.

On a global scale, Asia represented a third of the worldwide demand for writing and printing paper in 2005. APRIL therefore focused its efforts on growing key markets in the region. As a result, sales volume of uncoated wood free (UWF) paper grew by 9% to reach 379,861 tons. The Asian market accounted for more than 64% of this volume in 2005, up from 56% in 2004.

One of the driving factors behind the strong performance of the paper business was the sales growth of its value-added products, folio and cut-size, which posted a volume of 293,397 tons or a 9% increase over the 2004 volume. Most notably, PaperOne, the company's flagship brand, saw demand climb by 17% in 2006 to reach 107,579 tons. This premium brand of office paper, which is made from 100% plantation fiber, currently sells in more than 50 economies and continues to enjoy growing demand. Its strong market performance reflects the product's superior quality and the increasing market preference for responsibly produced paper.

In 2005, APRIL continued to fulfill the demand for environmentally responsible, quality fine paper by delivering only products that were certified to be made from plantation fiber to markets that included Japan, Europe, Australia and the United States. The company was also recognized as having production methods with the most technologically advanced and environmentally efficient processes, especially when compared with generally older mill operations in the Northern Hemisphere.

With predicted average growth rates of 4% in printing and writing paper demand in Asia over the next four years, APRIL believes it is in a position to harness this opportunity through its reliable and environmentally sound production capability.

Opportunities and Challenges for APRIL in the Supply Chain

As a player in the global market, APRIL is very conscious that its customers also face pressures from their stakeholders to buy only 'green' products, and greening the supply chain is a critical issue that is challenging but at the same time opening opportunities for a company like APRIL. Therefore APRIL is very serious about being a green company, producing only green products, and at the same time enforcing the same concept among its suppliers. This commitment explains why APRIL is passionate about doing the right things right, and communicating this to all the stakeholders.

Challenges to APRIL as Supplier

As supplier of pulp and paper products, APRIL faces the following basic challenges:

- 1. The general perception of overseas buyers that Indonesia is an economy where the government does not care for the protection of its forest resources, and where business players behave irresponsibly towards the environment.** Indonesia is known for its lack of protection of the economy's rich forest resources from illegal logging and other threats which have destroyed ecologically valuable forests and compromised the development potential of communities. The World Bank estimated that if this condition remained unabated, irreversible damage to the environment and the people of Indonesia would take place in 2005.

A 2005 qualitative perception study conducted by an independent PR consultant, Edelman-Melbourne, among Australian stakeholders highlighted the cynicism that still existed towards environmental initiatives promoted by the Indonesian pulp and paper industry (“From time to time we’ll have a customer cancel an order of paper because it came from Indonesia”), though a considerable proportion of those interviewed conceded that external certification of environmental practices was having a positive impact. (“Finally the Indonesian industry realizes that to compete on a truly global scale it needs to be competitive in environmental as well as quality and pricing standards.”)

APRIL recognizes that in markets where a commitment to environmental responsibility is fostered at the government level, customers particularly want to be assured that the relevant external standards are practiced by their suppliers. While this poses as a challenge to the company, APRIL believes that by behaving responsibly, it can be an opportunity to develop a competitive edge. The company’s commitment to sustainability and adherence to standards will continue to provide a point of differentiation which will in turn benefit the economy and the people of Riau.

2. The need to acquire the Forest Stewardship Council (FSC) certification, which is required by a number of global customers (e.g. five out of 50 buyers in the Japan market) and regarded by APRIL Sales/Marketing Director for Paper as a trade barrier. As it is now, it seems impossible to get the FSC certification because one of the criteria is exclusion of all plantations established in areas converted after November 1994. Majority of APRIL’s plantations do not meet this criterion.

It is widely accepted that forest resources and associated lands should be managed to meet the social, economic, ecological, cultural and spiritual needs of present and future generations. Because of the growing public awareness of forest destruction and degradation, consumers demand that their purchases of wood and other forest products should not contribute to the destruction of forest resources, but instead help secure these for the future. In response to this concern, certification and self-certification programs of wood products have proliferated. In all cases, the process of certification is initiated voluntarily by forest owners and managers who request the services of a certifying organization.

The Forest Stewardship Council (FSC) is an international body which aims to promote environmentally responsible, socially beneficial and economically viable management of the world's forests, by establishing a worldwide standard of recognized and respected Principles of Forest Stewardship. The FSC accredits certification organizations in order to guarantee the authenticity of their claims.

The scale and intensity of forest management operations, the uniqueness of the affected resources, and the relative ecological fragility of the forest are considered in all certification assessments. Differences and difficulty in interpretation of the principles and criteria are to be addressed in national and local forest stewardship standards. These standards are to be developed in each country or region involved, and will be evaluated for purposes of certification, by certifiers and other affected parties on a case to case basis. If necessary, FSC dispute resolution mechanisms may also be called upon during the course of assessment.

The FSC trademark provides international recognition to organizations which support the growth of responsible forest management. Its product label allows consumers to recognize products that support the growth of responsible forest management worldwide. Over the past 12 years, over 84 million hectares in more than 82 economies have been certified according to FSC standards while several thousand products are produced using FSC certified wood with the FSC trademark. FSC operates through its network of National Initiatives in 40 economies.

To overcome this stumbling block, APRIL has been actively seeking accreditation from LEI (Lembaga Ekolabel Indonesia or Indonesian Eco Labeling Institute). Since 2004, the company has started the Certification Support Program (CSP) under the QUALIFOR Program of SGS (Societe Generale de Surveillance) using FSC principles and criteria.

Opportunities for APRIL as Supplier

The following opportunities are presented to APRIL as supplier:

1. Secure and faster supply because the fiber comes from their own plantations and those of their partners. APRIL fiber plantations are located in Riau province, Sumatra, Indonesia. The plantations are in government land concessions granted for a period of 35 years plus one cycle of 326,340 hectares gross with a net plantable area (HTI) of 198,871 hectares as of June 2006. Additional plantations are obtained through joint ventures and joint operations (JV/JO) and community fiber farms (*HTR-Hutan Tanaman Rakyat*). Total accumulated net plantable area is 360,057 hectares, about 76% of which had already been planted.

2. Compared to European plantations, APRIL plantations in Indonesia with its tropical climate, have more favourable production conditions and shorter production cycle (yielding harvest at a much shorter turnover). The acacia plantations in areas around the equator such as Indonesia has a much lower turnover harvesting cycle (originally seven years), compared to pine plantations located in 4-season economies which need 30 years. The continuous research and development done at RAPP has even resulted in seeds which only take six years to harvest. This is definitely a significant competitive advantage for APRIL.

3. APRIL's mills are relatively new and very modern, hence highly efficient compared to the older mills in the Northern hemisphere which are mostly over 20 years old. APRIL's integrated pulp and paper mills at RAPP in Riau are benchmarked against the world's best. They have world class manufacturing facilities and practice clean and green production process. The modern, efficient mills at RAPP definitely contribute to cost efficiency. In addition, APRIL has the added advantage of having stable, secure and fast supply of raw materials for its mills since the plantations are company owned or partner owned.

Opportunities and Challenges for APRIL as Buyer

As a buyer of raw materials, one major opportunity presented to APRIL is the **development of HTR or Community Fiber Farms**. APRIL does not receive logs from third parties. To meet its fiber requirements, APRIL develops Joint Venture/Joint Operation and HTR partners in each of its fiber estates, which is possible under the Government of Indonesia Regulations. The well-established contractual arrangements with community partners provide the company a guaranteed supply of fibers. As of June 2006, APRIL had 61 HTR partners, including those located within APRIL's concessions.

On the other hand, controlling the HTR partners and combating illegal logging are the major challenges that APRIL is facing as a buyer.

Controlling the HTR partners. The HTR partners naturally are subject to strict checks from the company which makes sure that its supply chain is untainted. While the APRIL staff provide advice and support to the partners, this has not always been easy because most of these partners have been used to the "slash and burn" type of operations, which is irresponsible but is definitely much easier.

The company staff and partners are both expected to persuade the wider community to believe in the value of conserving and protecting the natural and planted forests.

Illegal logging. Illegal logging in Indonesia occurs in a number of ways which are: a) logging without a permit, where trees are extracted openly by small scale chainsaw gangs and large scale well-organized operations using heavy equipment; b) smallholder farming, where forest land is cleared for agriculture without the required permit and the timber sold in the black market; c) excessive logging of forest concession, meaning over-cutting of trees from forest concession meant for selective logging; and d) misuse of logging licenses, where trees are cut from areas other than designated cutting blocks both from government forest and company-owned plantations, including APRIL's.

APRIL realizes that illegal logging is one of the biggest threats to Sumatra's forest resources and is therefore very serious in combating the practice, which is probably the biggest challenge, because very often it is perceived by the local people as getting in the way of economic opportunities for them.

Greening the Supply Chain

Predictably, with Indonesia's reputation, the biggest pressure coming from APRIL customers are environment-related.

APRIL takes the environmental issue very seriously. The company believes that in Indonesia, leaving the forests alone is not an option since socio economic pressures would inevitably lead to their destruction over time. Through its operations and wider influence, APRIL has been working to protect the remaining high conservation value forest resources while developing renewable supplies of sustainable fiber to generate economic and social growth opportunities that the region needs and deserves. Likewise, APRIL is making sure that environmental related issues are also properly addressed in its manufacturing sector.

APRIL has pursued a number of initiatives to address the challenges and fulfill the requirements of the customer on greening the supply chain. The company believes that pursuing these initiatives would alter the buyers perception of Indonesian companies' irresponsible business practices.

APRIL as Supplier

A. Manufacturing Operations

APRIL's integrated pulp and paper mills at RAPP in Riau are benchmarked against the world's best. The company constantly improves its operations to ensure the health and safety of the employees and the surrounding communities. Optimizing the mill's environmental performance is also integral to its commitment to sustainability.

Approximately 90% of total energy produced in the power plant comes from black liquor, a bio-fuel by-product of the production process, and the balance comes primarily from wood bark and rejected wood chips with some coal and oil. The pulp and paper mills use the most advanced technology and processes. Both mills have been awarded ISO 9001:2000 certification for their quality management systems.

The power plant, pulp and paper mills have ISO 14001:2004 certification for their environmental management systems. Throughout the production process APRIL applies the 5R policy – reduce, recover, reuse, recycle, replace.

Environmental Management Rating

The Indonesian Ministry of Environment in its Satisfactory Compliance checks awarded APRIL mill operations the “Green Rating” for PROPER 2004-2005. This is a significant improvement over the “Blue Rating” obtained in 2002 and 2003. The rating system is given as part of the national Program for Pollution Control Evaluation and Rating (PROPER), a public reporting initiative implemented by the Indonesian government to promote compliance with environmental standards and strengthen transparency. Under PROPER, industrial firms are evaluated by the Ministry of Environment for their environmental performance on indicators like air emissions, waste water management, and solid wastes management. The results are given in the form of a five-color rating scheme-gold, green, blue, red and black – and reflect performance ranging from excellent to poor. The Green Rating indicates that the company’s mill performance is 50 percent above legal standards and that the mills use technology that is clean and green, minimizes wastes, prevents pollution, and conserves resources.

B. Fiber Operations

The Mosaic Plantation Concept

Indonesia’s highly diverse natural forests are shrinking at an extremely fast rate due to agricultural development, the establishment of all kinds of industrial plantations, and rural settlement. Since leaving the forests alone is not an option because of threats from illegal logging, forest fires, shifting agriculture, and poor forestry practices, the company strives to develop sustainably managed plantation forestry which increases forest productivity and eases pressure on the natural forests. APRIL is very serious in adopting the Mosaic Plantation Concept (MPC), and is committed to High Conservation Value Forest (HCVF) protection in plantation landscape, which it believes to be the best, if not the only way to stop forest degradation and loss in Indonesia.

The MPC is designed to integrate sustainable fiber production and environmental conservation while providing local communities with adequate natural forest (as source of timber and non-timber forest products and services) and land for livelihood. HCVFs are set aside to protect biodiversity and ecological and social values in plantation landscape. Under the MPC, the plantations are designed as integrated composites of fiber plantations, conservation areas, and community settlements. It incorporates fire prevention and control through the establishment of green buffer zones (e.g. riparian strips, greenbelts in the middle of the plantation and natural forest serving as wildlife corridors).

Acacia Ring Concept

Closely related to the MPC is the company's Acacia Ring Concept in which a ring of acacia is planted around the area of forest to be preserved to prevent encroachment by illegal loggers and the establishment of illegal plantations. It also provides employment to the local community. This innovative approach was first proposed to be applied in the Tesso Nilo forest complex to discourage elephants from invading nearby villages where crops may be damaged, villagers harmed and elephants slaughtered. APRIL was concerned, however, that the massive destruction in Tesso Nilo due to illegal logging and ‘slash-and-burn’ land-clearing would pose increasing

threat on the viability of the proposed Ring solution. The company has also proposed a similar approach in the Kampar Peninsula, a lowland area that has been targeted by illegal loggers and oil palm developers in recent years.

APRIL's strategy to manage forest resources by maintaining sustainable plantations balances commercial, environmental and social development needs. It focuses on the planet by conserving biodiversity and preventing environmental degradation; on the people by providing opportunities for social development and poverty alleviation; and on profit by ensuring a steady supply of renewable, high-quality and low-cost fiber. In developing well-managed mosaic plantations, the company can respond to the increasing fiber demand in Asia while enhancing and protecting the remaining HCV forests in Indonesia.

High Conservation Value Forest (HCVF) Protection

Within every fiber estate in its concessions, APRIL has delineated at least 20% conservation areas and has committed that no fiber should be sourced from these areas and none of them should be converted to plantation.

This complements APRIL's decision to adopt a policy for assessing and protecting HCVF in its concessions. As a first step in the implementation of this policy, during the third quarter of 2004, ProForest UK implemented a program to develop the company's technical and operational capability to conduct a full HCVF assessment. The guidelines and standards drawn up by ProForest followed the Indonesian HCVF Toolkit which was developed in 2003 by the Rainforest Alliance and ProForest. This in turn reflects the principles established by the Forest Stewardship Council (FSC) in 1999. After the training, the company formalized its commitment to identify, protect and manage HCVFs in its new concession areas within its Environment, Social, Health and Safety Policy.

By taking this step APRIL has become one of only two companies in the global pulp and paper industry to make a public commitment to protect HCVFs.

C. Control of Fire and Haze

To control fire and haze, APRIL adopted the following measures:

1. Greenbelts to help stop forest fires

The spate of forest and land fires in Riau demonstrated the importance of greenbelts in protecting fiber plantations by putting a break on raging fires.

In February 2005, a fire that started from the adjacent community, crossed over to the APRIL acacia plantation in Mandau Fiber Estate. The fire spread rapidly due to very dry and windy conditions brought about by a prolonged dry spell. The blaze was contained because of early detection and quick response by the Fire and Safety Teams and contractors. However, it was observed that the fire could have spread had there not been a 200-meter wide forested greenbelt to cut off the rapidly spreading three-meter high flames. The fire ran almost 1.5 km through an 8-month old acacia plantation before being stopped at the greenbelt. The shade and moist vegetation of the natural forest trees stopped the fire from spreading. This incident demonstrated how the greenbelt acted as a break, allowing fire-fighting teams to prioritize their fire suppression efforts on areas that were threatening the acacia plantation.

2. “No-Burn” Policy and Haze Prevention

APRIL has employed a ‘No Burn’ policy from the very outset of its operations and considers the slash and burn form of land-clearing as detrimental to the company’s operations. In developing its fiber plantation, the company uses only mechanical methods to prepare the land for planting because woody biomass provides a source of long-term soil nutrients and protects water quality. It also prevents mixing of the carbon from fire residues with the wood chips needed for pulp and paper production. Hence, APRIL plays its part in eliminating smoke/haze in Indonesia for the protection of air quality.

On 10 May 2006, with the endorsement of the Indonesian Government Ministries of Environment and Agriculture, APRIL and its partners, as well as other private companies in Riau, signed the Joint Declaration on Stopping Forest and Land Fires. This event was in response to the call of Indonesian President Susilo Bambang Yudhoyono to stop the “export of haze” during World Earth Day on 22 April 2006.

D. Conservation

APRIL readily accepts the responsibility to conserve as well as to develop its operations in an environmentally sustainable way. The company has taken major steps in earning external recognition for its conservation policies and practices and hopes to show others that it is possible to combine commercial considerations with the preservation of unique environments for future generations.

E. Sustainable Forest Management

In 2006 APRIL became the first and the only plantation forest company to attain certification under the Lembaga Ekolabel Indonesia (LEI) standards. The LEI is a multi-stakeholder body that comprises communities, NGOs, industry and eminent persons in Indonesia. Its certification standards are supported by the ITTO and other international organizations. This certification is expected to bring concrete assurance to the company’s customers that the fibers used in the manufacture of its pulp and paper products come from plantations that are nationally certified as sustainably managed.

This achievement affirms APRIL’s leadership position in sustainable plantation forest management in the region and brings it closer to its goal of international forest management certification. To address the insistence of certain buyers on FSC certification, APRIL is continuing with its Certification Support Program (CSP) on applicable FSC Principles, Criteria and Indicators with SGS which started in 2004. Its target completion date for the CSP is end 2008. Completion of the CSP-FSC will not entitle APRIL to a formal issuance of an FSC Certificate, though, because of FSC Principle 6.10 and 10.9 which allows only limited forest conversion (FSC 6.10) and no plantations developed after November 1994 (FSC 10.9) from forest conversion shall be qualified to be certified under FSC.

Nevertheless, despite the fact that no formal FSC certification will be issued to APRIL by completing the Certification Support Program (CSP)-FSC, APRIL keeps on implementing the program to benchmark its forest plantation management practices against the FSC standard and demonstrate that its forest plantation management practices satisfy FSC Principles & Criteria except FSC Principle 6.10 (contradicts Indonesian Government official policy on forest conversion) and FSC Principle 10.9 (which is just a date; not a performance criterion). Through these efforts APRIL expects to encourage the FSC to review its principle which disqualifies the company from fully pursuing FSC certification.

F. Embedding Sustainability Practices

In order to ensure that its commitment to sustainability should become firmly established within both culture and practice, APRIL adopted the Environmental, Social, Health and Safety Policy (ESHS Policy) in February 2005. The company determined that this policy should become the living expression of its commitment and therefore should be reviewed as knowledge and experience grow. The first revision of the policy was done in June 2005 when APRIL adopted the policy towards its HCVF commitment.

The ESHS Policy commits APRIL to the following:

- Creating national wealth and renewable raw material on land designated by the government for fiber plantation development; and supporting the government to reach and maintain favorable conservation status in the regions where it operates.
- Ensuring that only legal pulpwood enters its fiber flow and supporting the government's fight against illegal logging.
- Managing the concessions in a sustainable manner by applying the MPC to produce fiber, and to maintain or enhance representative natural ecosystem in the concession.
- Promoting and protecting the health, safety, and well-being of its employees, contractor personnel and the surrounding communities; continual improvement of Environmental, Social, Health and Safety performance; and achieving sustainable forest management certification.

Each aspect of the policy is supported by well-established practices and procedures which reflect external standards where applicable.

APRIL as Buyer

A. Fiber Sources

As stated before, APRIL does not receive logs from third parties. Instead it develops fiber farms with local community farmers as partners which will supply the needed fibers to the company, hence making sure its supply chain is untainted. And the partners undergo strict control from the company as elaborated underneath.

Community Fiber Farms (HTR)

APRIL has well-established contractual arrangements with community partners in each of its fiber estates. Aside from providing the company with a guaranteed supply of fiber through these partnerships, the communities also become self-reliant through the management of their own fiber farms. APRIL plantation staff provide advice and support and, with the partners, help to persuade a wider community of the value in conserving and protecting the natural and planted forests.

As of June 2006, APRIL had 61 HTR partners, including those which are located within its concessions.

B. Acacia Chain-of-Custody (CoC)

APRIL has implemented the Acacia Chain-of-Custody (CoC) System since 2004 to monitor, trace, document, and independently verify the flow of acacia fiber into its mill operations. The Acacia

CoC System is consistent with its Wood Purchase Policy which is part of the overall Wood Tracking System, established to prevent illegal pulpwood from entering its supply chain.

As a further step in this direction, APRIL commissioned Rainforest Alliance Smartwood Program to carry out FSC CoC and Controlled Wood assessment. Started in late 2005, the assessment is now in progress for fiber and mill sectors.

C. Pulpwood Legal Tracking System

To ensure that all pulpwood coming from JV/JO and HTR has come from an approved source, APRIL has a Legal Wood Tracking System to verify legal source and origins. It uses a mechanism called Request for Contract (RFC), serving both as an application form for a pulpwood supply contract with the company and as a verification document to evaluate the application. Both documentary and field inspections are carried out to determine that suppliers have complied with all the legal requirements and APRIL's policy.

In November 2005, the company incorporated new requirements into the RFC system in line with the HCVF and the FSC standards relating to non-FSC certified controlled wood entering the supply chain. Under these new requirements, APRIL will not accept any wood from identified and delineated HCVFs. In addition, the company will not source any wood harvested from any of the following FSC source categories:

- Wood from forest areas that violate traditional or civil rights
- Wood from non-FSC certified forest areas that have High Conservation Value (HCV)
- Wood from genetically modified trees
- Wood illegally harvested
- Wood harvested from areas which have been converted from natural forest to plantations which are inconsistent with government-approved land use plans

The third Wood Tracking Audit was carried out by SGS in February 2006. In addition to the normal audit, SGS conducted diagnostic steps towards eventually assimilating FSC controlled Wood Standard into the Wood Tracking System. APRIL wanted the February 2006 SGS Audit to verify its compliance with the FSC Controlled Wood standard, in addition to checking existing standards and procedures. While noting some corrective actions, SGS concluded that the company was moving towards compliance with the FSC Controlled Wood standard. A formal audit on FSC CW had since been implemented with Smartwood and APRIL is awaiting the assessment result from the certification body.

D. Combating Illegal Logging

APRIL realizes that illegal logging is one of the biggest threats to Sumatra forest resources. The best hope to conserve Sumatra's forest resources depends on sustainable forest management, which protects environmental values while generating social development opportunities for the local people.

Apart from its own unceasing efforts to stop illegal logging in its concessions and to secure the integrity of its fiber supply against illegitimate sources, APRIL has been actively participating in multi-stakeholder initiatives to identify preventive initiatives. The company realizes that it cannot halt illegal logging on its own and needs support from law enforcement authorities. APRIL also continues to develop relationships with other key stakeholders and further strengthen its collaboration with WWF.

Taking the matter beyond the discussion halls, in 2005 APRIL carried out a series of security actions against illegal logging along the Ukui-Gondai Access Road, located on the eastern boundary of the Tesso Nilo Forest in Riau. Working together with the Task Force that includes WWF Indonesia and concerned government authorities, strategic checkpoints and composite patrols were organized, reinforced by the blocking or cutting off of access roads used by illegal loggers.

Despite protests and even threats of force against the company, APRIL remains firm in its resolve to help combat illegal logging in the areas over which the company has responsibility. APRIL understands that economic necessity generally underlies the proliferation of this illegal activity. However, through the company operations, APRIL generates 35 direct and indirect jobs for every 100 hectares managed. These provide a legitimate livelihood option to people who might otherwise engage in illegal logging.

CSR in APRIL

APRIL is one of the few companies in Indonesia where CSR is already built into the company strategy, and APRIL has earned recognition and awards from various institution for its various CSR programs, the most recent one being the “Asian CSR Award of Excellence in Poverty Alleviation” granted to RAPP (the production arm of APRIL) by the Asian Forum on CSR 2007 in Ho Chi Minh City held in September 2007. RAPP is also the first and only Indonesian company accepted as member of the World Business Council for Sustainable Development in 2007. While greening the supply chain might be the obvious strategy for the sustainability of the company, APRIL has gone way beyond. For APRIL, CSR is the way of doing business, since it believes in the inseparable values of people, planet and profit.

The company’s commitment to sustainability has been reflected in various CSR programs of nature conservation mentioned above such as fire and haze prevention, combating illegal logging, and clean and green production process intended for greening the supply chain (planet-related). The profit-related elements are implemented by doing business responsibly and practicing good corporate governance. The people-related CSR initiatives are reflected in the wide-reaching community development programs and other programs discussed below.

CECOM Programs

APRIL believes that the natural partner to the development of sustainable forestry is the creation of a commercial environment in which the local community can also prosper. This continues to be the principal objective of its community development program which encourages self-empowerment by developing skills and a livelihood base that are self-sustaining

To develop self-sufficient communities through partnerships between the company and the local government, universities and non-governmental organizations, the program focuses on:

- transferring skills to local people to enable them to be self-sufficient and develop at a pace they can handle;
- contributing to social infrastructure development; and
- participating in fostering good governance in newly formed local district government units.

APRIL used to implement its massive CD program on its own, employing over 100 CD officers as facilitators. To create a positive impact on the broader community for future generations, the company established in July 2005 CECOM (Care and Beneficiaries of APRIL CD Program Empowerment for Community), an independent local foundation and non-profit organization, created to enable its programs to grow beyond their own capabilities by allowing partnerships and involvement with other parties.

APRIL will eventually turn over responsibility for relevant programs to CECOM. It currently provides the funding, management and human resource to enable CECOM to become self-functioning. This move was also made to distinguish between forestry and non-forestry related support by being open to those partnerships that, while generating value for the community, are also integral to its business. Over time, CECOM is expected to make the community understand the benefit of properly managing local resources and developing locally based, vibrant economies. Likewise, CECOM will encourage greater partnership and participation between employers and the community to train and develop the skills of the local workforce.

CECOM programs include the Integrated Farming System (IFS) which offers training on horticulture and livestock rearing, freshwater fish farming, composting and waste recycling, and food processing in four training centers in Riau. The farmers are also given cattle and/or fish, fertilizer, seeds and pesticides. They will in turn conduct the training in their respective villages, and this strategy has significantly increased the number of IFS farmers to 3,819 in 99 villages in 2006.

Another program is Support for SME Entrepreneurship, which APRIL helped to establish for SMEs in areas not related to its business-ranging from tailoring, weaving, beauty salons and bakeries to a motorcycle workshop, dynamo rewinding, brick making, and bee honey production. The individuals starting these new businesses join APRIL's Vocational Training Program, which is another program that CECOM implements under Capacity Building.

APRIL also has various social and infrastructure programs, educational and sport programs, and religious and cultural support programs in their CSR portfolio.

Community Involvement Program

Working in Partnership

The company continues to encourage the establishment of SMEs in lines of work directly applicable to its needs such as pallet production, plantation development, construction, landscaping, general supplier, and transportation. These business start-ups have the same access to advice and funding through the cooperative schemes with local banks facilitated by the company. By 2006, this particular program has created 1,300 jobs among 101 partners.

Community Fiber Farms (HTR)

APRIL's Community Fiber Farm Program develops unmanaged lands into acacia plantations through joint ventures with the villagers. The company provides start-up and technical support and offers villagers a 40% share in production on dry lands and a 30% share on lowlands. The scheme runs for up to six rotations, or approximately 40 years. By integrating Community Fiber Farms into its operations, farmers are given alternative means of livelihood other than illegal logging. As of June 2006, APRIL had a total of 61 HTR partners and some 26,000 hectares planted with acacia.

In 2005, APRIL's community programs received the Indonesian CSR Awards, Asian CSR Awards in Environment in Thailand and the Asian Forum on CSR Awards for its Community Fiber Farm program. The program was also cited as Best Practice in Social Program for all industries in the 2005 Asian CSR conference in Indonesia.

Conclusion

APRIL's business model (founded on the inseparable values of people, planet and profit) adopted in the supply chain, brings out the following learnings:

- In renewable resource industries like pulp and paper, stakeholder pressures are very real issues; to address them positively by greening the supply chain will provide significant competitive advantage to the company.
- Sustainability is key to long term profitability. It reinforces the company license to operate and expand, creates competitive edge for its products as it responds to a global market growing in environmental consciousness, and helps build trust that enables access to resources.
- Application of the triple bottom line concept in the industry by managing forest resources as sustainable plantations that harmonize commercial, social and environmental developmental needs:

Profit - Ensuring a steady supply of renewable, high quality and low cost internationally-competitive fiber, hence ensuring healthy profitable business;

People - Providing opportunities for social development and poverty alleviation; and

Planet - Conserving biodiversity and minimizing environmental degradation

is a winning strategy.

CSR and the Supply Chain: How a Japanese Sporting Goods Company has Successfully Engaged with International NGOs

Japan

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The case was developed with the cooperation of ASICS solely for educational purposes as a contribution to the Project entitled "New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective –" conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author(s) and the Asia Pacific Economic Cooperation. Names of individuals, organizations as well as figures are disguised.

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Executive Summary

This case tries to uncover two major management issues in global supply chain management. One issue was to obtain support from internal stakeholders which included management, shareholders, employees, factory managers and trading partners. The other issue was to develop trust among stakeholders outside the company such as international organizations, NGOs, unions, competitors and the press. In ASICS's case, both issues were unique for typical Japanese companies.

CSR concerns had become critical for most of the companies in Japan over the past several years, but these have been seldom treated as part of core management strategic themes. The issue discussed in the case shows how ASICS has incorporated CSR issues into its core management strategies and what the company's CSR team did to facilitate and implement the integration.

Likewise, ASICS faced a unique challenge from international NGOs. Japanese global companies are generally those in automobile and electronics industries. Because of their technology-focused operations, these companies' supply chains are more integrated than those of apparel and sporting goods companies like ASICS. Furthermore, these companies tend to own or control local factories through direct investment and/or ownership, thus they do not have similar labor and working environment issues in their supply chain that companies like ASICS have.

Since the early 1990s, labor scandals such as the so-called sweatshop issue had gained attention from all over the world. International NGOs like Oxfam, Amnesty and Global Union Organization were very actively engaged with the business sector. Nike, one of the first sporting goods brands which suffered from the sweatshop scandal, had to go through and overcome severe backlashes from those international NGOs and international organizations. Hence, ASICS was very careful when Play Fair at the Olympics Campaign approached the company in 2003.

ASICS was responsive and moved quickly to engage with the international campaign. Led by Mr Tanooka, the company's CSR team made great efforts to establish a working group in Japan together with its main competitor, Mizuno, and two Global Union organizations in Japan, UI Zensen and TWARO. These participating organizations frequently met and communicated with each other. The working group shared information related to the issue. After having interacted with the working group, UI Zensen and TWARO, led by Ms Akiko Gono, mediated between Japanese sporting companies and the campaign. The result has so far showed that neither ASICS nor Mizuno has been seriously attacked by the campaign or other international organizations.

Creating trust is a key success factor in engaging with both the internal and external stakeholders. Since the launch of the CSR team in June 2004, the team had focused on creating an environment where stakeholders could share necessary information as much as possible. Tanooka and the CSR team also concentrated on finding ways to integrate CSR value into the core management values, Quality, Cost and Delivery (QCD) which everybody in the organization knows and understands. If CSR becomes truly a part of the core management values like QCD+CSR, CSR issues can be easily communicated among the internal stakeholders and endorsed by them. If the internal stakeholders fully supported QCD+CSR, the CSR team could further strengthen the relationship with the external stakeholders.

At the time of writing this report, Tanooka and the CSR team have many things to do to achieve the QCD+CSR goal. However, the issues presented here have opened a way for the CSR team to reach their goal.

Case Study on ASICS and its Engagement with International NGOs

In the summer of 2003, Yoshizumi Tanooka received a letter mailed to ASICS's Europe office by Play Fair at the Olympics Campaign which puzzled him. The letter indicated that ASICS's footwear factory located in Indonesia abused and treated workers unfairly. Tanooka did not have any idea at all what it was all about – the factory in Indonesia nor Play Fair at the Olympics Campaign.

Tanooka was with the General Administration Department of ASICS and was in charge of monitoring the company's own factories in Japan and overseas, i.e. mainland China. Tanooka knew that there were international organizations conducting campaigns focusing on human rights and labor conditions which had gotten very aggressive as the summer Olympics in Athens approached. In the past, similar campaigns targeted global brands such as Nike and Adidas, forcing these companies to disclose their subcontractor factories in developing economies in their CSR report.

Tanooka initially decided to be quiet about the inquiry from Play Fair since ASICS did not have any subcontracting relationship with local footwear factories in Indonesia. However, Clean Clothes Campaign, one of the three global organizations which made up Play Fair Alliance and which was based in the Netherlands, pressured ASICS to respond to the inquiry. The other two organizations under the alliance were Global Unions and Oxfam International. The Play Fair at the Olympics campaign is one of the biggest ever mobilization campaigns against abusive labor conditions. Hundreds of organizations and many top athletes have participated in over 35 economies and more than half a million signatures have been collected in support of the campaign before the Olympics Games in Athens. Over 500 local campaign events have been organized and this has helped contribute to its extensive television, radio and press coverage in the press all over the world.¹

Tanooka decided to find out what was happening in the company's supply chain overseas. He thought that there might have been something going on in the supply chain which he was not aware of because some of the overseas consignment relationships were developed by Japanese trading companies. Hence it was difficult to know everything that happened in the company's supply chain.

Tanooka and his staff spent several months studying the company's supply chain. Finally, Tanooka was ready to respond to Play Fair at the Olympics Campaign but this proved to be too late. The Play Fair Alliance was already in the process of publishing its campaign report which included the possible abuse at the factory in Indonesia. The Play Fair Alliance published the report in March 2004 and this triggered a lot of E-mails sent to the president of ASICS criticizing ASICS wrongdoing in Indonesia. Between March and May 2004, Tanooka who arranged that this type of communication be sent to him instead, received more than 2,500 E-mails complaining about the situation in Indonesia.

Tanooka was shocked at how big and serious the relationship with the international organizations was. As a manager in charge of such corporate activities, Tanooka wanted to know:

- What relationship ASICS should develop and how it should communicate with international NGOs and other international organizations
- How he could get senior management involved in the process

¹ Please see The Play Fair Campaign website: <http://www.fairolympics.org/index.html>.

- Whether the company should create a team or group dedicated to global supply chain management
- Whether ASICS should engage alone or partner with other Japanese companies in the sporting goods industry
- How he could integrate this effort into the business objectives and get support from the rest of the organization

Tanooka was facing challenges that were very new to the company and perhaps to most of the Japanese companies. He had to move quickly but cautiously to tackle them.

Introduction

Founded in 1949 as Onitsuka Company Limited, ASICS Corporation (ASICS) has led the sporting goods industry in Japan and is now one of the leading sporting goods brands in the world. As a premiere Japanese sporting goods company, ASICS became a main product supplier for baseball stars like Ichiro Suzuki and many Olympics athletes, and thus its brand recognition grew dramatically in the global market. In addition to its world brand recognition, the company is also well-known for producing and marketing sporting goods in Japan and other parts of the world. Thus, unlike Nike which is mainly a marketing-oriented company, ASICS produces and at the same time markets sporting goods.

According to the company website, the company is now listed on the first section of Tokyo and Osaka Stock Exchanges. On a consolidated basis, ASICS employed more than 4,230 people and generated revenues of JPY194.5 billion as of 31 March 2007. Headquartered in Kobe, Hyogo, the company has main branches in Tokyo and Osaka and three local sales offices in Japan. It has 15 subsidiary companies in Japan and 19 companies overseas.

Since its brand and business operations have become global, more than half of ASICS's sales came from overseas operations. As of 31 March 2007, some 56.5% or JPY 113.1 billion (excluding the inter-segment sales) of the company's annual sales came from overseas and the rest, or JPY 81.4 billion, came from domestic sales. Major international sporting events such as the Winter Olympics and the FIFA World Cup Soccer in 2006 as well as marathon races around the world further increased ASICS's sales. Its overall operating income was JPY16.4 billion consisting of JPY3.9 billion, or 23.7% from domestic sales and JPY12.5 billion or 76.3% from overseas sales.

In addition to sales and marketing, ASICS is also into manufacturing. The company owns and operates factories in Japan and overseas, but it also consigns production capacity to factories overseas, mainly in China. Subcontractor factories in China are playing a pivotal role in the company's footwear business.

As a global company and a main product supplier, ASICS has successfully recruited top athletes like Ichiro Suzuki and leading marathon runners as product endorsers. In addition to its main brand, ASICS, the company has more than a dozen sporting goods brands for different market segments, ranging from kids to seniors, which have also gained worldwide popularity.

Business Goals

In Europe, Japan and the US, the populations are aging and more people have become health conscious. Starting as city marathons in major metropolitan cities in the world, running and jogging have become popular daily exercises. Demand for running and jogging shoes is increasing worldwide. In addition, Japanese athletes who had been associated with ASICS have joined overseas professional leagues and played very well in major competitions. This has enhanced ASICS reputation as a product supplier for the sporting goods market.

The company's business performance has been positive and it is expected that the company will continue to do well in the coming year with the start of the Olympics in Beijing and with more Japanese athletes playing in the global markets. ASICS brand and the other brands under the company have been increasingly well-received in major markets around the world. Based on its strong business forecast and its brand recognition, ASICS sets its sales target at JPY300 billion (US\$ 2.61 billion²) by 2010, which is roughly a 50% increase from the sales in FY2007 of JPY194.5 billion. This is an aggressive goal.

Planning, Manufacturing and Sales and Marketing are the company's three core business functions having their main focus areas, Quality, Cost and Delivery (QCD). If ASICS positions well in each of these three focus areas, the company is likely to meet the sales target. However, it is not an easy task.

Tanooka knew how hard the competition worked to keep up their QCD because he was facing a different force from different stakeholders that the company did not engage proactively. Producing high quality goods with less cost had been the company's main focus and many of Tanooka's colleagues in Planning, Manufacturing and Sales and Marketing believed the same thing. However, Tanooka also believed that ASICS had to take care of working conditions and labor rights at local factories, even though they were just subcontractors. If ASICS were reluctant in allowing the local workers to exercise their labor rights, it would be unlikely that the company would meet the expectations of the core business people.

Consumer preferences were changing quickly and frequently. Sporting goods brands had to accommodate such changing needs and wants. Most of the customers did not really care who actually produced the shoes or T-shirts or how bad their working conditions were.

Sporting brand companies like ASICS needed to deliver goods that satisfied consumer needs and wants as well as produce goods in a way that meets local workers' needs and wants.

CSR Team

The ASICS CSR Team was officially launched in June 2004. As the manager of the team, Tanooka has been leading the team since then. Although the launching of the CSR team was synchronized with the Play Fair Alliance, the company wanted to develop a group of employees who would dedicate their time and resources to CSR issues, especially global supply chain management. Tanooka's team was initially placed under the General Administration Department but was later on moved to the Legal Department. Under the General Administration Department, the CSR team inspected ASICS local and foreign factories; with the Legal Department, the team worked on implementing guidelines and policies to be shared with the entire organization.

² FX rate (JPY/US\$) = JPY115 per dollar.

When the CSR team was formed, Tanooka assigned two staff members to oversee supply chain management.³ Tanooka learned that the company's main rival, Mizuno Corporation also received a similar inquiry from the Play Fair Alliance. Thus, the CSR team asked Mizuno to work with ASICS and represent Japanese sporting brands in addressing the issue posed by Play Fair Alliance.

Aside from Mizuno, the CSR team also approached non-government organizations like the Japanese Federation of Textile, Chemical, Food, Commercial, Service and General Workers' Union (UI Zensen), International Textile, Garment & Leather Workers' Federation (ITGLWF) and ITGLWF's regional office in Asia and Pacific (TWARO). UI Zensen and TWARO were members of Global Unions, and Ms Akiko Gono represented the two organizations in Japan. She was willing to support ASICS and other Japanese companies in improving their CSR activities to include allowing labor unions in their factories.

The CSR team organized meetings and conferences among these stakeholders and presented to them how Japanese sporting brands worked with local subcontracting factories and what their labor rights policies were.

Engagement with NGOs

Play Fair at the Olympics Campaign (Play Fair Alliance) was initiated and run by three strong NGO organizations: Clean Clothes Campaign, Global Unions and Oxfam International. Clean Clothes Campaign first approached the Europe office of ASICS to inform the company that its local staff discovered that there were some labor abuses at a factory manufacturing sporting goods for ASICS in Indonesia. They informed the ASICS's European office that they were going to campaign against the company unless ASICS responded to the issue.

Tanooka did not know how to respond to the issue because ASICS at that time had no relationship with any local footwear factory in Indonesia. Before the CSR team was officially formed, Tanooka and his team had monitored factories that ASICS had relationship with on product quality, as well as working conditions including safety and training, on a regular basis. He was therefore shocked that labor abuses were allegedly committed by ASICS factories.

After a thorough investigation of the issue, Tanooka figured it out. The factory in Indonesia cited in Play Fair's letter was manufacturing counterfeit goods of brand companies like ASICS. While it was obvious that the factory produced fake products, Play Fair Alliance did not respond as Tanooka expected. It turned out that this was because Oxfam Australia replaced Clean Clothes Campaign as the main organization assigned to deal with ASICS because Oxfam Australia was the expert on labor rights issues in the Asia Pacific region.

Play Fair Alliance thought that they had not received a satisfactory reply from ASICS when the Campaign was about to publish their campaign activities. Play Fair Alliance published the campaign activity report in March 2004. The report concluded that ASICS committed labor abuses at its local footwear factory in Indonesia and that ASICS did not respond to the issue seriously. Because of the publication of the report, more than 2500 E-mails from around the world were sent to Tanooka for the next three months, citing ASICS alleged involvement in the incident in Indonesia.

³ As of August 2007, Tanooka assigned Mr Koji Takiyama, Mr Toshiaki Kawasaki and Ms Seiko Inoue to oversee the supply chain management in CSR team.

Tanooka found out that Mizuno, a key competitor of ASICS was also facing the same issue from Play Fair Alliance. Through Tanooka's efforts, Mizuno agreed to work with ASICS to address the issue and continue to do so if necessary. Tanooka felt that ASICS and Mizuno had to represent Japanese sporting brands in order to show how well Japanese companies had been working with local factories. He also arranged to communicate directly with Oxfam Australia and later on invited other NGOs like Oxfam Japan, TWARO, and UI Zensen to a meeting where they discussed the issues confronting companies like ASICS and Mizuno.

Management Involvement

Management involvement was one aspect that the CSR team had to hurdle at that time because they themselves were not very familiar with the workings of so-called activist organizations like Play Fair Alliance which did not seem to be legitimate organizations. Greenpeace was the only activist legitimate organization that they were aware of. Therefore, Tanooka did not have any idea at first how to handle the letter from Play Fair at the Olympics Campaign.

Tanooka later on learned that there were many different types of organizations among NGOs, from activist NGOs to yoga NPOs (People's Organizations). He also learned that Play Fair Alliance had its own track record and its objective was not entirely extreme; some of their assertions were legitimate and appropriate.

Despite Tanooka's deeper understanding of NGOs, he found it difficult to make the company's management understand what the NGOs were doing and who they were. Management did not have any clue why ASICS needed to pay attention to these organizations and how seriously the company had to relate with them. It was the CSR team which made the management understand the nature of international NGOs like Oxfam Australia and how important it was for ASICS to relate with them.

In order to obtain buy-ins from the management, the CSR team deliberately developed relationship with the international organizations and informed the management of every development, from minor events to critical issues, that arose with these relationships. The management now understands who they are and what they are doing, as well as why they are critical for ASICS. It was a very important step for the company to seriously consider its relationship with these NGOs which, in the past, were considered outsiders in the world of business. Tanooka now believes that the management counts on his experience and relationship with these international NGOs.

Organizational Support

Organizational support was another hurdle that the CSR team had to overcome. There was no simple way of estimating the risk to the company that Tanooka and the CSR team were trying to address. Therefore, there was no proof that the engagement with the stakeholders in the company's value chain deserved to be prioritized by the company. While it was true that the importance of the stakeholder engagement was seriously regarded by ASICS since the Athens Olympics and the Germany World Cup soccer were critical for the company's business, it was also true that its global sales continued to increase, even without paying attention to this concern.

Because of competition in the sporting goods industry and rapidly changing customer preferences, QCD (Quality, Cost and Delivery) was the focal point of the company's strategy. Tanooka's problem was how the CSR risk could be incorporated into the strategy or how CSR could be considered as equally important to QCD by ASICS's employees. Not only was CSR a new concept for the employees, but the stakeholders such as Play Fair Alliance and Oxfam were also very new to them. They had no idea why the company should care about these stakeholders when they were not part of the company's value chain at all.

As an ASICS veteran manager for 20 years, Tanooka was certain that the employees would not easily understand what was happening and what impact it would have on the company, its value chain or its customers. He and his team had to come up with solutions to tackle employees' attitude step by step. For the management, the employees as a whole and even to Tanooka himself, the attack on Nike and Adidas by the above-cited international NGOs was fire on the other side of the river. They did not realize that ASICS was a leading global brand in the sporting goods industry, which means that the brand had become a potential subject of any negative campaign by outsiders or activists who were on the look-out for well-known brands to lend more impact to their campaigns.

How the CSR Team Responded to the Challenges

What relationship ASICS should develop and how it should communicate with international organizations like NGOs

The CSR team was organized in June 2004. When the issue with the Play Fair Campaign cropped up, the company had already been discussing the organization of the CSR team within the company's Legal Department. Regardless of CSR activity, the company wanted to set up an internal oversight capability for overseas factories. As ASICS business expanded globally, its supply chain had gotten global as well. The company had actively made a consignment contract with local factories, mainly in China, through trading companies and agencies. ASICS thought that it could monitor the volume, product quality and production time of the factories. Thus, in terms of its QCD, a function like an internal audit was necessary for the company to catch up with increasing demands in the global market.

However, after the Play Fair Alliance incident, the company found out that creating an internal audit function was not enough. What the company needed was a function that would take on not only an internal audit role but also a catalyst role, engaging with stakeholders such as NGOs and other interested parties.

At the same time that the CSR team was being organized, Tanooka and his team started dialogues with Play Fair Alliance, mainly with Oxfam Australia. Oftentimes, ASICS represented Japan in the dialogues. The company invited Mizuno and other Japanese sporting goods companies and TWARO which was representing factory workers. TWARO was part of the Global Unions but during the dialogues with ASICS, the organization served as an objective mediator. For example, in ASICS's dialogues, the negotiations were done between Japanese companies and the campaign representative, Oxfam Australia. While Japanese companies created jobs and hired workers in developing economies, the campaign promoted the quality of workers' life. Thus, TWARO which represented textile, garment and shoe workers, supported and joined the campaign group, and at the same time, tried to mediate between the group they represented and ASICS to come into an

acceptable solution to improve labor rights in developing economies. For Oxfam Australia, TWARO served as a reliable source of information on local issues.

ASICS's strategy to move the dialogues forward was to conduct them on a regular basis and allow active exchange of communication, with all Japanese companies such as Mizuno and others in the sporting goods sector, acting as one team, Team Japan. It was very important for Oxfam to know that Japanese companies were serious in addressing the issue. The involvement of TWARO in the dialogues and negotiations further contributed to their success.

Moreover, the company also conducted dialogues with factory workers. In July 2005, ITGLWF organized a symposium in Hanoi, Viet Nam where local factories and sporting goods brand companies discussed and consulted with each other on how they conducted business with local factories. By attending the symposium and small workshops in Viet Nam, the CSR team learned more about the factory workers and the issues and concerns affecting them.

ASICS's efforts were well-received by the team of negotiators. Ms. Akiko Gono, secretary of TWARO, pointed out that several Japanese companies including ASICS and Mizuno had been working hard on improving their supply chain management and actively engaging with local suppliers and international NGOs. She noted that it was time for the suppliers and unions to improve themselves. For example, some local suppliers as well as workers did not have knowledge of worker's rights due to lack of training. Thus, even though sporting brand companies like ASICS did not oppose the organization of trade unions among these workers, the suppliers for their part, were not ready to accept labor unions and were not aware of the pros and cons of having them in the company. Ms. Gono informed Tanooka and the CSR team that educating local suppliers was important in order to strengthen supply chains and make them transparent.

Ms. Gono also felt that international NGOs and other international organizations like ITGLWF and TWARO needed to strengthen themselves if they were to continue to be good partners with the business sector. In order to be credible counterpart to companies, ITGLWF and TWARO had to strengthen their affiliates in their organizing and research activities.

Lastly, Ms. Gono emphasized that international NGOs and organizations should respect the social norms in each society and culture. In order for TWARO as well as UI Zensen to act effectively, these organizations needed to understand how to deal with foreign companies. For instance, the Play Fair Campaign which was led by western organizations, tended to focus on attacking a target company and mounting large negative campaigns in the initial stage. The main purpose of such campaigns was to increase awareness concerning some social issues and to demand that companies should improve or change their ways of doing business. Hence, to be more effective, international NGOs and international organizations should respect social norms of the society where target companies conducted their main business.

How he could get senior management involved in the process

As mentioned earlier, a negative campaign was something that senior management could not understand at the start. Tanooka exerted a lot of effort to let senior management know that the issue was as important to the company as QCD. If left unattended, the issue could destroy corporate reputation or diminish its image just like what happened to Nike. Tanooka reported to his boss and senior management on a regular basis the status of the campaign, how the company has responded or should respond to it, as well as what similar activities in the industry were taking place especially among ASICS competitors, and how these companies were also responding.

Senior management reacted positively to the efforts of Tanooka and the CSR team. They finally appreciated the importance of the issue and fully supported the CSR team to take care of this issue in their role as catalyst. Tanooka and the CSR team had the full backing of senior management to hold meetings and attend conferences and symposia where Tanooka shared how the company worked with local factories and their employees.

Whether the company should create a team or group dedicated to global supply chain management

Launching the CSR team had been a pressing issue for the company. In order to keep QCD rolling and monitor CSR issues such as labor rights and working conditions at the same time, it was necessary to organize a CSR team. The functions of what was to become the CSR team were initially done by the General Administration Department where Tanooka belonged. However, since the issue with Play Fair Alliance highlighted the need to cover labor rights as well, the company decided to launch the CSR team within the Legal Department instead of General Administration.

One of the team's first tasks was to develop the company's Code of Conduct (see Appendix 2) and Corporate Policy of Engagement (see Appendix 3). This was done not only for the benefit of the employees of the company but for its subsidiaries and the other stakeholders, including factories and trading companies in ASICS supply chain. The team wanted to emphasize that ASICS had a Code of Conduct and Corporate Policy of Engagement which had to be strictly followed.

The development of the code and the policy sent a clear message to the employees that ASICS had become a company proactively taking care of labor rights and working conditions even in its overseas activities. The global supply chain is a key to the company's success in meeting its sales target of JPY300 billion in the short term.

Tanooka and his team actively promoted the Code among its local factories and trading companies which were also connected to some local factories through their business relationship. The CSR team visited local factories on a regular basis (e.g. once a year), and monitored the operations of local factories and their compliance with the working conditions standards established by the Code.

In addition, ASICS decided to join and partner with Fair Labor Association (FLA), "a nonprofit network which gets major footwear and clothing manufacturers to agree to disclose specific factory names, and where in the world their products are manufactured."⁴

According to the FLA website, "the FLA represents a multi-stakeholder coalition of companies, universities and NGOs. There are currently 20 leading brand-name companies participating in the FLA. These are Adidas AG, ASICS, Eddie Bauer, Drew Pearson Marketing, GEAR for Sports, Gildan Activewear, H&M, Liz Claiborne, Mountain Equipment Co-op (MEC), New Era Cap, Nordstrom, NIKE, Outdoor Cap, Patagonia, Phillips-Van Heusen, PUMA, Reebok, Top of the World, Twins Enterprise, and Zephyr Graf-X. These companies have committed to a rigorous program of Workplace Standards implementation, monitoring and remediation in order to bring their manufacturing sites into compliance with FLA standards." In addition, 194 colleges and universities have joined FLA.⁵

⁴ Please see FLA website: <http://www.fairlabor.org/all/about/index.html>.

⁵ Ibid.

By joining FLA, ASICS is expected to promote both the company's code of conduct as well as FLA's Code of Conduct (see Appendix 4). Moreover, FLA requires a participating company to report local factories and their addresses to FLA. As a third party auditor, FLA goes to local factories and investigate how the factories operate. ASICS believes that such a third party audit is effective and objective. However, as of now, ASICS has decided not to disclose the full information of their contract factories such as names and addresses to the public, but instead has given the information to FLA for them to monitor these factories.

The CSR team again started to promote FLA's code of conduct within the company and with local factories in its supply chain. By asking local factories and trading companies to follow FLA's code of conduct, ASICS has become more confident in its oversight of local factories and managing its reputation in the global supply chain.

Whether ASICS should engage alone or partner with other Japanese companies in the sporting good industry

In dealing with Play Fair Alliance, ASICS had to involve Mizuno, its rival company, and some other Japanese sporting brand companies. From ASICS's point of view, in such a campaign, ASICS or Mizuno was simply considered a Japanese brand or Japan as a whole. The Play Fair Campaign tended to claim that Japanese companies or Japan as a whole, did not respect labor rights at local factories. It became more of a national matter rather than an issue affecting a single company. ASICS thought that it would be a good idea to work together with other Japanese companies. Mizuno who had faced similar issues from Play Fair Alliance sympathized and cooperated with ASICS.

However, ASICS seemed to be the only Japanese company dealing with other international NGOs such as the FLA. During the time that ASICS was strengthening the CSR team and its internal audit capability, the company relied more on the third party audit done by FLA. The third party audit presented to the company an objective view of working conditions at local factories and uncovered other aspects of factory operations that the internal audit could not capture. Given the unpleasant responses from local factories, ASICS decided to disclose detailed information on the factories to FLA as basis for their inspection.

Among Japanese companies, ASICS pioneered in the global supply chain management which was being followed by many companies. The company hopes that it could persuade other companies to join FLA or similar third party auditors in the near future.

How he could integrate this effort into the business objectives and get support from the rest of the organization

Tanooka's strategy was to (1) have his staff regularly visit all the company's own factories and those with subcontracting arrangement with ASICS; (2) inform senior management of the latest status of the company's global supply chain activities and get management support; and (3) bring CSR to the level of QCD by getting the company's employees involved in CSR issues in the global supply chain.

In order to achieve these three objectives, Tanooka started to form a CSR team consisting of two staff who regularly visited local factories as part of internal audit. Tanooka also regularly reported to the management on the latest situation in the global supply chain, including stakeholder engagement with Oxfam Australia and FLA.

By being concerned with just QCD, the employees tended to overlook those who were actually working for the company and its products. QCD was centered on products and not the people who manufactured them. Tanooka believed that people management should be given the same importance as QCD for while it was important to focus on QCD to achieve the business goal, it was equally important for the company to take care of those who actually produced goods for the company. QCD plus CSR were what Tanooka and the CSR team had to promote.

The CSR team started to conduct internal training sessions to promote CSR among the entire corporate communities. The team also promoted the code of conduct of ASICS and FLA among representatives of trading companies. In February 2007, Tanooka successfully organized the first CSR session for employees and trading company representatives at the company headquarters. More than 80 people attended and learned ASICS's global supply chain management system and the company's efforts to improve CSR initiatives and working environment.

After ASICS's continuous efforts to promote the company's CSR and improve its supply chain management, Oxfam International agreed that there had been improvements in the company's supply chain. In 2006, Oxfam International published its research publication called *Offside* and mentioned that "Until a few years ago, ASICS had done very little to address labour rights in its supply chain but recently there have been a number of positive developments, including:

- ASICS's willingness to engage in dialogue with trade unions and NGOs and the company's interest in cooperating with these groups to ensure that workers receive labour rights training;
- ASICS's communication to its suppliers that it expects them to comply with international labour standards and the company's willingness to investigate violations and seek to remedy them; and
- ASICS's decision to submit part of its supply chain to the FLA's monitoring program."

Going Forward

Looking back at what they had gone through in this complex issue, Tanooka and the CSR team recognize that there are two important aspects that both make ASICS unique. One is that ASICS confronted this issue as a global social issue rather than a minor issue happening overseas. As described earlier, the ASICS's Europe office received the letter from the Play Fair at the Olympics campaign. The Europe office's interest in this issue was so strong that Tanooka and his team had to address it as a global issue. Hence, they had to pay attention to various stakeholders on a global basis. The CSR team believes that had the Europe office not received the letter of complaint, the results might have been quite different.

The other aspect is that there were just a few Japanese companies which were subjected to the global supply chain issues that confronted ASICS and Mizuno. This was because most Japanese brand manufacturers were in electronics and automobile production which required highly technical skills, thus production was mainly done in factories owned directly by a Japanese company. On the other hand, ASICS and Mizuno products did not require high technical skills from their workers. Sporting goods and apparel companies hired local factories to produce sporting goods and apparel products at the least cost and at the shortest possible time. Thus, corporate governance at the local factory level is quite different between an automobile factory owned by a Japanese company and a garments factory owned by a local subcontractor.

With these aspects in mind, Tanooka thinks that there are many things that the CSR team will have to work on. He believes that the company is ahead in supply chain management compared to the Japanese sporting goods industry and most of the Japanese companies. Thus he thinks that the company can continue to lead in the social aspects of CSR. However ASICS still has to incorporate more environmental considerations into its CSR practices to address the environmental aspects. The company is trying to promote recycling of used shoes at retail shops but as a manufacturing company, Tanooka believes that the company can do much more since the environmental issues are critical for the company's CSR project and its core business. He and the CSR team need to develop some innovative programs on the environment.

Likewise, the CSR team wants to inspect all company-owned factories and those of its regular subcontractors. While the team relies on the third party inspection by FLA, the team wants to have the same information internally. Having the information internally could create efficiency in the supply chain management as well as the company's business operations. Furthermore, the company itself is seriously considering lessening its dependence on its subcontractors in China and on its local suppliers which are mostly Chinese-owned. It is a serious business risk for ASICS to place a big portion of its business in the hands of just one source of supply. Hence, the company is now seriously considering a way to develop new suppliers and subcontracting networks outside China, thereby diversifying the global supply chain risk. In order to do so, it is critical for the team to observe and monitor all the factories that do business with ASICS and make routine internal audit of all factories in the near future.

Lastly, the team would like to make CSR part of ASICS's DNA. The team plans to organize for the entire organization a series of seminars and workshops to spread the concept of CSR and the company's CSR standards. Educating the employees is critical.

The Code of Conduct workshop in February 2007 helped employees understand what is happening around the company's core business. It is important to recognize how CSR relates to what employees are doing at work everyday. Such learning opportunities are critical for the company as a team to pursue certain objectives together. For example, ASICS has a concrete business goal to achieve JPY300 billion sales. In order to achieve this sales figure, it is necessary to produce high quality goods cheaply and market them as quickly as possible to meet the demands of the market. At the same time, it is equally important to know the process behind manufacturing, sales and profit making or who produces the products, how those products are made and how the workers are treated. Hence, process management is also people management. In the global supply chain management, these two management strategies must be incorporated. These will eventually have great impact on the company's core business.

Conclusion

Having celebrated the third anniversary of the launch of the CSR team in June 2007, Tanooka feels confident of what he and the CSR team have done for the past three years. When the CSR team was created, international NGOs and activist campaigns were totally foreign to him. However, he soon realized that these international NGOs were behind the attack on Nike and Adidas for having violated labor rights at the supplier and subcontractor levels. ASICS is a global brand company as well as a manufacturer, so its business model is somewhat different from that of Nike and Adidas. ASICS initially believed that the problem with Nike and Adidas was fire on the other side of the river. However, due to ASICS increasing global presence in the world's sportswear market, ASICS had become a likely target just like Nike and Adidas.

Tanooka believes that the CSR team has handled the said critical situation well by building a good stakeholder relationship with international organizations. By many accounts, ASICS is regarded as a leading Japanese brand in the global supply chain management. Tanooka himself is being invited to speak before college students and business professionals, among others. The CSR team has contributed to increasing ASICS brand further.

More importantly due to the efforts of the CSR team, ASICS feels confident in entering Viet Nam as an additional manufacturing location. The company's target of JPY300 billion by 2010 is very aggressive and cannot be achieved without having additional subcontracting factories overseas. Currently, the company's manufacturing capability is heavily concentrated in China and ASICS's management strongly feels the need to build up additional capacity outside China.

Having experienced the campaign by activist NGOs, Tanooka and the CSR team have learned how to handle similar campaigns in the future. The campaign should not be regarded as an enemy but also as a good teacher or instructor for the company, because the campaign often represents factory workers and local people in the area where the company has some relationship. Knowing what local workers want or need is very important for the company to do business in the area.

Usually, the campaign is formed by a group of organizations and each organization has its strength in certain issues. In this case, Oxfam Australia, ASICS counterparty has extensive network and wide-ranging experiences in Asia in terms of labor rights and working conditions. Tanooka has established a good relationship with the organization, so he knows what the company has to do after it launches a manufacturing capacity in Asian economies other than China.

As head of the 8-person staff of the CSR team, Tanooka believes that there are many other CSR activities that they have to implement other than the global supply chain management. Yet, for Tanooka, the CSR team and the company, the global supply chain management has been one of the most important CSR issues that the company faced and successfully hurdled. With the experience that they have gained, the CSR team continues to improve ASICS CSR practices and is now ready to address the other CSR issues.

**Appendix 1:
A Scene from Play Fair at the Olympics Campaign in Athens**



(Source: Play Fair at the Olympics Campaign in Athens Website
<http://www.fairolympics.org/countries/international.html>)

**Appendix 2:
ASICS Corporation Code of Conduct**

The 'ASICS CORPORATION Code of Conduct,' based on ASICS Vision and ASICS Principles (established in 2003), which set out the fundamental views of the management, aims to clarify the essence of a corporate conduct to be accepted and respected by all persons. The contents outline appropriate corporate behaviour as a Code of Conduct to be observed by each and every director, officer, auditor and employee of ASICS CORPORATION (hereinafter to be referred to as 'the Company') in accordance with their values, with corporate ethics and with the law.

ASICS CORPORATION Code of Conduct

1. Purport and scope of application

The 'ASICS CORPORATION Code of Conduct' (hereinafter to be referred to as 'the Code') outlines the principles that are to be complied with by all directors, officers and auditors of the Company (and those in similar positions) and all employees (hereinafter to be referred to collectively as 'we', 'our' or 'us') during the daily conducting of business. In observing these principles the said persons are to remain fully aware of the Company's social responsibilities and must act in accordance with all relevant laws and ordinances in all corporate activities, fully recognising that socially acceptable conduct is indispensable for the sound development of the Company.

2. Our basic stance

(1) In all of our corporate activities we shall comply with all relevant laws, ordinances, international rules and regulations and in-house regulations including the Code, to the letter and in spirit. We will endeavour to see to it that the corporate activities of the ASICS group are managed properly and that they are consistent with social ethics.

(2) We will respect the fundamental human rights of all persons in all of our corporate activities. We will not discriminate against individuals on the basis of their ethnic origin, race, nationality, religion, gender, age or any disability, nor will we impair their dignity.

(3) We believe in appropriate disclosure of information and will work to bring this about. We will maintain fair, just and transparent relations with anyone having an interest in the Company, and will conduct fair transactions.

(Courtesy of ASICS Corporation)

Appendix 3: ASICS Corporation Corporate Policy of Engagement

A. Objectives

1. ASICS expects all of its business partners, which include but are not limited to ASICS' suppliers and subcontractors ('ASICS Business Partners'), to operate their businesses in line with the principles set out in 'ASICS Vision', 'ASICS Philosophy' and the 'ASICS Code of Conduct'.
2. The purpose of this policy is to establish and to ensure that ASICS Business Partners comply with ASICS' policy regarding the minimum requirements relating to human rights, labour, health, safety and environmental issues at all facilities operated by ASICS Business Partners. This policy is based on ASICS Vision', 'ASICS Philosophy', the 'ASICS Code of Conduct' and the model Code of Conduct issued by the World Federation of the Sporting Goods Industry (WFSGI).
3. ASICS will assess all ASICS Business Partners on the basis of their compliance with this policy. As such, this policy is a tool that enables ASICS to select and retain ASICS Business Partners that follow business practices which are consistent with ASICS' policies and values.

B. Standards

ASICS expects ASICS Business Partners to run their businesses in accordance with the following standards:

1. General principle: ASICS Business Partners are to operate in full compliance with all national and local laws, rules and regulations as are applicable to their business operations.
2. Employment standards: As regards the employment of any and all employees of ASICS Business Partners ('Employees'), ASICS Business Partners are to comply with the following standards:
 - a) Forced Labour: ASICS Business partners shall not make use of forced labour, either in the form of prison labour, indentured labour, bonded labour, or any other form. No Employee can be compelled to work through force, the threat of force or intimidation of any kind.
 - b) Child labour: ASICS Business Partners shall not employ persons under the age of 15 (or 14 where employment at the age of 14 is permitted by the relevant laws), nor shall they employ persons who have not yet reached the age at which they should complete compulsory education in the country in which they are employed where such age is higher than 15.
 - c) Harassment or abuse: ASICS Business Partners must acknowledge that their Employees have the right to a workplace where there is no physical, sexual, psychological or verbal harassment or abuse and are to treat Employees with respect and dignity.
 - d) Discrimination: when employing or hiring, the salaries, benefits, promotion, training, discipline or conditions of termination or retirement offered by ASICS Business Partners shall not show any discrimination based on gender, race, religion, age, disability, sexual orientation, nationality, political opinion, or social or ethnic origin.
 - e) Right of association and collective bargaining: ASICS Business Partners shall recognize and respect the rights of Employees' to organise and join associations of their own choosing, and to bargain collectively.
 - f) Wages: ASICS Business Partners must recognise that Employees are to be fully remunerated for all time worked and must be provided with a clear written payslip showing details of their pay for each pay period. ASICS Business Partners shall pay Employees at least a) the minimum wage required by law or b) the prevailing industry wage, whichever is the higher. In addition to remuneration for regular hours of work, for overtime hours Employees are to be paid at least the premium rate required by law or, in those countries where such laws do not exist, a rate that exceeds the regular hourly rate.
 - g) Hours of work: including overtime, ASICS Business Partners shall not require their Employees to work more than sixty hours a week or the maximum working week established by the relevant law, whichever is shorter, on a regular basis. ASICS Business Partners are to give Employees at least one day off in every seven-day period on a regular basis and paid annual leave as required by the relevant law.
 - h) Benefits: ASICS Business Partners are to see to it that their Employees receive all legally mandated benefits.
 - i) Health and safety: ASICS Business Partners are to provide a safe and healthy working environment, which includes but is not limited to adequate lighting, heating and ventilation systems and protection from fire, accidents, and hazardous substances. ASICS Business Partners' Employees must have access to clean and adequate sanitary facilities at all times. Where residential facilities are provided for Employees, the same standards apply.

3. The environment: ASICS Business Partners are to comply with all applicable environmental legislation and regulations and must work to further improve environmental conservation. Furthermore, ASICS Business Partners are to run their businesses with due consideration for health and safety and the environment by saving resources and energy, reducing emissions, showing due concern for the environment when purchasing and by preventing pollution.

C. Publicity

ASICS Business Partners are to make every effort to ensure that their Employees understand this policy by informing Employees of this policy orally, and by distributing written copies of this policy, or by displaying this policy, translated into the local languages spoken by Employees, in a prominent place in the workplace.

D. Documentation and inspection

ASICS Business Partners are to maintain all documents necessary to demonstrate compliance with this policy and any applicable laws, and must submit these documents to ASICS upon request. Furthermore, ASICS has the right to conduct inspections or to have a designated independent inspector conduct such inspections with or without prior notice in order to ascertain that ASICS Business Partners are complying with ASICS standards and the applicable laws. ASICS Business Partners are obliged to accept such inspections.

E. Application of this policy to ASICS group companies

ASICS group companies are to operate their businesses in accordance with the principles set out in this policy.

(Courtesy of ASICS Corporation)

Website: <http://www.asicseurope.com/Sitewide/AboutUs/CorporatePolicyOfEngagement.htm>

**Appendix 4:
Fair Labor Association Code of Conduct**

Workplace Code of Conduct

Forced Labor There shall not be any use of forced labor, whether in the form of prison labor, indentured labor, bonded labor or otherwise.

Child Labor No person shall be employed at an age younger than 15 (or 14 where the law of the country of manufacture* allows) or younger than the age for completing compulsory education in the country of manufacture where such age is higher than 15.

Harassment or Abuse Every employee shall be treated with respect and dignity. No employee shall be subject to any physical, sexual, psychological or verbal harassment or abuse.

Nondiscrimination No person shall be subject to any discrimination in employment, including hiring, salary, benefits, advancement, discipline, termination or retirement, on the basis of gender, race, religion, age, disability, sexual orientation, nationality, political opinion, or social or ethnic origin.

Health and Safety Employers shall provide a safe and healthy working environment to prevent accidents and injury to health arising out of, linked with, or occurring in the course of work or as a result of the operation of employer facilities.

Freedom of Association and Collective Bargaining Employers shall recognize and respect the right of employees to freedom of association and collective bargaining.

Wages and Benefits Employers recognize that wages are essential to meeting employees' basic needs. Employers shall pay employees, as a floor, at least the minimum wage required by local law or the prevailing industry wage, whichever is higher, and shall provide legally mandated benefits.

Hours of Work Except in extraordinary business circumstances, employees shall (i) not be required to work more than the lesser of (a) 48 hours per week and 12 hours overtime or (b) the limits on regular and overtime hours allowed by the law of the country of manufacture or, where the laws of such country do not limit the hours of work, the regular work week in such country plus 12 hours overtime and (ii) be entitled to at least one day off in every seven day period.

Overtime Compensation In addition to their compensation for regular hours of work, employees shall be compensated for overtime hours at such premium rate as is legally required in the country of manufacture or, in those countries where such laws do not exist, at a rate at least equal to their regular hourly compensation rate.

Any Company that determines to adopt the Workplace Code of Conduct shall, in addition to complying with all applicable laws of the country of manufacture, comply with and support the Workplace Code of Conduct in accordance with the attached Principles of Monitoring and shall apply the higher standard in cases of differences or conflicts. Any Company that determines to adopt the Workplace Code of Conduct also shall require its licensees and contractors and, in the case of a retailer, its suppliers to comply with applicable local laws and with this Code in accordance with the Principles of Monitoring and to apply the higher standard in cases of differences or conflicts.

(Source: Fair Labor Association Website: <http://www.fairlabor.org/all/code/index.html>)

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**CSR Management/ Supply Chain
Management at Fuji Xerox
(Fuji Xerox of Shenzhen):
Management Centered on Human Resources:
The Importance of Capacity Building of
Workers—Development of Communication Capabilities**

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The case was developed with the cooperation of Fuji Xerox Co., Ltd. and Fuji Xerox of Shenzhen solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective –” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author(s) and the Asia Pacific Economic Cooperation.

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Executive Summary

This case study focuses on the importance of building the capacity of factory workers in basic work-life skills in order to create a working environment that supports the diffusion of Corporate Social Responsibility (CSR) throughout the supply chain. In particular, this case focuses on developing workers' communication skills. The authors wish that this case can become an effective source of learning for corporations' top management (in its headquarters and in its overseas operations), human resources department and CSR department.

The issues addressed in this case are:

1. How to pursue CSR in overseas manufacturing operations; and
2. How to integrate CSR into corporate management and solve management issues.

Nomura, a manager of the Planning and Promoting Group, CSR Department at Fuji Xerox, was under pressure to come up with an effective plan for ethical sourcing.

Before requesting its suppliers to comply with Fuji Xerox's (FX) CSR requirements, Nomura had to check whether FX's own factories met the CSR requirements that ethical sourcing would also require from the company's suppliers. Nomura's experience told him that there would not be serious problems within FX's manufacturing sites in Japan. However, since more than 70% of the company's manufacturing was taking place in China, Nomura decided to survey the CSR management situation of FX factories in China.¹

Despite his anxieties, Nomura did not find critical CSR problems at Fuji Xerox factories in China and specifically at the main facility in Shenzhen (hereafter referred to as "FXSZ"). The environmental management seemed to have been done at a high level.

In fact, when Nomura interviewed Inagaki, the general manager (equivalent to president) of FXSZ, Inagaki told Nomura about his eagerness to improve employee satisfaction as the next step. Inagaki initiated thorough environmental management as a differentiating factor of FXSZ, and after accomplishing it, he was envisioning to create a sense of unity among employees—both workers and management—so that the young people working at FXSZ could realize personal growth and feel satisfied working at FXSZ.

At that time, the employee morale survey scores at FXSZ were not as good as those at FX in Japan. After consulting a local NGO specializing in labor issues, Inagaki realized that the lack of communication among workers, line managers and the staff might be causing problems and thus creating discontent. The local NGO suggested introducing a worker communication education program to investigate their hypothesis. The NGO also suggested that worker education could in fact improve high turnover rate, which characterized factories in China. This situation was not unusual in China and reflected the underlying demographics, internal migration from rural to urban areas and the lack of prior industrial work experience among many workers. The NGO also mentioned that when workers quit after a short while, continuous skills improvement was not possible, and there was no payoff for the cost of training. These labor market characteristics hindered product quality, cost and delivery (QCD) improvements.

Although Inagaki was a little doubtful whether such education program would be effective, he gave his approval to conduct a human communication training on a trial basis for some of the FXSZ workers.

As it turned out, the communication and human relations training program was a great success. A trial program was carried out for 220 workers. The participant workers, as well as their line managers, praised the effect of the program.

¹ See Appendix 1 for basic information on Fuji Xerox.

Reflecting on such a result, Inagaki decided to provide the communication training to all 4200 workers within three months. The questionnaire that the CSR department of FXSZ administered to the program participants revealed the workers' personal concerns, which became a crucial factor for FXSZ to develop its worker educational and psychological care programs. Quick decision-making and action is a virtue of management in China.

Nomura was relieved to see that the first step was a success. He faced the next two challenges: first, to integrate the program into FX's suppliers' processes as part of ethical sourcing, and second, to prove that workers' capacity building measures, such as the communication training, is really cost-effective.

Issues Fuji Xerox of Shenzhen Faced

Fuji Xerox of Shenzhen (FXSZ), Fuji Xerox's main factory, is located in Shenzhen, China. FXSZ faced increasing inquiries from its customer companies about FXSZ's CSR activities, particularly on environment and labor management. FXSZ was also worried about the possibility of production line stoppage at its supplier factories due to labor disputes. As a result, ethical sourcing was becoming a necessity at FXSZ.²

Global Ethical Sourcing Trend

The global ethical sourcing trend has gradually spread across the manufacturing sector since 1996, when a Nike supplier factory was criticized for hiring underage workers and making them work in a hazardous environment. However in Japan, environmental management or so-called "green procurement," began to receive serious attention, as soon as the European Restrictions of Hazardous Substances (RoHS) Directive was announced in 2003. Many manufacturing industries have now implemented green procurement.

The labor management dimension of ethical sourcing has become an even more focused issue globally. Competitive downward pressures on manufacturing costs have spread throughout the supply chain, and these in turn have turned attention to the possibility of inadequate working conditions and practices in factories, particularly in developing economies, where many labor-intensive products are made.

In this sense, manufacturing businesses are increasingly faced with operational stoppage risks caused by labor management practices. For a sound supply chain management, the appropriate management of environment and labor has become critical.

Labor Issues in China

Labor Issues in Shenzhen

² See Appendix 2 for basic information on FXSZ.

Shenzhen City which is located in the southern coastal part of China adjacent to Hong Kong, China, is one of the most rapidly developing industrial cities in China. Since Shenzhen became a special economic zone in 1979, foreign capital has flocked into the area. The Pearl Delta, that includes Shenzhen and its neighboring city Dongguan, has become one of the major manufacturing clusters in the world.

Migrant Worker Problem

There are some characteristics of the Chinese industrial labor market that pose problems for employers and workers alike, and which are relevant to an understanding of the context of this case.

China has two kinds of family register. One is the family register for rural areas and the other is for urban areas. As industry rapidly developed over the past twenty years, inland Chinese farmers on the rural family register have poured into the coastal areas as migrant workers. Currently, the number of migrant workers is said to be between 120 million to 150 million. Many of them work in factories or construction sites and they underpin China's economic development, but they are at the bottom of the social pyramid. Many of them are very young--in their teens--and have little education; thus, they receive low salaries and have no job security. In addition, due to the rural family register, they lack access to social security when they work in urban areas. The plight of these workers is a major cause of the increasing poverty and deteriorating safety in the industrial areas of China.

Manufacturing companies in the region have relied on these migrant workers. Companies expect a continuous flow of low-cost workers, so they do not seriously consider the low retention rate. It is said that in general, the annual turnover rate is between 30% to 50%, which means that a little less than half of the workers quit within a year. However, as a result of China's policy of one child per family, China's labor force growth is slowing down and the supply of labor is becoming more scarce.

Fuji Xerox and Fuji Xerox of Shenzhen's Partner: Institute of Contemporary Observations (ICO) in Shenzhen

The Institute of Contemporary Observation (ICO), an NGO that studies social conditions in China, characterizes the problems at the factories in the South China region as follows:

1. Line managers lack work experience and knowledge, which leads to labor management inefficiency.
2. Factories (and companies) do not take care of their workers' needs in terms of the psychological aspects, which contribute to labor disputes and poor retention rate.

Therefore, ICO focuses on worker education. Many migrant workers are forced to accept harsh working conditions because in many cases they do not have enough knowledge of labor rights. In addition, many young migrant workers from rural areas do not even have the common sense necessary to live on their own in the urban areas.

ICO also points out that young migrant workers do not consider themselves and the company they

work for as a community sharing a common aim to prosper. Instead, they only see the company as an organization that gives them a salary. Thus their connection to the company is short term and their commitment limited.

Japanese Management Style in the Age of Rapid Economic Expansion

How did the Japanese industry develop so rapidly in the past? One of the major reasons is that Japanese companies focused on capacity building of workers. Japan was a poor developing country after World War II. To attain economic recovery, Japan pursued the processing trade (importing raw materials and exporting manufactured products), which required many factory workers. Therefore, many Japanese companies hired young workers from rural areas who had just finished junior high school or high school. Companies called these workers their “golden eggs,” and provided them various educational and training opportunities as well as family-like care and support in daily life. These included not only technological skill development, but also capacity building to adjust themselves to urban society, offering them psychological support as well as recreational opportunities such as company trips and outdoor amusement. These efforts on the part of the company created a harmonious community within factories, and the workers worked hard to respond to such care from the company. These workers with high morale matured as leaders and supported the steady growth and strength of companies and the Japanese economy. In this respect, corporations played a really important role in the socialization of workers in an industrial society. The earlier Japanese experience provided some important lessons for Fuji Xerox’s management in the new industrial regions in China.

Fuji Xerox’s Project on Ethical Sourcing Starts

Start of Ethical Sourcing

Fuji Xerox introduced the Green Procurement Guidelines in 1999. The company anticipated that its major American customers would require Fuji Xerox to implement ethical sourcing in the near future, and therefore decided to make a plan on ethical sourcing in September 2005.

In general, companies introduce ethical sourcing projects according to the following process: First, they formulate a supplier code of conduct, then hold briefings for suppliers, and finally, develop an audit structure. When companies find out during the auditing process that suppliers have not complied with their requirements, they decide whether to ask for improvement, or to terminate business with the supplier. Initially, Fuji Xerox thought of following a similar process.

However, things changed completely in April 2006 when the project team explained the plan to Tadahito Yamamoto, then executive vice-president in charge of development and production (and currently company president). Yamamoto was concerned that ethical sourcing could only work effectively if it were built on a solid management foundation. Therefore he decided that a corporate ethical sourcing program would only be phased in after readjusting the requirements for quality improvement, cost reduction, and delivery improvement that had already been imposed on suppliers. In other words, his strategy was to integrate ethical sourcing into a process of continual improvement base, in cooperation with suppliers. The implication was that CSR requirements

would be fully implemented in the procurement process rather than treated as an independent program. Yamamoto was worried that if ethical sourcing were added on top of such requirements, the pressure on suppliers would exceed their capacity to respond, and the suppliers would implement ethical sourcing just as a formality.

The project team requested the cooperation of the nine managing member companies of the Global Co-Prosperity Society which was made up of Fuji Xerox's key business partners. Following repeated study group meetings since June 2006, member companies became increasingly concerned with production and shipment stoppages as a result of labor disputes at overseas sites. Approximately 80 percent of Fuji Xerox's production is currently associated with manufacturing sites in China. In addition, many managing member companies of the Global Co-Prosperity Society conducted production activities in China. Although many Japanese factories in the Shenzhen area shared the same issue, no solution was apparent.

In response to the situation, the study group held a 5-day meeting in Shenzhen City, China in November 2006. In addition to the original members from Japan, approximately 50 people from the nine companies, including their Shenzhen factories' managing directors and procurement officers as well as Fuji Xerox's Shenzhen and Dongguan factories, participated.

ICO explained in detail to the study group China's social conditions, current problems, and future challenges regarding China's labor issues. The group members also interviewed the presidents and chief operating officers (COOs) of several local companies. They learned advanced practices and participated in simulated auditing of factories, canteens and dormitories. The group members likewise learned examples of capacity building activities that actually led to productivity improvements in several companies such as a supplier of an American sportswear company who built a school within the dormitories. The participants also engaged in a full-day group discussion.

In this way, Fuji Xerox shared its ethical sourcing preparation process with the nine managing member companies of the Global Co-Prosperity Society. Fuji Xerox considered it critical for the top management of suppliers to understand the necessity of ethical sourcing, so that they could engage in the continuous improvement of their own companies' CSR management.

Similarity between Present-day China and Japan's Experience of Rapid Economic Development

All participants shared the impression that the current labor situation in China is similar to that of Japan from the late 1950s to the early 1970s. During that period, many young people in Japan who came from rural districts to work in factories, experienced psychological instability and felt that they were left out of society. The experience of Japanese management from that era would therefore be relevant in addressing issues related to Chinese social conditions and their impact on the workplace and on human resources development.

In addition to job training, it was essential for management to make a sustained effort to guide employees in their daily life and support their self-reliance. The study group members felt strongly that treating employees according to societal conditions in China was essential for maintaining product quality. They realized that what had been Japanese companies' practice of caring for workers needed to be remembered and implemented in their factories in China as well. Even if companies implemented an excellent system of labor management relations, it would not have functioned as expected if the workers themselves did not know how to use the system effectively, or if they harbored discontent towards the company based on external factors related to broader socio-economic conditions. Capacity building would lead to quality improvements by minimizing

risks caused by environment pollution, product safety liability, fraud cover-ups and labor disputes. In short, human resources development would be critical in creating an effective management system, which in turn would be a necessary foundation for introducing ethical sourcing.

Experiment at FXSZ

Before asking its suppliers to implement CSR management, Fuji Xerox considered that its own operations should integrate CSR management in China and that this should be presented to the company's suppliers as a model case. Fuji Xerox decided to make Fuji Xerox's main manufacturing site, Fuji Xerox of Shenzhen, the model factory. Fuji Xerox has other manufacturing sites in Japan, and their CSR management seemed better than that of FXSZ, as evidenced by the environmental management and employee morale survey. However, since major manufacturing risks resided in China operations, and many of Fuji Xerox's suppliers operated in the southern part of China, Fuji Xerox decided to make FXSZ the model case.

Furthermore, although FXSZ was Fuji Xerox's subsidiary, FXSZ operated as an independent company, and most of its employees were Chinese. So Fuji Xerox believed that introducing ethical sourcing in FXSZ would be a perfect first step.

When the project leader Nomura suggested making FXSZ the model case to Inagaki, the general manager of FXSZ, Inagaki agreed. After 10 years of operations, FXSZ was already capable of producing a full line-up, including color machines, medium and high-speed machines. Since his inauguration as the general manager, Inagaki had eagerly set out to implement environmental related activities. As a result, FXSZ was awarded the Chinese government's certification as the Environment Friendly Corporation in 2005. "Recently I have come to believe that it all comes down to people," Inagaki said. "Employees must be able to feel a sense of satisfaction from working with the company. Therefore, we are making even greater efforts in areas concerning personnel, such as occupational health and safety."

It was a fact that Japanese companies' factories operating in the region suffered high labor turnover rate. Inagaki had heard that some factories were facing the risk of strikes due to labor disputes. If strikes occurred in FXSZ's supply chain, and key parts from suppliers stopped flowing into FXSZ, then there was a serious risk that FXSZ's manufacturing line would grind to a halt. If the manufacturing line stopped for even one day, the cost reduction efforts that FXSZ was going through would be in vain. Therefore, enforcing labor management and promoting CSR management at FXSZ was becoming a necessity just as asking its suppliers to do the same was also becoming a necessity for FXSZ.

Training Program on Communication and Human Relations

Based on the information and the experience of ICO regarding labor issues in the region, Nomura thought that communication training for the workers would be effective. Communication problems between the Japanese management team and the Chinese workers had been pointed out before, but it seemed that communication among the Chinese workers in the actual manufacturing line was even more of a problem and affected workers' retention rate.

Many of FXSZ's line workers were only 18 to 20 years of age. Line managers, the first line supervisors, were only slightly older. Workers were assigned to become line managers only after experiencing one or two years with the manufacturing line, and still lacked management experience or training. Often they did not know how to control the workers and lacked the skills to convey work orders clearly, or give feedback or discipline their subordinates when the latter did not follow

their orders. Some managers treated their subordinates too harshly in front of other group members, which deeply insulted the concerned workers. Nomura assumed that if communication between the Chinese workers and leaders were smoother, workers dissatisfaction would diminish.

The workers who lived in dormitories far removed from their families experienced emotional stress due to homesickness, roommate trouble, romantic attachments and so on, and these stresses were exacerbated by lack of effective communication skills for resolving differences.

After consulting ICO, Inagaki thought that the lack of communication among workers, line managers and the staff might have been causing problems and creating discontent. ICO suggested introducing worker communication education program to investigate the hypothesis. Although Inagaki was a little doubtful whether such education program would have immediate effect, he approved the implementation of a human communication education program on a trial basis for 220 of the 4200 FXSZ workers.³

The program was a basic course on human communication that lasted for only two hours. The seminar started with the definition of effective communication, followed by ways to establish human relationship, and the appropriate distance for communication. Many workers were astonished to hear the lecturer say: “You can put into words only 80% of what you think you want to say, and those who hear you can truly understand only 20% of what you say. So you have to listen very carefully—you have to think what the person is thinking when you listen to one another.”

The Result of the Trial Training Program

The training program was a great success. Both the workers and their managers praised the seminar. Nomura interviewed a 19 year-old worker, who said “I learned that I can’t convey my thoughts to other people without making the effort to talk to them. I felt how self-centered I had been, getting upset that people don’t understand me when I had not even made the effort to talk. I have more friends now that I can communicate more smoothly. Since the program, I also try hard to listen to what people have to say. Now I can truly say that I have made the transformation from a student to a working adult.”

The program received high marks from the participants. The results of the questionnaire revealed that 99% of them were satisfied with the program. Participants’ written comments included: “I felt inferior not voicing my opinion,” “I learned how I should talk to people,” “I want to learn more about communication,” and “I appreciate that the company offers such training.” Inagaki himself felt the effect through reports from the line managers. He was surprised that a mere two-hour program had such an impact. Inagaki immediately decided that all 4,200 workers should take the same communication training.

All workers at FXSZ took the two-hour communication program within three months after its trial run. Since this was a compulsory education or training by the company, FXSZ provided overtime pay for those who attended. This program has become mandatory education for all new entrants to FXSZ. FXSZ offers a free advanced course on communication and human relations to those who want to participate voluntarily. For this course, overtime is not paid, because it is optional.

Other Labor Management Efforts

The results of the questionnaire on the communication training program revealed that many

³ See Appendix 3 on FXSZ Communication and Human Relations Trial Training Program.

workers experienced emotional stress. To minimize such stress, FXSZ introduced several measures. First, FXSZ implemented a hotline by contracting an NGO which provided the services of a psychological specialist to receive telephone calls and give advice to troubled FXSZ employees. Second, FXSZ placed six “CSR Opinion Boxes” near the entrance of dormitories, canteen, and factory lines. FXSZ received an average of 20 written opinions per month in the CSR Opinion Box. Many of them were complaints regarding their colleagues or requests to improve cafeteria meals. Some comments merited immediate attention from the human resource department since they were concerned with serious issues. Some made constructive suggestions regarding manufacturing line management.

The Opinion Box accepts written complaints without indicating their source. The CSR department staff continue to take each complaint seriously, and respond individually whenever the opinion poses serious personnel matters. There were several cases where capable workers who initially posted in the Opinion Box that they would quit decided to continue working at FXSZ, after consultation with the CSR staff.

These efforts by FXSZ are bearing fruit. According to an employee survey asking “What do you like about FXSZ?” the respondents who answered “the education and training program” jumped from 10% in 2006 to 32% in 2007.⁴

Implementation among Suppliers

This CSR management know-how on worker management in China has been recorded and incorporated into ethical sourcing implementation. Fuji Xerox has developed a “Management Guideline on CSR” that includes Fuji Xerox’s requirements of suppliers’ CSR management processes, with background information as to why such management is necessary, and problem cases and possible solutions to those problems. Fuji Xerox also compiled a “Self-assessment Checklist” that comprises some 380 questions. Fuji Xerox’s request to introduce capacity building is incorporated in the “Management Guideline on CSR” and “Self-assessment Checklist,” although this is not mandatory. Fuji Xerox notes that the company places importance on human capital, and that it regards capacity building as a key factor in building trust between company management and the workers, that would result in QCD improvements.⁵

Fuji Xerox also invited several key suppliers to FXSZ to show them actual worker problems and solutions that FXSZ found feasible.

There are reasons for Fuji Xerox to involve the suppliers in the ethical sourcing preparation process, and to share Fuji Xerox’s experiences in solving problems. Simply requesting suppliers to comply with Fuji Xerox requests would result in suppliers hiding the real problems. This result is not what Fuji Xerox aims to achieve through ethical sourcing, rather its aim is to implement an effective system so that suppliers would voluntarily adopt CSR management, and minimize supply chain risks that affect product QCD, as well as contribute to a sustainable society.

Unless the suppliers are motivated to do so, the chain of CSR management would remain artificial, and no true improvement on environment, labor, corporate ethics and governance can be expected. In order to make the suppliers implement CSR management seriously within their organizations, Fuji Xerox needs to find solutions, or at least find some clues to solve problems, then to communicate these clues to suppliers. This is what Fuji Xerox calls engagement.

⁴ See appendix 4, for the result of the questionnaire.

⁵ See appendix 5, for the content of Management Guideline and Self Checklist.

Conclusion

Engaging with the suppliers to promote CSR management is a key factor in making ethical sourcing effective. Fuji Xerox's experience indicates that engagement between workers and companies is also the key to promote sound company growth. Communication between Fuji Xerox and its suppliers as well as between companies and its employees underpins better understanding of each other's requirements and positions and helps the company to further advance its growth. The communication training trial that FXSZ introduced had been successful. Likewise, the communication to the managing companies of the Global Co-Prosperity Society has become the company's cornerstone for successful ethical sourcing.

Fuji Xerox introduced its ethical sourcing program in August 2007 to some 300 suppliers.⁶ Fuji Xerox's challenge is how thoroughly it can communicate ethical sourcing to its several hundred suppliers, and to convince them to implement CSR management. Nomura's challenge continues.

⁶ See Appendix 6 for ethical sourcing roadmap.

Appendix 1 Fuji Xerox's Basic Information

- Established: February 1962
- Capital: 20 billion yen
- Shareholders: Fuji Film Holdings (75%, Japan), Xerox Limited (25%, USA)
- Employees: Fuji Xerox: 13,600 (Unconsolidated), 40,200 (Consolidate): (March 2007)
- Fuji Xerox defines "documents" not only as information inscribed on paper but also as knowledge in a multimedia format including electronic data, images, audio and so forth. In supporting customers' businesses, the company believes that the vital point is how they can share "documents," which are very important managerial resources, and utilize them in a creative and effective way. Based on this awareness, by providing document services to customers and through process innovation, Fuji Xerox aims to deploy activities to increase office efficiency and contribute to its customers by helping them solve their management issues.
- Fuji Xerox's sales and services area covers China, Japan, and other Asia-Pacific countries and regions. Other areas are covered by Xerox Corporation and Xerox Limited. Fuji Xerox manufactures more than 70% of its products in China.
- Key products are: office multifunction devices, workstations, personal computers, facsimiles, CAD systems, plotters, printers, paper, electronic parts, educational services and others.

Appendix 2 FXSZ's Basic Information

- Name: Fuji Xerox of Shenzhen Limited
- Established: June 1995
- Type of enterprise: Exclusively foreign-owned enterprise
- Capital: US\$38 million (Fuji Xerox 90%, Fuji Xerox China 10%)
- Employees: approximately 5000 employees, including 500 administrative personnel and 30 Japanese expatriates. (as of March, 2007)
- Total investment: US\$ 59 million
- Scope of operations: To develop, design and manufacture laser printer, ink-jet printer, optics and electron copying machine, digital copying machine, digital multifunction machine (integrated with functions of printing, faxing, scanning and copying), cartridges and relevant components. To sell product manufactured by FXSZ and to provide services after sales.
- For further information on FXSZ and its CSR activities, please refer to the following homepage:
Website: http://www.fxsz.com.cn-gb-environment-KechixufazhanReport-2007_EN.pdf

Appendix 3

FXSZ Communication and Human Relations Trial Training Program

- Education participants: 220 line workers, ages between 17 and 18, average work experience at FXSZ less than three months. 60% of the participants were women.
- Lecturer: Institute of Contemporary Observation (ICO)
- Theme: Communication and human relations

Photos of the Training Program

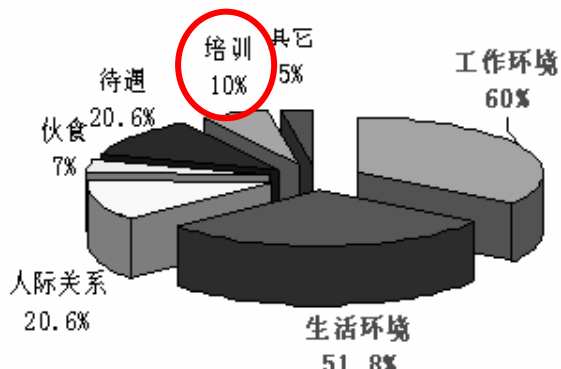


Appendix 4

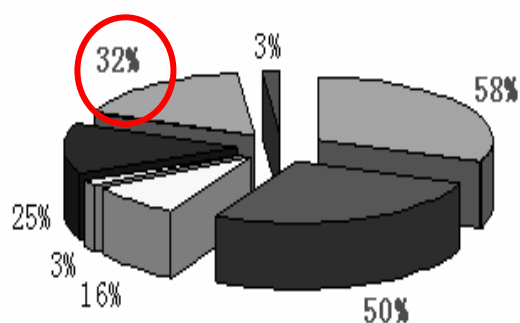
FXSZ Survey (Comparison Between 2006 and 2007) on CSR Activities at FXSZ and its Results on Employee Assistance Program (Survey data from 2007)

Key message: The workers who feel satisfied about the education program at FXSZ has jumped from 10% in 2006 to 32% in 2007.

(Results from the 2006 survey)



(Results from the 2007 survey)



Additional information on the survey done by CSR department, FXSZ:

1. Aim of the survey
 - Achieve top level CSR management (Improve worker satisfaction)
 - Care for the employees (Hire top quality workforce)
 - Understand employees' work and life conditions, and provide support
 - Increase and improve the quality of employees' leisure time
 - Provide opportunities for the employees to experience joy of personal growth
 - Maintain and improve psychological health of employees
2. Method
 - Survey target: all line managers and 10% of the line workers
 - Survey documents: two kinds (one for the line managers and the other for the line workers)
 - Distribution method: E-mail survey sheets to line managers. For line workers, distribute by paper through representatives of each department.
 - Collecting method: same as distribution method.
3. Survey frequency
 - Once a year, every June.

Appendix 5

Contents of Fuji Xerox Management Guideline and Self Checklist

Environment

1. Prevention of Global Warming
2. Promotion of Resource Conservation in Products (Reduced Use of Natural Resources)
3. Recycling and Proper Waste Disposal
4. Proper Management of Chemical Substances
5. Promotion of the Natural Environment Preservation (Biodiversity and the Ecosystem)
6. Adherence to Administrative Procedures
7. Promotion of Third-Party Certification of an Environmental Management System (EMS)
8. Promotion of Recommendation and Application to Your Company's Suppliers

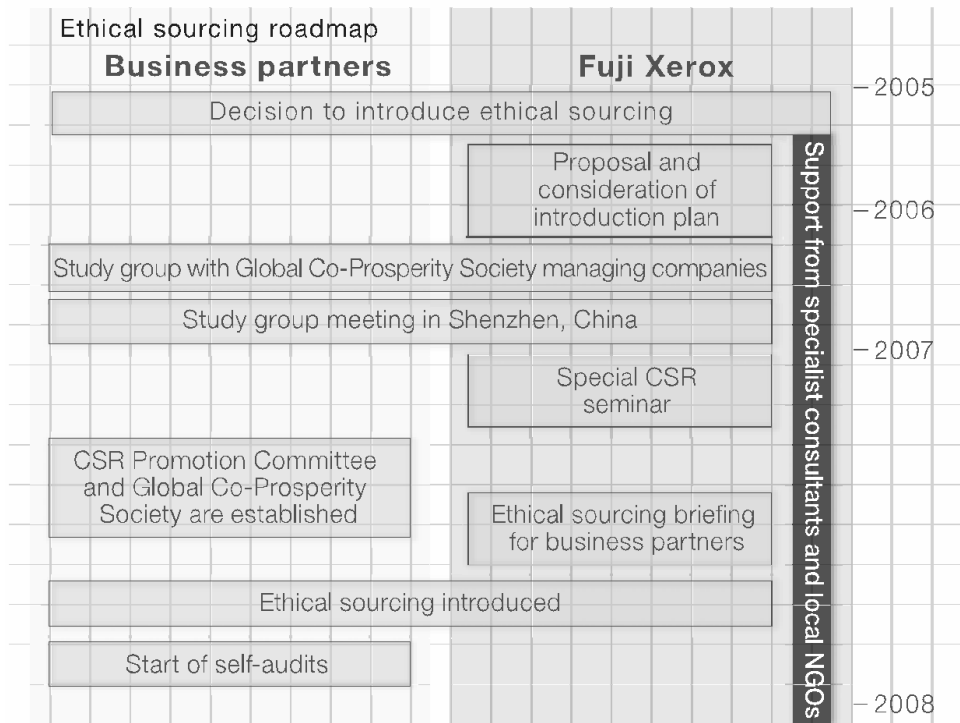
Human Rights and Labor

1. Prevention of Forced and Child Labor
2. Prevention of Unfair Discrimination and Privacy Infringement
3. Prevention of Violence, Sexual Abuse, Sexual Harassment, and Excessive Punishment in Workplaces
4. Provision of Appropriate Wages and Proper Management of Working Hours and Mandatory Days Off
5. Guarantee of Right of the Directly Employed for Organization and Collective Bargaining
6. Prevention of Work-Related Accidents at Workplaces and on Duties
7. Establishment of Measures on Treatment of Illnesses and Injuries and Maintenance of Health
8. Sufficient Healthcare Facilities and Welfare Measures
9. Promotion of Human Resource Development
10. Promotion of Third-Party Certification
11. Promotion of Recommendation and Application to Your Company's Suppliers

Corporate Ethics

1. Corporate Ethics and Compliance Management
2. Anti-Corruption
3. Protection of Intellectual Property
4. Guarantee of Fair Procurement Transaction
5. Establishment and Management of Raising Concerns and Whistle-blowing
6. Establishment of Information Security System
7. Promotion of Recommendations and Application to Your Company's Suppliers

Appendix 6
Fuji Xerox's Ethical Sourcing Roadmap



From Fuji Xerox Sustainability Report 2007, Highlight 2
 Website: <http://www.fujixerox.co.jp/eng/sr/>

Establishing Greener Supply Chain: Case of Fujitsu Limited

Japan

Written by

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The case was developed with the cooperation of Fujitsu Limited and Alpha Network Inc, solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

Executive Summary

This case focuses on activities that Fujitsu Limited, one of the Japanese leading electronics and information technology (IT) companies, undertook to address the environmental aspects of its supply chain management. Fujitsu has just promoted its CSR conscious procurement activities with the CSR Procurement Guidelines based on its CSR philosophy, The Fujitsu Way. The Fujitsu's CSR supply chain activities follow the same process as its green procurement activities which have been implemented for eight years.

The EU RoHS Directive made Fujitsu consider the necessity of revising its Green Procurement Direction (GDP). The latest revision of the GDP in March 2007 requires suppliers to establish an Environmental Management System (EMS), comply with regulations for Fujitsu specified chemical substances and establish Chemical Substances Management System (CMS).

Since majority of Fujitsu's suppliers were located in the Asia and Pacific regions, Fujitsu established the Environment Management Center (EMC) in Chinese Taipei, which was responsible for green supply chain management, especially in China and Chinese Taipei. No other Japanese company has established an independent overseas audit office such as EMC for green procurement. Since green procurement was not popular at that time, EMC had to communicate with the suppliers patiently to make them understand the concept, to overcome the gap between what suppliers said and what they did, and to follow through with their recommendations.

Alpha Network, a Fujitsu major supplier, obtained a "C" rank from EMC auditing at first but later on succeeded in establishing its own robust chemical substances management system and obtaining certification from its major customers other than Fujitsu. The key point of Fujitsu's achievement in the establishment of the green supply chain is the existence of the EMC which facilitated frequent and courteous communication with suppliers that led to mutual understanding and solutions to common concerns.

Introduction

This case study focuses on the actions taken by Fujitsu Limited, one of the leading electronics and information technology (IT) companies in Japan, to address the environmental aspects of its supply chain. There are two reasons for this focus. First, the management of hazardous chemical substances throughout the supply chain has become critical for Fujitsu. Second, Fujitsu's initiatives in Asia are regarded as one of the most advanced among those undertaken by other Japanese electronics companies.

Background

In 2001, the Dutch government banned the sale of Sony Play Station in the Netherlands because cables attached to the play station contained an amount of cadmium that exceeded what was allowed by Dutch standards. Although the cables were not produced by Sony but sourced from its suppliers, Sony had to bear the costs of pulling out the shipment and terminating the contract with the buyers. Learning about the incident, Fujitsu executives acted immediately to assess and control hazardous substances in their suppliers' products globally. In addition to "Sony shock", Fujitsu reviewed its definition of the containment of hazardous substances and clarified the

Fujitsu Group's view of this definition considering that it was the European Union (EU) which established the RoHS Directive.*

The EU RoHS Directive which regulates the content of certain hazardous substances in electrical and electronic equipment was issued on 01 July 2006. It restricts the use of six substances: lead, mercury, cadmium, hexavalent chromium, polybrominated biphenyls (PBB) and polybrominated diphenyl ether (PBDE). Except for cadmium with a maximum permissible concentration of 100ppm, the permissible concentration for the other substances is 1000ppm. The requirement is applied to every homogeneous material. Manufacturers of finished goods are responsible for all homogeneous materials in their finished products. Hence, they need to assess and control six hazardous substances in their suppliers' products.

In addition to the EU, China has also introduced a similar kind of regulation called China RoHS, which was enforced on 01 March 2007. To cope with these regulations, electronics related companies have to monitor their supplier's products seriously.

Fujitsu's Green Procurement Direction

Prior to the introduction of the RoHS Directive, Fujitsu predicted that hazardous chemical substances in products would be subjected to stricter legal regulations. Thus, it formulated its Green Procurement Direction (GPD) in June 2001. Fujitsu realized that the presence of hazardous substances in their products presented two types of risk: legal penalty and CSR risk. Fujitsu considered CSR risk as the more serious of the two. Fujitsu revised the GPD in July 2003 (Edition 2). The revised GPD specified how to manage and evaluate containment of the specified hazardous substances since it was necessary to survey rigidly whether the specified hazardous substances were contained in products or not, in order to meet legal regulations.

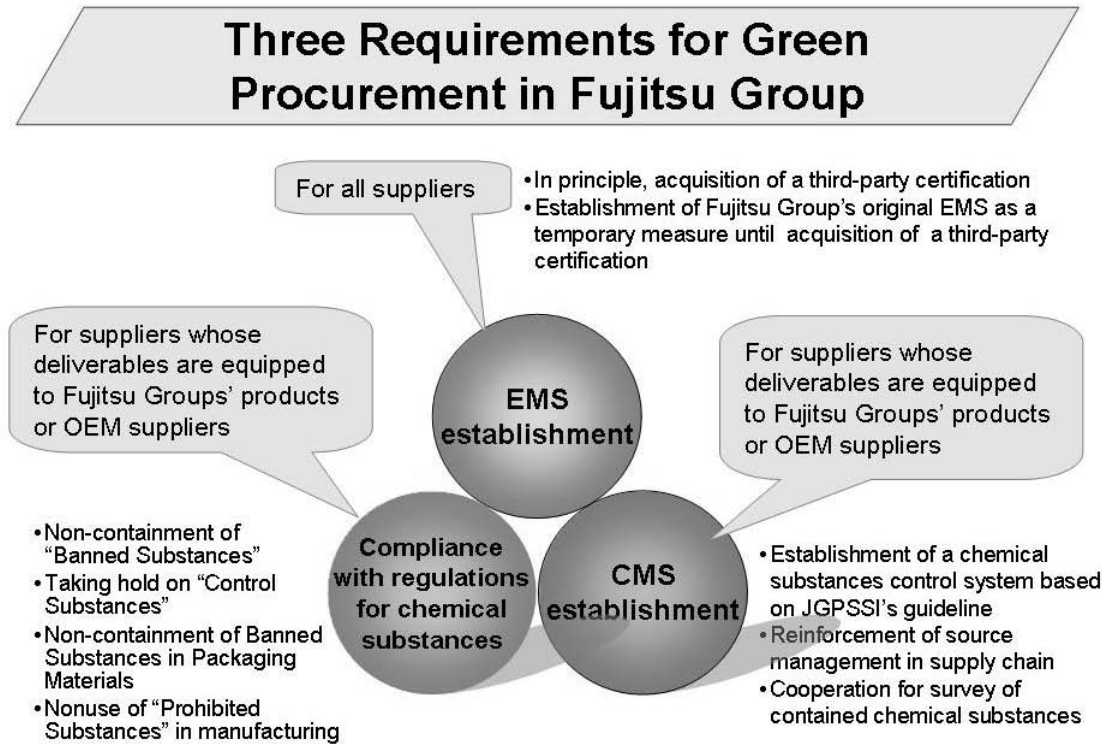
In consideration of the strong concern for CSR and the RoHS movement, Fujitsu made another revision (Edition 3.0) on the GPD in November 2004. The main points of this revision were: a) the review of the definition of the containment of hazardous substances; and b) the promotion of the purchase of all items, including equipment and software and services, from suppliers who have built their environmental management system (EMS).

In May 2007 Fujitsu revised the GPD (Edition 4.0) for the fourth time since strict control of certain hazardous substances in products had become vital in every supply chain. In addition to the establishment of an EMS system, Fujitsu requested suppliers to establish a management system that would allow them to control the use of chemical substances in products delivered to Fujitsu. The revised GPD also made some changes on regulations governing specified chemical substances.

At present, there are three main green procurement requirements to be met by suppliers. As indicated in **Figure 1**, these are the following: 1) EMS establishment, 2) compliance with regulations for Fujitsu specified chemical substances, and 3) Chemical Substances Management System (CSM) establishment.

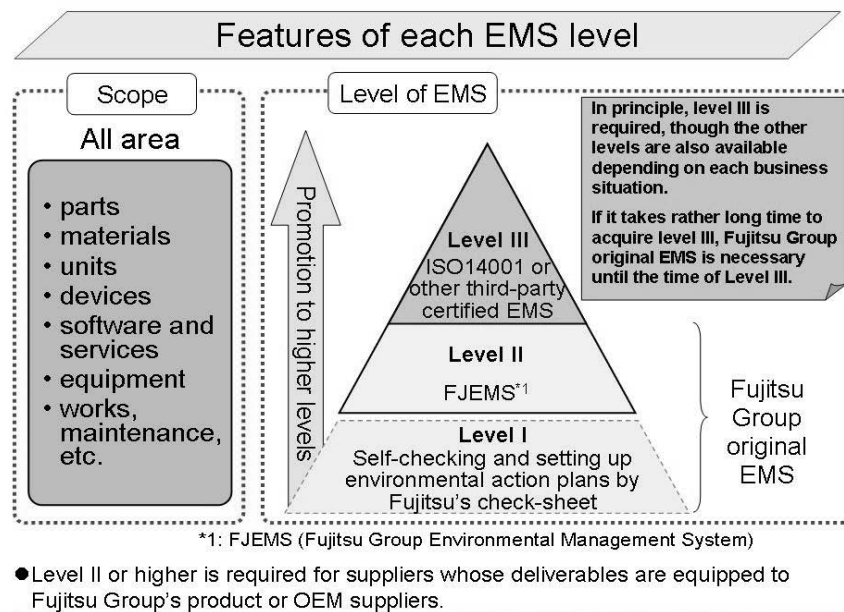
* The RoHS Directive stands for Directive 2002/95/EC of the European Parliament and of the Council on 27 January 2003 on the restriction of the use of certain hazardous substances in electrical and electronics equipment.

Figure 1:
Requirements for Fujitsu's Green Procurement



In principle, EMS certification by a third-party organization is necessary. Fujitsu, however, has provided original EMS in consideration of small and medium-sized suppliers who would have difficulty acquiring third party EMS certification. As shown in **Figure 2**, there are three levels of EMS implementation status. The scope of EMS includes all areas of production such as software and services, equipment, works and maintenance, etc. as well as parts, materials, units and devices.

Figure 2:
Features of Each EMS Required for Suppliers



To address the second requirement, Fujitsu defined its own regulations on chemical substances related to deliverables which are used in Fujitsu’s products or OEM products. Suppliers are requested to comply with the regulations. The specified chemical substances are classified into five categories: banned substances (28 groups), control substances (9 groups), banned substances of packaging materials (4 groups), prohibited substances in manufacturing process, and other restricted substances in delivery destination economies or areas.

In terms of CMS, Fujitsu requests the establishment of CMS by suppliers whose deliverables are inputs to Fujitsu’s products or are OEM suppliers. Each company in the supply chain needs to implement proper and effective management of chemical substances in their products. There are 15 action items in CMS as shown in **Table 1**. Fujitsu provides suppliers self-check sheet to manage the chemical substances content of their products. After the self-checking done by the suppliers, Fujitsu visits them and undertakes audits on CMS compliance based on the submitted self-check sheet. If necessary, Fujitsu requests the suppliers to improve their CMS operation and advise them how this could be done.

Table 1:
Action Items in CMS

No.	Action Items
1	Guideline establishment
2	Definition of customer and other requirements
3	Definition of application parameters
4	Definition of organizational systems, roles, and responsibilities
5	Design and development
6	Obtain and confirm information regarding substances in products
7	Purchasing management
8	Confirmation on receipt
9	Process management
10	Revision management
11	Shipping confirmations
12	Handling non-conformances
13	Education and training
14	Documentation and documentation management
15	Communication (sharing and provision of information)

Action items are subject to change, if necessary.

Fujitsu’s green procurement activities do not aim to select good green-concerned suppliers and to cut off any supplier that does not meet Fujitsu’s standard. The purpose of Fujitsu’s activities is mainly to promote CSR in cooperation with suppliers. Fujitsu has requested that suppliers build their own EMS and CMS while phasing out the use of hazardous substances. In case a supplier is not able to meet the standards, Fujitsu intends to help the supplier build, operate and improve EMS.

Green Procurement Activities in Asia and Pacific Regions

Most of Fujitsu’s suppliers are located in Asia and the Pacific regions. Fujitsu started green procurement by holding conferences on environment management in Chinese Taipei, Hong Kong,

China and Singapore in October 2003. In December 2003, Fujitsu established the Environment Management Centre (EMC) in Fujitsu Taiwan Limited (FTL), which was responsible for green supply chain management in Asia, especially in China and Chinese Taipei. At that time, there was no Japanese company with independent overseas office to audit green procurement compliance.

The EMC had four people in charge of audit. One came from the Fujitsu head office in Japan and the other three were local staff. EMC targeted to audit approximately 80 first tier suppliers, 70% of which were Chinese Taipei capital companies, 20% were Chinese (and Hong Kong, China) capital companies and the other 10% were Japanese capital companies. However, more than 80% of these suppliers were located in mainland China. The four EMC staff have audited more than 90% of these suppliers, traveling frequently between mainland China and Chinese Taipei.

EMC started with a survey of the suppliers during which they tried to make their suppliers understand Fujitsu's green procurement philosophy and the company's support for their activities for green products. Next, EMC did an on-site survey in order to: a) know their suppliers current situation; b) help them establish their environmental management system; c) provide advice on lead-free products; and d) introduce their suppliers to laboratories which inventory hazardous substances contents of products. By the end of November 2004, EMC had completed the survey of 61 suppliers.

Since green procurement was not a popular concept at that time in Asia, most suppliers were reluctant to accept EMC's survey. EMC had to communicate with the suppliers patiently and make them understand the concept of green procurement and its importance in reducing the risk of pollution, which could result in lost business opportunities if left unattended. EMC's consistent efforts gradually changed the suppliers mindset and increased their awareness of green products.

In January 2005, EMC started the second step survey or auditing of the green products activities of their suppliers. They conducted interviews and gathered documentary evidence. Based on the results of the survey, each supplier was assigned a letter grade (A, B, C and F). The grade reflected suppliers action items, such as a) environment management, b) suppliers management, c) design and development management, d) procurement management, e) production management, f) response to customer requirement and g) change management. The grade which was assigned to a supplier was used by Fujitsu sourcing managers to guide their procurement decisions.

By March of 2006, the EMC had finished the survey of about 50 suppliers who were graded A (20%), B (40%), and C (35%). One supplier was awarded an F grade. The A-rank supplier could supply its products without any supplementary requirement. However, the B-rank supplier was advised by EMC to further improve its management, and the C-rank supplier had to fulfill EMC's other requirements. On the other hand, if the F-rank supplier could not improve its performance, the supplier would not be able to supply its products to Fujitsu.

In 2006, there were some changes in the original method which EMC used to audit the above-mentioned green procurement activities. By April 2006, however, the new standardized auditing tool for all Fujitsu suppliers had been introduced globally.

In this common auditing tool, the number of suppliers action items increased to 15 from seven in the previous EMC system (Table 2). There were 81 requirements and some of them were critical requirements. The criteria for ranking A, B, C, and F were also changed. An A-rank meant that there was 100% compliance with the 81 requirements. B-rank indicated 100% compliance with the critical requirements, but not with the whole 81 requirements. C-rank was given when there was at least 60% compliance with the critical requirements and F-rank when there was less than 60% compliance.

Under the new auditing system, 80 suppliers were audited between April 2006 and February 2007. Among them, 20% were rated as A-rank, 10% as B-rank, 65% as C-rank, and one supplier as F-rank. After this audit, 45% of the non A-rank suppliers were advised on how to improve their performance. By the end of February 2007, about 90% of this group moved up to the A-rank category.

Table 2:
Action Items in Fujitsu's Supplier Auditing Sheet

Action Items	Number of Questions
Guideline establishment (Policy development)	3
Definition of customer & other requirements (Identification of customers, clarification of their requirements)	3
Definition of application parameters (Scope of control)	3
Definition of organizational systems, roles & responsibilities	3
Design/Development (Design and development)	8
Obtain and confirm Information regarding substances in products (Procurement of chemical substances content information, verification)	7
Purchasing management (Supplier management)	7
Confirmation on receipt (In-coming confirmation)	4
Process management (Process control)	14
Revision management	3
Shipping confirmations (Shipment)	4
Handling non-confirming	4
Education/Training	3
Documentation and documentation management (Documentation and control)	6
Communication (Sharing & provision of information/ Information sharing)	9

The EMC survey did not aim to police the suppliers green product activities, but to help the suppliers understand the concept and management of green products. Suppliers who met EMC green product requirements were awarded Fujitsu Notification on Control on Chemical Substance Contained in Products (See **Appendix 1**). They displayed the notification in their CEO room and use it as an evidence of good trade practices, when they started new businesses with new customers.

The EMC also encountered some problems and obstacles. During the initial stage of implementing the CMS, suppliers did not recognize the importance of CMS and EMS as tools to improve environmental performance. The targeted first-tier suppliers were relatively large scale companies which traded with European and American customers, hence they understood basically the environmental issues affecting their business activities. The problem was that most of these companies were supplying other customers not only Fujitsu, and did not feel the urgency to respond to what they perceived as troublesome requirements of the company.

Having made the suppliers accept Fujitsu's green procurement rule, the EMS team was again confronted with another problem that occurred in the implementation phase. Compared to the Japanese suppliers, managers of overseas suppliers were likely to exaggerate what their respective companies have done to "green" their products. The EMC auditors sometimes found a gap between what suppliers reported and what they did. It was important that EMC observed first what the company was doing.

The other problem stemmed from the description of the procurement rule originally issued in Japanese. When the EMC used the audit sheet that was directly translated from that Japanese version, some provisions were unclear to Chinese suppliers. In the Japanese version, many articles were described as "recommendation" which Japanese suppliers usually followed and sometimes did voluntarily. However, Chinese suppliers took it to mean that they had some leeway as to how far they should go along with the "recommendation" which were really not just recommendatory. After EMC found this cultural gap, they started to explain to suppliers that what were given as recommendations were really orders that they had to follow.

Supplier's Activities – Alpha Network

Alpha Network Inc is one of the major Fujitsu suppliers. It was founded in August 2003 from a spin-off of the ODM/OEM business unit of D-Link Corp. Its major product lines include MAN/LAN, broadband, wireless, VoIP/IAD, and digital home. Alpha Network is the largest networking ODM/OEM vendor in Chinese Taipei, with US\$551 million revenue in 2005. Its head office is located in Hsinchu, Chinese Taipei, and the production centers are in Hsinchu and in Dongguan, China. The company has more than 4,500 employees worldwide.

Fujitsu mainly procures switches and broad-band devices from Alpha Network. At that time, Alpha Network was trying to catch up with Japanese companies in operational excellence at the plant level and introduced TQM (Total Quality Management) and TPM (Total Productive Maintenance). However, they did not realize that controlling hazardous chemicals in their products was important to achieve sustainable growth. They were not supportive of Fujitsu's environment management audit because they thought that accepting Fujitsu's environment management requirement was an additional burden. Fujitsu EMC realized that it was necessary to change their Asian supplier's mind to be more environmentally conscious.

In 2005, Alpha Network obtained a C-rank from EMC's auditing. The low rating embarrassed the CEO who then ordered all employees to tackle green product activities seriously to get the Fujitsu A-rank. With the support of Fujitsu EMC, Alpha Network introduced various measures in quick succession. It also adopted its original green product (GP) standard and the GP information management system.

Alpha Network's GP standard was based on RoHS standard compliance which has almost the same definition of hazardous substances as Fujitsu's. However, there was a difference in the allowable concentration value of cadmium and its compounds. The maximum allowed by Fujitsu's standard was 75ppm, but Alpha Network's standard allowed a maximum of 100ppm. Fujitsu's 75ppm standard was according to the standard of the Netherlands, which was stricter than the 100ppm standard of EU.* Fujitsu and Alpha Network discussed this issue carefully, and Fujitsu finally agreed to accept Alpha Network's standard. One reason was that Alpha Network had many customers other than Fujitsu. Hence, it was not reasonable to impose Fujitsu's 75ppm

* After the revision of the Green Procurement Direction in May 2007, Fujitsu changed the standard from 75ppm to 100ppm.

standard that other customers did not require. In addition, Alpha Network's GP management system seemed very reliable and was designed to minimize environmental risk.

In order to maintain GP quality, the lead-free operation area was separated and materials from the material receiving area to the finished goods warehouse were labeled "GP" for identification. In the Dongguan factory, there were two types of production lines: one was non-GP and the other was GP line. "G" was added at the end of the original P/N to make it easy to identify green products. Even tools, baskets and other devices which were used for production were separated into two categories, GP and non-GP. Shop floor workers are also separated into two groups, GP and non-GP. Alpha Network experienced a mix of GP and non-GP products in 2005, but in 2006 and 2007, no such mix was found. In 2006, 83% of GP products were ready for mass production and 85% of total materials were GP materials.

While Fujitsu exerted much effort in the beginning to help Alpha Network in pursuing the GP track, Alpha Network had since then aggressively established its own dynamic chemical substances management system. Through these efforts, Alpha Network was awarded certification not only by Fujitsu but also by its major customers.

Fujitsu and CSR Supply Chain Management

Company Profile

The communications division of Fuji Electric (now Fuji Electric Holdings Co.) was spun off into Fuji Tsushinki Manufacturing Corporation in June 1935 to manufacture communications devices. The name was changed in 1967 to Fujitsu Limited. At present, Fujitsu is a leading provider of customer-focused IT and communications products for the global market.

Fujitsu recognizes that IT permeates nearly every aspect of daily life, greatly expanding convenience and producing dramatic changes in the way things are done. Along with this trend, Fujitsu believes that IT systems deployed in business and social infrastructures have become increasingly sophisticated and complex, and the requirement for high system reliability is more important than ever. Therefore, Fujitsu continually seeks to create new value by providing customers with comprehensive solutions comprising highly reliable high-performance products and services based on powerful technologies. Based on a thorough understanding of the environments in which the customers operate, the overall nature of its operations and its business challenges, Fujitsu creates and deploys IT solutions that contribute to the growth and development of its business. Moreover, Fujitsu fully realizes that the stable operation of IT systems is critical in supporting the activities of business and society as a whole, and therefore Fujitsu is renewing its focus to improve operational quality. In so doing, Fujitsu seeks to grow together with its customers as a valued and trusted business partner.

As of the end of March 2006, Fujitsu's employees totaled 158,000 and its net sales amounted to 4,791.4 billion yen.¹ In fiscal year 2005, in order to provide comprehensive solutions that combined world-class hardware, software and services and ensure high customer satisfaction, Fujitsu reclassified the business segments from a product and technology-focused orientation to a customer-centric categorization. Fujitsu's major business segments were: 1) Technology Solutions

¹Consolidated financial figures for fiscal year ending March 2006.

(consisting of two sub-segments as System Platforms and Services), 2) Ubiquitous Product Solutions (PCs/mobile phones, hard disk drives and others) and 3) Device Solutions (LSI Devices, electronic components and others). With the change in the business segments, Fujitsu has added the term “solutions” to each segment to clearly emphasize the business objectives at Fujitsu which is to provide solutions that convert technology into business value for its customers. Shares of the net sales by business segments were 57.4% for Technology Solutions, 20.4% for Ubiquitous Product Solutions, 13.6% for Device Solutions, and 8.6% for the other operations.

Fujitsu avoids a one-size-fits-all global business approach and pursues instead business development strategies tailored to specific regional markets. Overseas, Fujitsu is now developing its business operations through 70 locations. Some 33.2% of the net sales comes from overseas operations (14.4% from Europe, 8.1% from the Americas, and 10.7% from Asia, Australia, and others). Currently, outsourcing services to the public sector in the UK are performing well. This is also true with the optical communications business in North America, and sales of the system platforms in Europe and the US (due in good part to Fujitsu Siemens Computer).

Fujitsu CSR Philosophy – The FUJITSU Way

The FUJITSU Way, which was introduced in 2002, is the core set of principles guiding the corporate and individual actions of the Fujitsu Group and their continuing development as good global corporate citizens.

The FUJITSU Way underlines the great importance that management places on customers, employees, environment, and quality and makes explicit the values they associate with each of these. Fujitsu believes that focusing equally on all these areas enables them to contribute to the well-being of their stakeholders, suppliers and customers, local and international communities, public entities and administrators – and as a result helps foster the profitable growth of the Fujitsu Group. Underlying this thinking is its commitment to promote the concept of sustainability. Meeting this commitment requires highly integrated efforts encompassing several different aspects of corporate activity: a social aspect, wherein the corporation fosters fair and honest work practices and a respect for human rights; and an economic aspect, wherein the corporation pursues sound and efficient management and seeks to explain its actions by providing adequate disclosure of information. It also requires an environmental aspect, wherein the corporation promotes global environmental protection initiatives ranging from actions to prevent global warming to actions that help build a recycling-minded society. Fujitsu hopes to continue meeting the expectations and earning the trust of its stakeholders by demonstrating measurable results in each of these so-called triple bottom line areas. As the core set of principles guiding Fujitsu’s socially responsible corporate behavior, The FUJITSU Way is the inspiration for all business policies, plans and Group-wide activities (See **Appendix 2**).

In July 2004, The FUJITSU Way Promotion Council was established in order to accelerate its penetration and implementation as a body reporting directly to the Management Council and a Compliance Committee. In addition, Fujitsu realigned the Risk Management Committee and Environmental Committee, which both had previously operated independently, under The FUJITSU Way Promotion Council.

To promote risk management, The FUJITSU Way Promotion Council continuously monitors the implementation of risk prevention measures by working to raise awareness of risks and by gathering information on specific risks, including potential ones. In anticipation of the enactment of Japan's Financial Instruments and Exchange Law, in the second half of fiscal 2005, Fujitsu launched a project to construct an internal control system that would ensure the validity and

credibility of financial reports. Along with establishing a promotion organization dedicated to this endeavor, Fujitsu is working to extend the system across the Group, including domestic and overseas subsidiaries. The goals of the project also include achieving greater efficiency through the pursuit of business process reforms across the Group (See **Appendix 3**).

Among the various CSR issues, Fujitsu has strong orientation towards operating in harmony with the environment since its earliest days. Fujitsu does not regard environmental protection as a cost, but rather as a key corporate value. Based on this stance, Fujitsu engages in a wide range of leading-edge environmental activities. As a result, the globally integrated certification of Fujitsu's environmental management system Fujitsu acquired in March 2006, under the ISO 14001 international standard. The concept of business operation in harmony with the environment is taking even firmer root in Fujitsu's corporate culture.

CSR Supply Chain Management

Recognizing a growing awareness of the importance of CSR, Fujitsu is working with its suppliers to ensure that procurement activities are carried out in accordance with CSR principles throughout the entire supply chain. In April 2005, the CSR Reinforcement Department was established in the Procurement Planning Division of the Procurement Unit. In March 2006, the Procurement Policy was published. This policy emphasizes: a) coexistence with suppliers, b) fair and proper evaluation and selection of suppliers, and c) promotion of CSR conscious procurement activities.

Based on The FUJITSU Way, a basic stance on procurement was articulated under the theme, "Promoting CSR Conscious Procurement." At the same time, the CSR Procurement Guidelines were published, outlining for its suppliers various CSR-related considerations Fujitsu requires in order to do business. These guidelines stipulate items concerning the following: a) protection of the global environment, b) legal compliance, c) respect for human rights, labor, health and society, d) assurance of safety and quality of products and services, e) maintenance and promotion of information society, and f) fair trade and corporate ethics such as protection of confidential information and intellectual property, and prohibition of bribes.

Fujitsu's CSR supply chain management has just started, and Fujitsu is going to stipulate additional CSR measures as part of the criteria by which Fujitsu can evaluate and prioritize its suppliers. Fujitsu is also planning to boost the CSR related support for its suppliers by providing assistance in developing environmental management systems, hosting CSR related seminars, and so on. The CSR conscious procurement activities covered domestic suppliers at first, and then expanded to international suppliers. Fujitsu's CSR supply chain activities would follow the same way that its green procurement activities did.

Further Considerations

With the rapid progress of globalization, MNCs (Multi-National Companies) have extended their supply chain to developing economies. Their focus on the core activities, resulting in outsourcing of non-core functions, makes their supply chain more complex and sensitive. However, hazardous waste, hazardous chemical content, child labor and poor working conditions have become serious problems in factories located in developing economies. The concern about such environmental and societal issues is growing in government and society.

For example, Nike was criticized for sourcing its products from factories with low wages, poor

working conditions and human rights problems. These criticisms were fed by a series of scandals and public relations nightmares, involving underpaid workers in Indonesia and child labor in Cambodia and Viet Nam, that combined to tarnish Nike's image (Locke and Romis (2007)². These environmental and health problems occurred at their suppliers' plants and workers at these plants were not Nike employees and yet Nike was punished.

At present, international nongovernmental organizations (NGOs) are very much concerned with the working conditions in electronics and IT factories in developing economies. Their interest in the electronics industry stems in part from some improvement of the supply chain conditions in the textile and food industries which they used to criticize. Other reasons for this interest are: 1) remarkable influence of electronics on society through worldwide spread of IT, 2) pollution resulting from hazardous substances at production and disposal stage, and 3) the industry lends itself well to CSR because young people are major customers of electronics products such as mobile phones and personal computers (PCs).

In today's society companies have social responsibility not only to themselves, but also to their suppliers. Hence, in addition to the traditional considerations of quality, delivery, and cost, their supply chain management should be concerned with environmental and social aspects. The companies are expected to develop and implement responsible supply chain strategies.

The EU introduced the RoHS Directive which defined maximum concentration of electrical and electronic equipment on 01 July 2006 and electrical and electronic manufacturers had to meet the maximum concentration of every single homogeneous material. Companies became responsible for hazardous substances in their suppliers' products.

Fujitsu has been leading green products procurement in the world and requires the highest standard from its suppliers. As a result, suppliers know that if they meet Fujitsu's requirement, they automatically meet other companies' standards and they can apply the same standards on their suppliers as well.

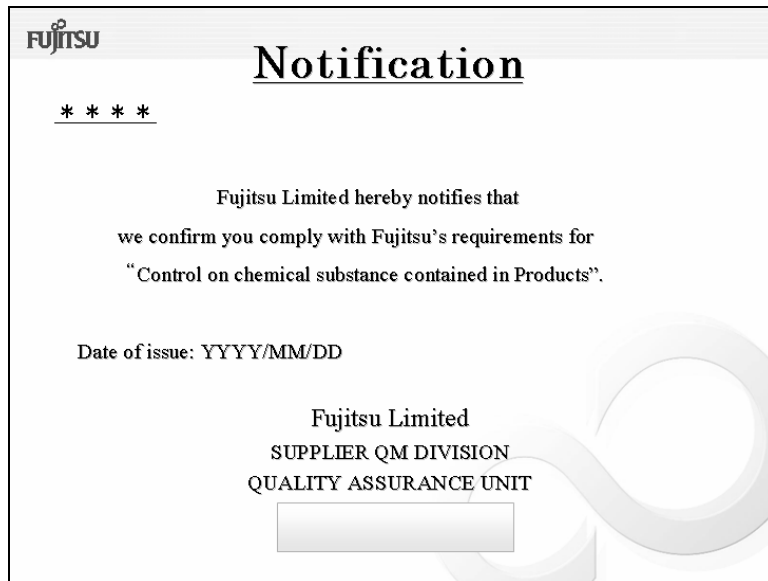
Just like other electronics companies, Fujitsu faces the problem of high worker turnover in supplier companies which reduces their capacity for greening the supply chain management system. Electronics companies are constrained to undertake continuous audit of suppliers which becomes an additional burden for them.

To address the problem, Fujitsu has established an overseas audit office, the EMC. The EMC makes it possible to have frequent communication with the suppliers resulting in mutual understanding or a *guanxi* relationship. According to Kambil et al. (2006)³, *guanxi* is "the effective use of social capital to advance business relations and is created through personal contacts, to bridge critical information gap, enabling favor based on trust or mutual benefits."

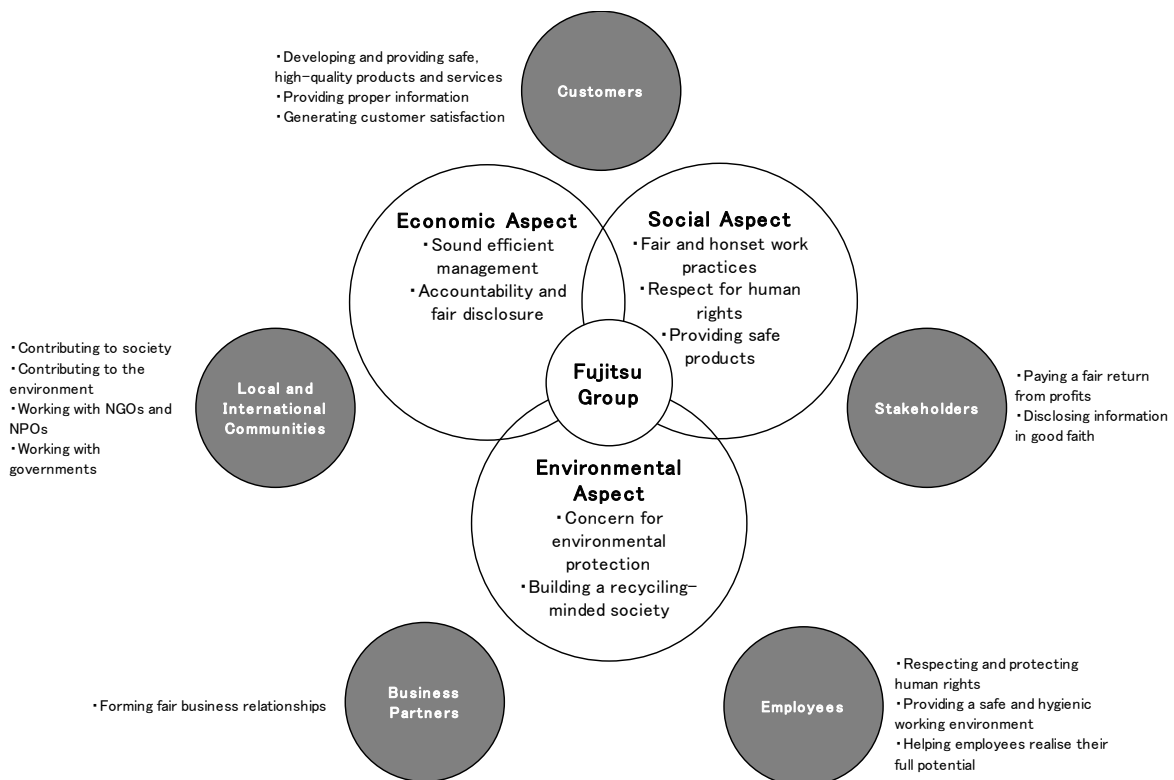
² Locke, Richard and Monica Romis, "Improving Working Conditions in a Global Supply Chain", *MIT Sloan Management Review*, 48,2 (Winter 2007).

³ Kambil, Ajit, Victor Wei-the Long and Clarence Kwan, "The Seven Disciplines for Venturing in China", *MIT Sloan Management Review*, (Winter 2006).

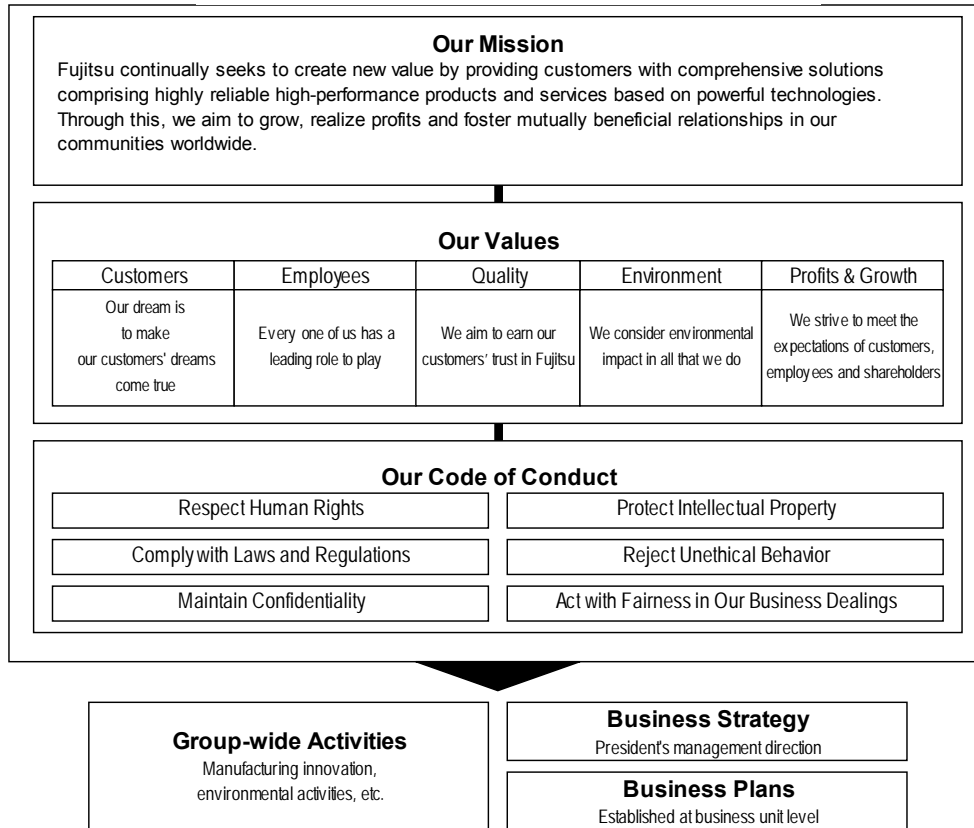
Appendix 1
Sample of Notification to Fujitsu Supplier



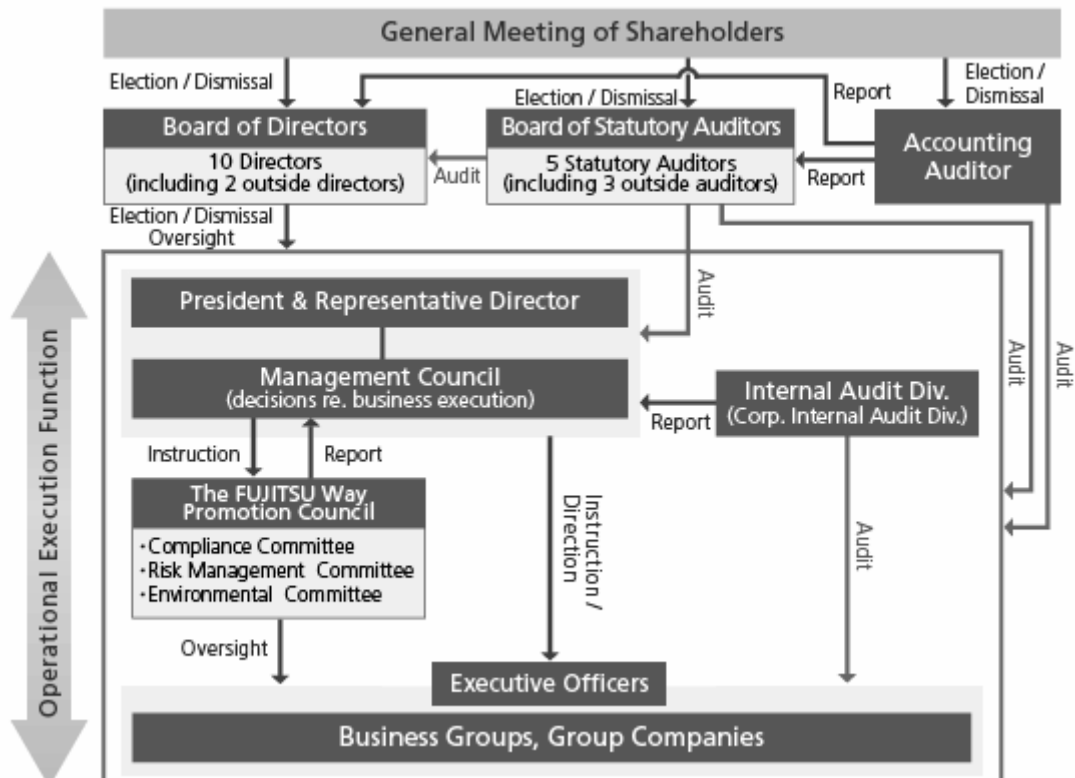
Appendix 2
The FUJITSU WAY



The FUJITSU WAY – Turning Dreams Into Reality



Appendix 3 Corporate Governance Framework (including The FUJITSU Way promotion organization)



Implementing Corporate Social Responsibility in Small and Medium Suppliers through the Value Chain of a Large Mexican Firm

Mexico

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The case was developed with the cooperation of ANAHUAC INSTITUTE FOR BUSINESS DEVELOPMENT (IDEA) – ANAHUAC UNIVERSITY, solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

CEMEX is one of the most dynamic and profitable global enterprises in the industry, being the largest cement producer in Mexico and the third largest in the world.

CEMEX's story of success, however, can also be linked to its deep commitment to the community and sustainable development. CEMEX has worked diligently towards building a corporate behavior that not only ensures returns to its shareholders, but also responds to societal and environmental concerns and values, making Corporate Social Responsibility (CSR) an important part of its business strategy. CEMEX is also committed to promote industry opportunities in CSR and its growing role in social and economic development is expected to continue.

Businesses are realizing that their response to demand for CSR is critically dependent on the behavior throughout their value chains of distributors, suppliers and clients. Large company influence can be an effective means to motivate small and medium enterprises (SMEs) to implement CSR measures. When more SMEs are motivated to act accordingly and achieve direct benefits, more small enterprises would likely become convinced of its effect on their businesses and thus interested in implementing CSR measures, generating a virtuous circle.

In 2006, CEMEX decided to participate in a pilot Mexican program with nine other "keystone" firms to support implementation of CSR measures among 10 of its small and medium suppliers.

This study focuses on the methodology employed by CEMEX and the other nine companies in implementing CSR measures among SME suppliers in their value chains. In particular, the following issues are discussed: a) the methodology used to develop a project work plan for implementing CSR measures among SMEs, b) CEMEX's ability to recruit and select 10 SME suppliers interested in participating in the program, c) the specific CSR priority areas that were transferred to the SMEs, and d) the development of indicators for monitoring and measuring impact of CSR implementation among smaller enterprises intended to capture the various CSR actions transferred from CEMEX to its value chain.

Finally, the conclusion of the study focuses on the analysis of the lessons obtained from CEMEX through its participation in the project "Implementing Corporate Social Responsibility Measures in Small and Medium Enterprises through the Value Chain".

These findings are also related to published studies on the benefits gained by large enterprises in disseminating their best practices along their supply chains, with the inherent understanding that the ultimate quality of the output of an integrated value chain cannot be greater than the quality of its weakest link. By the same token, quality management of the entire value chain is a vital tool of business management and a critical element in enhancing differential competitiveness. Consequently, responsible value chains can lead to a better relationship with suppliers, and improve public reputation as well as risk management policy.

Background

CEMEX is a growing Mexican company that produces, distributes and markets cement, ready mix concrete, aggregates and related building materials in more than 50 economies across five continents. In 2006, CEMEX achieved gross revenues of US\$18.2 billion, with an annual production capacity of approximately 93 million metric tons of cement.¹ In 2007 it announced that it expected to make investments of US\$1 billion in order to increase its operational income from emerging markets.²

¹ *Responsible Competitiveness Report, CEMEX*. Website: <http://www.CEMEXmexico.com/> (2005).

² Source: company information.

Founded in 1906, with headquarters in the city of Monterrey (located in Nuevo Leon, an industrial state at the northeast region of Mexico), CEMEX has evolved from a small local player into a global company with more than 65,000 employees throughout the Americas, Europe, Africa, the Middle East, Asia and South Pacific Basin.

For decades, CEMEX like many other companies in Mexico operated in a very protected and regulated environment, expanding operations only within the economy. Once the government abandoned the old model dominated by state inward looking policies however, the company was exposed to global competition under the new rules of a free market economy. This accelerated CEMEX's entry into the global markets in the nineties and in 1992, CEMEX started to expand abroad, buying the two largest Spanish cement companies, Valenciana and Sansón.

Under this scenario, CEMEX adopted a new and solid business model that led to explosive growth, acquiring companies (wholly or partially) and purchasing production and distribution facilities throughout the world. In 2005, it acquired the UK-based RMC for a total price of US\$5.8 billion (Hoyt, 2005: 3). But its biggest acquisition was made in 2007 when it acquired an Australian-based company, Rinker, thereby making the United States the most important market for CEMEX.

Since this new era of geographic diversification, CEMEX has not only reinforced its strategy to improve economic performance by achieving efficient operations, but has also pursued its transformation from simply selling "commodities" to selling "solutions".

Corporate Social Responsibility Path

The story of success of CEMEX reflects its unwavering commitment to society and the environment. Corporate Social Responsibility (CSR) has been integrated into the company-wide strategy. In particular, a solid commitment to the communities where CEMEX operates has enhanced the company's prestige and boosted consumer confidence.

The way social, ethical and environmental issues are incorporated into the day-to-day management business relies on three core values that support the integration of CSR issues into the company's strategy. These are: **collaboration**, working together with stakeholder groups in program development; **leadership**, essential in enabling a sustainable future for the company, industry, society and the world; and **integrity**, encouraging employees to adhere to the highest ethical standards and motivating them to assure compliance.

Table 1 summarizes CEMEX vectors of responsible competitiveness, which focus on four CSR activities and their specific courses of action.

Table 1:
Responsible Competitiveness Vectors

FOCUS ON CSR ACTIVITY	SPECIFIC COURSE OF ACTION
1. Community Involvement and Improvement Engagement in community programs that respond to shared corporate interests and promote a positive social environment.	Home building and improvement, as well as development of infrastructure in communities.
2. Employee Quality of Life Enhancement Commitment to ensure the best possible conditions to foster employees development.	Training for self-employment and Education
3. Environmental Protection and Preservation Essence of sustainable competitiveness, that guarantees a continuous improvement in environmental relationship through its conservation and rehabilitation.	Environmental Sustainability
4. Business Ethics Warranty that corporate behavior will be guided by the core values of the company, through their communication and implementation.	

Source: CEMEX 2005 *Responsible Competitiveness Report*, p.3.

CEMEX has developed a practical CSR matrix (Table 2) that allows it to track CSR results and impacts through various indicators. Nevertheless, since companies do not become model citizens overnight, CEMEX has worked diligently to advance through what has been called the “stages of organizational change,” moving toward the civil, and last stage, to directly promote industry opportunities in CSR (Zadek, 2004: 127).

Table 2:
CSR Matrix

VECTORS	INDICATORS	DESCRIPTION
1. Community Involvement and Improvement	1. Prosperity building 2. Quality of life improvement 3. Education and culture	<ul style="list-style-type: none"> Contribute to infrastructure improvement in communities at the base of the pyramid Build alliances for the development of social initiatives that contribute to the improvement of the well-being of local communities Promote educational excellence, encourage fine arts development and facilitate access to cultural assets
2. Employee Quality of Life Enhancement	1. Encourage the implementation of best working conditions 2. Work place security 3. Diversity significance 4. Knowledge for development and innovation	<ul style="list-style-type: none"> Enforce the creation of favorable conditions for employee engagement in corporate objectives, including CSR activities Promote a job security culture Guarantee the enforcement of equal opportunities and conditions Develop and strengthen capacities and abilities
3. Environmental Protection and Preservation	1. Maximization of environmental benefits 2. Harmonious relationship with the environment 3. Environmental management performance	<ul style="list-style-type: none"> Ecoefficiency Program Air Emissions Control Program and Waste Materials Management Natural Resources Conservation Program
4. Business Ethics	1. CEMEX values embedment	<ul style="list-style-type: none"> Resolution of cases by the Mexico Ethical Committee
5. Social Innovation	1. Innovate to add value 2. Best practices communication 3. Open communication to new ideas	<ul style="list-style-type: none"> Develop sustainable social solutions which add business value and benefit stakeholders Build alliances for CSR best practices dissemination Maintain an open and successful communication with external stakeholders

In 1997, CEMEX adopted a “continuous improvement philosophy” that led to a dramatic change in the way CEMEX addressed its supply chain management, as well as its market by focusing not only on production efficiencies, but also on meeting customers needs.

In terms of supply chain improvement, CEMEX has developed a very close relationship with clients, distributors and retailers. In order to enhance value to customers, CEMEX provided the products customers wanted at the needed time and location, which led to important structural changes in the management of the supply chain. CEMEX not only expanded its product lines beyond cement into construction materials, but also provided technical building assistance and efficient and comprehensive building solutions to their customers (e.g. *ConstruTips*)*. This way, CEMEX was able to leverage its global industry knowledge to deliver customized solutions to each local market, sector and channel. This had a positive impact on the satisfaction and diversification of customers, which included architects, homeowners and engineers in addition to the previous primary group of customers, the bricklayers (Hoyt, 2005: 11).

These learning experiences with customers helped launch programs such as “Patrimonio Hoy”, where low-income families were organized into self-financing cells and which facilitated do-it-yourself home building. This meant that for more than 160,000 Mexican families the dream of home ownership had become a reality. Community action went even further through the implementation of the “Piso Firme” Program. Under this program, CEMEX helped more than 200,000 disadvantaged families create a clean and healthy environment by replacing their dirt floors with unique antibacterial concrete. This program was implemented in partnership with federal, state and local governments in Mexico, and was starting to be implemented in Colombia for the poorest residents in the economy.

CEMEX developed several communication initiatives to stay close to their distributors. For instance, a group of distributors in each region met with the CEMEX staff to discuss new ideas and analyze the evolution of the programs. These forums proved to be very useful learning mechanisms, since the distributors who attended the forums cascaded down what they had learned to the other distributors in the region.

CEMEX also shared information on the latest technological devices with its distributors, training them on managerial skills and the usage of new tools, to avoid potential product shortages and provide superior service to customers.

The implementation of “Construrama” in 2001 allowed CEMEX to have a closer relationship with its distributors. Under this initiative, the company developed a very successful branding program embracing a large number of independent retailers. Distributors thus became part of a large and solid network, rather than being simply single, small local businesses. CEMEX offered training courses on basic business functions, helping distributors to improve their overall enterprise performance. They also provided computer access to advertising, insurance programs and financing. This way, Construrama retailers were able to adopt standard business practices that helped them transform and improve dramatically their business performance. This has resulted in a win-win situation, with stores sales of CEMEX cement increasing exponentially. This program demonstrates how a large firm successfully extended its benefits to small distributors and preserved local and regional employment as well.

CEMEX and other businesses in Mexico are realizing that their overall CSR strategy is critically dependent on the behavior of distributors, suppliers and clients along the value chain. Large companies can influence SMEs to implement CSR. As more SMEs are motivated to act accordingly and achieve direct benefits, more small enterprises will likely be convinced of its positive impact and will be interested in implementing CSR measures, thus generating a virtuous circle. This interrelationship is aptly demonstrated in the IDEARSE project.

* *ConstruTips* is a series of simple brochures that gives step-by-step instructions for tasks such as plumbing, electrical or concrete construction projects.

Large Corporations Supporting SMEs: Partners for Sustainable Development (The IDEARSE Experience)

In January 2004, the Inter-American Development Bank (IDB) announced that the Anahuac Institute for Business Development (IDEA, for its Spanish acronym), a think-tank of the Business Economics Faculty at Anahuac University in Mexico, had been chosen as the executing agency for the program "Implementing Corporate Social Responsibility Measures in Small and Medium Enterprises in the Value Chain". IDEA saw this as a great opportunity to promote a systematic adoption of CSR measures among Mexican SMEs.

While working on the draft of the project, we were convinced that improvements in competitiveness and sustainability of SMEs in the long run could only be achieved by embedding CSR practices in their daily operations and strategies. It was our intention to develop a managerial model based on quality and centered on values, that would allow SMEs to visualize tangible results from the adoption of CSR actions, beyond their merely legal commitments.

This was anticipated to be a difficult and challenging task, since this would require working closely with SME owner-managers and convincing them of the benefits to their business of being socially responsible. We also needed to ensure that these owner-managers understood that in order to obtain business gains, it was important to engage in CSR in a systematic, rather than in a sporadic, unstructured way.

We also had the challenge of overcoming the belief that only large companies had a role to play in CSR practices. It was crucial, therefore, to disseminate successful cases of socially responsible SMEs in Mexico and in other parts of the world. We had to demonstrate to them that, due to their financial, human and technical realities, these companies could actually adapt easier to different situations and could be more innovative and creative in the social arena.

We faced a basic question: how could we appeal to a great number of SMEs so they would adopt CSR principles that are embedded in the proposed managerial model, but in a more systematic way?

We started by recognizing the significant attributes that SMEs have: adaptability, innovation capacity, and first and foremost, community connections and local confidence. Since the beginning, we recognized that several obstacles might impede CSR efforts, such as: conflict of interests in allocating time and other scarce resources; strong pressure to deliver immediate results; lack of know-how and "know-who"; strong dependence on external consultancies, which were often outside of the reach of economic reality; and a misunderstanding of what CSR actually means which prevents them from having a more structured approach to its implementation.

Large companies can be important allies to SMEs in reinforcing the implementation of CSR measures and supporting their active role in the value chain. Their participation will also encourage SMEs to regard social and environmental responsibilities as fundamental aspects of their business practices. Furthermore, the large companies can serve as mentors sharing knowledge and information, which can lead them to adopt better business practices (OECD, 2001: 57-63).

The project submitted to the Multilateral Investment Fund (MIF) at the IDB, proposed a pilot initiative that incorporated the participation of 10 large companies and 100 SMEs (each large firm with 10 SME participants from their value chain) totaling 110 enterprises. The ten large selected companies had to have economy-wide and global recognition for their CSR reputation, had to be committed to provide the financial support, and were willing to collaborate and assist their selected SMEs, and help disseminate their best CSR practices among them. The intent was not only to seek a variety of economic activities and geographical diversity among the participating firms for appropriate representation but also to make sure that the large enterprises were from different parts of the world, including Mexico.

For Anahuac University, one of the top five private academic institutions in Mexico, the project meant reinforcing its social commitment, an issue it has always been identified with. In its more than 40 years of existence, Anahuac had a built-in reputation for the formation of leaders of positive action, and was socially recognized as a substantial contributor to the transformation of poor communities in Mexico and other parts of the world.

Since the foundation of the university in 1964, the Business Economics Faculty has worked hard to develop the entrepreneurial capabilities of young Mexican men and women. In 1996, when IDEA started operating with the main purpose of linking academics with the real world, it was clear for the university authorities that neither financial nor natural resources were enough to achieve Mexico's needed economic development, and that the creative and ethical initiatives of entrepreneurs were the most important engines to achieve it.

The project "Implementing Corporate Social Responsibility Measures in Small and Medium Enterprises through the Value Chain" added to a series of efforts of the public and private sectors in Mexico to encourage SMEs to adopt CSR as a corporate strategy and to highlight the benefits that could be derived from doing so. Needless to say, the entrepreneurial and social character of Anahuac University was strengthened by carrying out this important project that could have a positive impact on the future evolution of CSR in Mexico.

The Search for Committed Enterprises

In 2005 after nearly a year of planning and organizing, the operational and administrative unit for the program, IDEARSE (IDEA's Corporate Social Responsibility unit) started operations.

The main objective of the program "Implementing Corporate Social Responsibility Measures in Small and Medium Enterprises through the Value Chain" was to strengthen competitiveness and market opportunities for SMEs affiliated with participating corporations. Thus, the first stage was to find the 10 large enterprises that would participate and constitute the backbone of the program.

IDEARSE established relationships with two business associations. It signed a cooperation agreement with the American Chamber of Commerce of Mexico (AmCham), wherein AmCham would disseminate and promote the program, while IDEA would offer information to AmCham members on CSR best practices and would share learned experiences and applications derived from the program. The Japanese Chamber of Commerce and Industry had to send information on the program to their members and invite them to participate.

In this initial process, the Mexican Foundation for Innovation and Technology Transfer (FUNTEC, for its Spanish acronym), the SME brand at the Federation of Industrial Chambers of the United States of Mexico* (CONCAMIN, for its Spanish acronym), played an important role in promoting the program. FUNTEC led the development of the "Industry Ethics and Values Award**", which is a well-recognized award among private sector companies in Mexico. FUNTEC joined in the effort by inviting companies to participate in the program.

Two enterprises joined the program early on. The first one, Novartis, a European firm, is a leader in scientific research and pharmaceutical products that protect, improve and save lives. The second one, the Coca-Cola Company, an American firm, is the world's leading manufacturing, marketer and distributor of non-alcoholic beverages, concentrates and

* Institution constituted in 1918 that gathers all the industrial chambers and associations in Mexico, by the law of Business Associations and Confederations.

** This award was created by the Federation of Industrial Chambers of the United States of Mexico, to promote a culture of values and ethical behavior in industry, in general, and to publicly acknowledge to organizations, chamber associations and enterprises, committed with ethical and urgent community demand.

syrops. The third enterprise that became part of the project was Santander. The Spanish bank was one of the first banks to provide financial products to SMEs in Mexico, and the Board believed that the institution had a role to play in the implementation of CSR among SME suppliers and clients. Wyeth, the fourth company to incorporate into the program, is a very well-recognized American pharmaceutical company whose CSR staff had always had good relationship with Anahuac right from the beginning. The Japanese company, Sony, was the fifth to join the program; this enterprise received the invitation letter of its chamber and was interested to know more about the program.

Up to that moment, we had confirmed a group of five participating corporations, after having visited more than 40 leading enterprises in CSR. Hence, the executing agency had derived some learning experiences on how CSR was envisioned in the entrepreneurial community in Mexico, and how it was managed. Without question, CSR was recognized as one of the most important issues among the entrepreneurial community in Mexico, but the concept was still at the awareness stage, or at most was still going through an evolutionary process towards its adoption as a systematic business practice.

In some cases, we encountered a misunderstanding of what precisely CSR meant and the commitment it embodied. Nevertheless, it was perfectly clear that enterprises were expected to take greater responsibility for managing their impacts on society, although they did not know exactly what these impacts were, or even how to measure, control and evaluate them. It was even more surprising to learn that the Global Reporting Initiative (GRI) was only being applied by a few companies and remained unknown to most.

Consequently, we learned that CSR practices were different from firm to firm, and the process was emerging in very diverse directions, from merely philanthropic actions to being a major focus of the business strategy. In many cases, the implementation of CSR measures was a mandatory policy from headquarters located in other countries and transferred through standards and common codes of conduct, which typically included some business principles related to workplace safety, human rights, transparency and anti-corruption issues, consumer protection and environmental management.

In general, Mexican companies focused on a single area to implement CSR activities, particularly where they have identified the highest vulnerability. In addition, CSR engagement was lodged in different departments (Human Resources, Public Affairs, Marketing, among others), and only in a few cases was it considered an integral strategy that cut across all areas and levels of the company. Nevertheless, it was evident that CSR actions could only be effectively implemented when there was commitment from top management.

Partnerships and alliances especially those that involved the government, the academe and the business associations were seen as powerful mechanisms to help firms become more socially responsible and generate a positive business climate and a sense of mutual benefits.

In general, some corporations declined to adhere to the program, not because they considered CSR irrelevant, but because of time and staff constraints and a lack of development in CSR areas. So it was quite clear at this stage that there was a long way to go before we could build a culture and promote systematic adoption of CSR among companies operating in Mexico. But at the same time, IDEARSE was concerned about the lack of large Mexican companies participating in the program. This was unacceptable, considering that the program was being led by a Mexican entity within Mexico.

The Consolidation of the Group: Mexican Firms Momentum

The second group of five large enterprises consisted of CEMEX and the following: FEMSA, the largest integrated beverage company in Latin America; Grupo Modelo, the leader in the production, distribution and retailing of beer in Mexico; Grupo Zapata, a large firm leader in wrapping and packaging; and Homex, a large company belonging to the construction sector. The first three went through a long authorization process before

becoming part of IDEARSE, but once incorporated have played very active roles in the project.

Grupo Zapata's decision to join IDEARSE was due to the enthusiasm of one of the members of the Board who attended the second CSR Symposium devoted to the project diffusion and was impressed by the testimony of the two participating SMEs of the Coca-Cola and Santander projects. She informed the president and the CEO of Grupo Zapata that she wanted to meet again with the executing unit to understand better how IDEARSE would be implemented and what benefits could be derived from it.

Homex incorporation was made possible because one of the firms tapped to join the group was unable to join the program. Homex was referred to IDEARSE by one of its most important consultants while the company was seeking advice on how to improve its CSR practices. The methodology of SME intervention proved to be very interesting and a step forward in its efforts to adopt a coherent socially responsible strategy. Homex was the last firm to join IDEARSE which had by then visited 86 enterprises. Although its participation legally materialized only in February 2007, Homex sensitized and selected its 10 SMEs in a record time of one month.

CEMEX formally joined the IDEARSE program after a long period of presentations and interviews with various executives. When CEMEX signed its incorporation into the program in its headquarters in 2006, the CEO of the company who was there to sign the document gave a message to the Board of directors and Anahuac University authorities, represented by the Principal and the Dean of the Business Economics Faculty. One of his principal messages was that the signed agreement endorsed CEMEX's commitment to build a better future, and that its stakeholders were witnesses and participants of the company's vision. This was reflected in policies, practices and programs governing the daily ethical behavior of the company. By joining IDEARSE, CEMEX reinforced its commitment to support and mentor the development of SMEs and its social responsibility engagement. (For detailed description of CSR activities of each company, see **Appendix 1**).

The CEMEX Case: Making CSR Happen in the Value Chain

From what has been discussed it is obvious that CEMEX is an outstanding company based on its financial and commercial performance, providing the best working conditions for its associates, supporting the development of local communities, strengthening its relationships with its stakeholders and promoting the conservation of greater environmental responsibility.

In joining IDEARSE, CEMEX was attracted by the prospect of finding a systematic way to facilitate the development of its SME suppliers and retailers by sharing with them the company's CSR best practices. At the same time, the SMEs documented in a systematic way the CSR best practices standards included within the IDEARSE model that would help CEMEX obtain an accurate diagnosis of the extent by which CSR practices have been embedded in its own business strategy.

The levels of CSR established by the IDEARSE Model are: **Level 1 - Process not started** - in which the company does not have any evidence of the use of a methodology for implementing CSR measures; **Level 2 - Focus** - at this level the owner-managers are interested in CSR topics and implement them in an informal way; **Level 3 - Implementation** - the company has a well-established methodology that allows it to accomplish certain CSR practices in some of its areas or departments; **Level 4 - Improvement** - at this stage the company has a systematic methodology that consolidates the main CSR topics through all the areas.

The first task was to gather all relevant information that sustained CEMEX's CSR commitment. The objective was to analyze each action, taking into account the model principles of self-regulation, human rights, labor aspects, stakeholders, environmental responsibility, and community development. For each principle, various matching guidelines were formulated. For example, corporate core values were part of the first principle. At the same time, each guideline followed a concrete action, such as the elaboration of a code of conduct, as indicated in the example above.

In order to obtain all the necessary information to undertake this study, the IDEARSE consultants reviewed all the evidence related to sustainability and social responsibility reports. They also studied the self-diagnostic document submitted to CEMEFI, which constituted the basis for earning the emblem as a "Corporate Social Responsible Enterprise" in Mexico. In addition, the consultants met with the staff in charge of CSR in CEMEX, to understand better how the firm managed CSR programs and projects.

When this stage was completed, we were all clear that CEMEX was a leader in CSR having established policies, indicators and reports involving its stakeholders - the community and the environment were involved.

According to the IDEARSE Model, CEMEX is at the highest level of CSR maturity referred to as "improvement." At this level, the organization is considered as "outstanding", since it consistently adheres to its CSR practices and is able to share its best practices with its stakeholders. Two of the most important findings during this period were the recent initiatives undertaken by CEMEX - the development of a sustainability management system (SMS) and its participation in the Cement Sustainability Initiative (CSI). SMS is a tool that allows the firm to monitor the responsible management in the social and environmental aspects, allowing innovation and flexibility in each of its operating plants and among its other business units. CEMEX is among the core members of CSI, along with nine other major cement companies. The company is responsible for managing the initiative, identifying companies' commitments, defining and funding the work program and inviting new members. CSI was formed to help the cement industry address the challenges of sustainable development. Its main purpose is to identify and facilitate actions that companies can take as a group and individually to accelerate the move towards sustainable development.

Once the analysis of the main CEMEX CSR principles had been concluded, the next step was to invite a group of SMEs in its value chain to participate in the IDEARSE project. Just like in the search for the large firms, the selected SMEs must have a strong commitment and willingness to work towards managerial improvement to develop an integral approach to CSR.

Since the beginning, the IDB has established an annual sales limit of US\$5 million to categorize a firm as an SME and to participate in the program. CEMEX itself added some selection criteria in order to invite key SMEs, facilitate the recruitment process of its distributors and suppliers, and allow them to obtain a representative universe of the SMEs in its value chain. It intended to constitute a group having close relationship with CEMEX, preferably a long-term one, which recognizes that CSR could provide tangible benefits for them and that it requires more than a goodwill approach. Finally, it was considered important to have SMEs representing different economic sectors.

This was a great challenge for CEMEX because the company had to pre-select a group of SMEs from its large list of suppliers and distributors, without knowing in some cases their level of sales. The CEMEX personnel involved in the project then realized that the company needed a more efficient database, one which would allow the different departments to obtain more and better information on its stakeholders, especially its distributors and suppliers.

CEMEX and IDEA invited the pre-selected firms which met the criteria stated above. Each SME was invited to participate in an event, where the pursued objectives and benefits of the project were pointed out. Forty SME enterprises attended the event and reacted in various ways. Some owner-managers ignored the discussion on CSR topics; others were dubious about all the good things CSR could bring to their business; others appeared concerned due to their human resource and financial constraints. However, some SMEs readily accepted the invitation to participate in the project.

After visiting each firm, presenting the project information and responding to their inquiries, CEMEX selected 10 SMEs. These firms were into home-building, building materials, printing, personnel recruitment and outsourcing businesses.

CEMEX then organized a special event to formalize the incorporation of the SMEs into the project and to announce the next steps to be undertaken. Some small entrepreneurs and communication firms attended the event. An agreement among CEMEX, Anahuac University and the 10 SMEs was signed which clearly established the commitments and responsibilities of each. The vice-president for Institutional Relations and Communication of CEMEX thanked the SMEs for participating in the project. He invited them to take advantage of the opportunity to return some of the benefits they had received from their communities and establish businesses in which both parties could obtain benefits. He also affirmed CEMEX's continuing support to the project.

Soon after, CEMEX started working with the 10 selected SMEs. The first step was to run through an induction session with all the project participants. These sessions eased the initiation of the project and marked the beginning of the long path to be taken with these firms. We announced the objectives of the projects and the steps that were going to be followed: a) development of the baseline study, b) diagnosis of CSR actions, c) development of the plan for changing, e) plan implementation, f) impact evaluation and g) documentation. The sessions also established an appropriate work environment and secured the commitment of participants to play an active role in the project throughout the different steps. In other words, the evangelization process continued, but it was now focused on the SMEs and their people working in them.

Since the beginning, SMEs had been committed to the program and had been appreciative of CEMEX support for their participation. They were enthusiastic and helpful in collecting relevant information on their companies to facilitate the work of IDEARSE consultants.

In doing the baseline study, we were looking for the SME's financial data, organizational environment and leadership and business relationships with CEMEX, in order to develop a SWOT Analysis (Strengths, Weaknesses, Opportunities and Threats) for each SME. This analysis allowed us to have a good grasp of each business and its operations and personnel management. As a result of these initial analyses, we were able to determine certain characteristics that could be considered as common to all SMEs in Mexico. These included some positive attributes such as flexibility and capacity to respond quickly to customers' demand, and innovation and creative capacities in the business. But it also demonstrated some weaknesses such as the lack of structure and organization which had negative impact on the company's efficiency and prevented owners from doing short and medium-term planning.

By that time, we had already identified several value generating areas that were discussed with each of the owner-managers of the SME's in order to develop different activities that would improve their daily performance. In general, their main concerns were improving financial performance, building a labor environment that guaranteed clients satisfaction, and involving human resource in this new organizational culture.

During this analysis, we witnessed the excellent relationship that CEMEX maintained with its stakeholders, and the good opinion that the stakeholders had of the company. The vast majority of the SMEs participating in the project were CEMEX distributors who considered themselves part of a large network. The suppliers who were invited were also aware of CEMEX's interest in enhancing value-added aspects of their activities. It was not surprising then that CEMEX provided its SMEs additional consultancy beyond those offered by the project in critical areas, such as the business code of conduct elaboration and the development of health and safety activities.

Later on, in order to obtain a complete CSR diagnosis, further information gathering technique called Diagnosis Matrix was used. The matrix is divided into the six main principles established by the IDEARSE model, known as: self-regulation, human rights, labor aspects, stakeholders, environmental responsibility, and community development. For each principle there are various guidelines, and for each one of those, there is a concrete action that follows. Consultants hired by IDEARSE showed how the instrument could be effectively used. Upon application of the instrument, the owner-managers realized that their respective companies had already implemented several CSR activities, but not in a holistic and structured way. This was a turning point, as SME owner-managers began to understand the benefits to their business of being socially responsible.

Upon being shown the matrix results, many owner-managers became enthusiastic in implementing corrective actions immediately. Others however had to wait until the entire group was analyzed since the process had to be finished together, in order to achieve economies of scale. As was expected, firms reacted differently. Some of them immediately helped the consultants complete the Diagnosis Matrix, while others took their time according to their priorities and responsibilities.

The subsequent step required each SME to work on its Plan for Changing. This was specifically designed to fulfill the needs identified in the diagnosis process. In this step, the owner-managers were deeply involved in formulating a plan that fit their requirements. They shared and discussed the plan with their staff in order to identify immediate actions that would have a positive impact on the company.

The positive attitude and motivation of owner-managers have been fundamental factors for the development of the project. Their active participation in each and every activity hastened completion of some stages of the project.

The findings reinforced the interdependence of certain activities within the value chain, which provide CEMEX distributors and suppliers a competitive advantage in the market. The techniques that these companies used to conduct logistics, service delivery, marketing, human resource management, etc., were tailored to offer a unique added value. By adopting best CSR practices, these companies will attain a superior performance, as each company is expected to reach a superior level of CSR, or at least have initiated the process, by the time the project is finished.

Learning Experiences in SMEs

Working with SMEs throughout the value chain of huge corporations has been a very gratifying experience, both for the consultants and for IDEARSE. This is not only because of the learning experiences obtained from the project, but also of the transformation towards a quality model based on values that the enterprises have achieved.

The results drawn from the SME analysis reflect several problems with their internal organization. We found that a lot of enterprises lacked the basic elements of a business plan, such as mission,

vision and short and medium term objectives and goals. They also had to overcome the lack of clarity on human resource performance and responsibility. Most of the SMEs participating in the project demonstrated only an anecdotal way of communication and did not have in place a well-established system with embedded standards. A lot of companies also showed that their inefficiencies in managing their business were, to large extent, caused by family-related issues (small Mexican firms are generally family-run businesses), which limited the strategic development of the business.

In general, the lack of a strategic focus is a serious obstacle for the future of the company. The inadequacies that SMEs face in terms of time, resources, etc., cause their operational processes to inhibit their strategic directions, frequently impeding the possibility of obtaining results and growth.

A lot of SMEs showed a proactive attitude when shown the results of the CSR analyses. Many of them started to implement some measures even before the Plan for Changing was started to counteract the negative impact that family relationships could have on management. They tried to understand better the negative consequences of family relationship and the essential changes needed in order to enable their businesses to operate under higher corporate governance standards. Some enterprises, however, demonstrated some resistance to change. This was specially true when an investment was needed to transform them, even if the financial resources needed were not significant. Sometimes, this represented a critical point among consultants and owner-managers were encouraged to use more creative methods of communicating, or ways to resolve these financial shortages through government and state funding.

We also found that a lot of duties were concentrated in a few workers, which limits SMEs from responding effectively to their clients (including large enterprises) and ensuring the quality required in the process. This reality, along with the lack of strategic planning related to achieving the targeted objectives, were key factors that affected the individual SME's performance and future prospects.

In most of the enterprises, we found a general openness for new ideas and flexibility to adopt the required change; however, enterprises showed more resistance to the processes which they did not fully understand or posed a higher risk.

In every single one of the value chains, the SME participants were very satisfied with the support of the large enterprises, and were thankful that they were invited to be part of the IDEARSE program. It is interesting to note that when the large enterprise showed great flexibility in transmitting its best CSR practices, the SMEs responded faster.

The SMEs requested that IDEARSE establish more communication channels among them so that they could learn from the experiences of other enterprises. Consequently, IDEARSE designed a monthly newsletter containing relevant news about the participating SMEs, highlights of CSR issues, and successful cases of firms that have adopted CSR measures.

It was very gratifying to see that by joining this CSR project with large firms, IDB and Anahuac University, some enterprises were able to obtain new contracts. Market acceptance was, in this sense, a good ally for stimulating SMEs' interest in implementing the identified corrective measures.

It is clear that CSR is a long process and in many cases it requires courage to take action, even when the social return cannot be seen in the short run. Nevertheless, when the process of change is initiated, the possibility of entrepreneurs sharing their experiences with other SME owner-managers from different industries has a lot of value, and encourages them to continue in this path.

It is also important to point out that beyond the strategic value due to the competitive advantages gained by the firm, the multiplier effect of the IDEARSE program was evident. Many SMEs, for example, were interested in transferring the recently adopted CSR principles to other small businesses in their value chain.

The *modus operandi* of a program of this kind requires a large amount of input from consultants, but multilateral organisms, large enterprises and SMEs, academics, chambers and associations, which have complementary federal and state funding can be strong engines of change. Enterprises, being value and wealth generators, when operating under CSR principles can be turbo engines of growth and sustainable economic development.

Appendix 1

IDEARSE Program: The Other Nine Large Companies Committed to CSR*

Novartis

Novartis, a leading Swiss pharmaceutical company, has maintained a long-standing relationship with IDEA, as its academic partner in the creation of its corporate University, UNO. For Novartis, entering the project represented a step forward in its corporate citizenship commitment, as an active player in CSR practices which has led the company to achieve important recognition, such as: the “Great Place to Work” and the “Industry Ethics and Values” Awards, and to obtain the emblem “Socially Responsible Enterprise” awarded by the Mexican Center for Philanthropy. CEMEFI is a non-profit private institution, founded in 1988, whose mission is to promote philanthropy and social responsibility culture in Mexico, as well as to strengthen organized participation of society.

The Coca-Cola Company

The Coca-Cola Company, a recognized leader in CSR, decided to enter the project, because it perfectly fitted into its Corporate Citizenship Principles, all of them integrated in its business strategy.

The success of the Coca-Cola Company depends on every employee in the organization and sustainable growth for the firm means ensuring that each member of the Coca-Cola family continuously grows as a member of a team that works together for a common purpose. In Mexico, Coca-Cola Export is one of the three largest employers. Its remarkable commitment to the micro-distributors of its products, not only help them to build their capabilities, serving as enablers, teachers and coaches, but also transferring learning experiences, technological support and effective sourcing strategies to them. The environmental management system is critical to the company's interests. Because of the main impacts of the business, the organization has concentrated a significant portion of their efforts on ozone protection, water resource and energy management, and post-consumer recycling.

When the IDEARSE program began it was understood that, aside from the benefits that the 10 large companies would achieve through their participation, this initiative would also provide a benchmark for clear mechanisms that would measure the impact of social actions in SMEs. In addition, it was expected that large firms could share learning experiences of different CSR approaches with other businesses in other industries. The IDEARSE program would also help to extend their CSR experiences and practices at the local level. Coca-Cola Export, for example, started an interesting initiative among the group of large companies, by sharing its Quality System. The Coca-Cola Quality System (TCCQS) embodies the requirements of globally recognized standards for quality, safety and environment. This is what was expected from the IDEARSE program, that is, that the network would provide a powerful mechanism for helping firms to become more socially responsible. It was made clear from the initial conversations with the large firms, that the program did not want donors, but committed organizations.

Santander

Santander, a Spanish financial institution, not only established a specific area to offer services to SMEs, but was also very innovative in the conformation of a portfolio of financial instruments that gave more flexibility and credit access to these entities. But Santander has also distinguished itself, because it supported a variety of programs for the educational and cultural development of young students, through well-established programs, such as “Portal Universia.” “Portal Universia” is an initiative of Grupo Santander Central Hispano, created in 2000, in Spain. Its main objective is to provide an academic network that includes universities, professors, researchers and students, generating a favorable environment for communication between young people, in 10 economies where the program operates. Unlike the other two enterprises, Santander contacted IDEARSE staff following the advice of the IDB. When the program was presented to several bank authorities, the decision to join the IDEARSE project was automatic. The financial institution focused on developing an efficient risk management system, as a mechanism to generate value in a permanent way. This would imply, among other things, a rigorous application of CSR practices. Thus, the IDEARSE program was in line with their thrust.

* Companies are listed in the same order as they were incorporated into the IDEARSE Program.

Wyeth

Wyeth, a leading American pharmaceutical company, had integrated a very experienced team that had led the organization to achieve recognition in business social accountability. Wyeth is acknowledged as an organization that stands out because its employees are proud of their work. Its Human Resources best practices are recognized because of leadership in processes, design, implementation and continuous improvement. The company also distinguishes itself for its relationship with the community and care for the environment. During the implementation stage of the project, Wyeth decided to finance a cluster of medium enterprises that, because of their size, did not fit into the program category established by the IDB for SMEs (annual sales of US\$5 million). This initiative went beyond the original project and Wyeth demonstrated again its commitment to support their suppliers who had shown a lot of enthusiasm towards the project. The cluster would work in parallel with the other 10 SMEs thereby activating the program's desired multiplier effect.

Sony

In Sony, an outstanding Japanese manufacturer of audio, video, communications and information technology, CSR had been integrated into three main areas: leadership, environmental management and commitment to the community. To pursue its commitment to the community, Sony Mexico has developed two outstanding programs: "SomeOne Needs You" and "SHARE" (Sony Helps Around Enterprises). The first one is a program of voluntary service, designed to improve community outreach that contributes to enhance the quality of life and help disadvantaged residents and victims of tragedies. This program is adapted to community needs, and personnel participation is motivated. The second one consists mainly of sharing the company's best practices with their stakeholders. The project "Implementing Corporate Social Responsibility Measures in Small and Medium Enterprises in the Value Chain" perfectly fitted with "SHARE" objectives. When Sony signed the agreement with its 10 SME suppliers and distributors, the CEO of the company led the event, reinforcing the belief that CSR is a valued asset in the life of the company, and that this is shared by all throughout its value chain.

Femsa

Founded in 1890 in Monterrey, Mexico, FEMSA is comprised of three complementary business units: FEMSA beer, Coca-Cola FEMSA and FEMSA Commerce. Its main brands are: Sol, Carta Blanca, Tecate, Dos Equis, Coca-Cola and Sprite, among others. FEMSA has been very active in promoting the continuous improvement of the quality of life and living standards of its employees, reducing to the minimum negative environmental impact of its operations following standards beyond those required by the law, and generating positive impact. Femsa has social investments in a variety of programs. For example, "Designed Driver" or "Responsible Waiter" were established in order to promote more moderate alcohol consumption and car accidents reduction. These actions have made FEMSA a well-recognized and awarded firm in CSR.

Grupo Modelo

Grupo Modelo, a Mexican leader in producing, distributing and retailing beer in Mexico, has developed a very successful branding system. It has at least 10 trading marks, with global, economy-wide and regional character. One of its products, Corona Extra is dubbed as "the most sold Mexican beer in the world". With presence in more than 150 economies, Grupo Modelo has been very active in promoting Mexico and its cultural values in the world. Grupo Modelo has developed specific CSR programs that go beyond its legal obligations. Filantropia Modelo, A.C., founded in 1998, was the result of a solid company history of commitment to ethical values and its contribution, particularly, to social vulnerable groups, and its search for a more efficient way to manage resources provided by the different firms of the Group.

Grupo Zapata

Grupo Zapata, founded in 1926 as a small Mexican family business, has evolved to become a large firm leader in wrapping and packaging. The present administration is taking a more strategic approach in its CSR efforts by adopting a business model that is based on these principles and on ethical values. The company has recently modified its structure and established a specific unit that coordinates the CSR initiatives. Grupo Zapata sees its workforce as its main stakeholder; hence, it does not only preserve workers' rights and provide them fair pay and a safe working environment, but also actively supports in training them so that the workforce can obtain certain qualifications and capabilities. Its

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social responsibility activities are also extended to other important stakeholders, such as workers' families and local communities. Its incorporation into the IDEARSE program reflects Grupo Zapata's belief in SME suppliers as important drivers of CSR principles in its value chain.

Homex

Homex is a firm belonging to the construction sector, with headquarters in Culiacan, in the State of Sinaloa, in the northwest region of Mexico. Although Homex is a recently constituted Mexican enterprise, its growth, along with its built-in reputation for being socially responsible has been phenomenal. Homex is truly committed to improve the quality of life of its workforce and its families and develop the local community through the provision of quality home-building at affordable prices. Other key CSR issues involve the adoption of equal opportunity policy in hiring. The enthusiasm that exists in the company has spread to the staff and has made them more committed and productive as seen in reduced cases of staff turnover and absenteeism.

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Corporate Social Responsibility in an International Supply Chain

New Zealand

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The case was developed with the cooperation of a company that wishes to remain anonymous solely for educational purposes as a contribution to the Project entitled "New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -" conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

This case discusses a situation in which good Corporate Social Responsibility (CSR) practices were instituted in a supply chain extending from China to New Zealand and Australia. This was accomplished through the forceful and consistent efforts of a supply chain logistics intermediary, ABS Logistics.

ABS Logistics helped a New Zealand manufacturer, Woodward Laundry Products, contract out a portion of its manufacturing to a Chinese firm named Conghua Metals Company, with the assistance of a North American sourcing company, Hayden International Sourcing.

In spite of the generally low level of visibility in New Zealand of human rights and labor abuses by contract manufacturers in many low-cost labor economies, ABS Logistics did not only persist in developing its own CSR policy in this area but it also convinced Woodward Laundry Products (the customer) to institute a similar policy. The two firms required similar policies and compliance on the part of Hayden International and the supplier, Conghua Metals.

The case describes the companies involved, the nature of the supply chain and the activities conducted, and the lessons learned from the process of instituting good CSR practices in a supply chain.

The good practices illustrated here include formulating a CSR policy, inculcating the meaning and application of the policy among the employees, persuading both customers and suppliers to comply with the policy, and putting in place methods to ensure continued compliance by all parties. But the most important characteristic of an effective CSR policy is the will of the firms involved to make sure everyone lives up to it.

Introduction

This case deals with four parties in an international supply chain stretching from China to New Zealand and Australia. The players in this supply chain consist of a New Zealand manufacturer (Woodward Laundry Products Limited), an international logistics company based in New Zealand (ABS Logistics), a service provider known as a “sourcing” company founded by North Americans and operating in China (Hayden), and a manufacturing company in Guangdong Province, China (Conghua Metals Company).

Woodward Laundry Products of New Zealand is a manufacturer and supplier of metal and plastic laundry products to the New Zealand and Australian appliance retail, building and plumbing industries. The Woodward product range includes laundry tubs, ironing centers and ducting. The company enjoys a strong market share in New Zealand (over 50%) and is a growing presence in the Australian market. Since its founding in 1982, Woodward has manufactured its complete product range at a factory in Auckland, New Zealand.

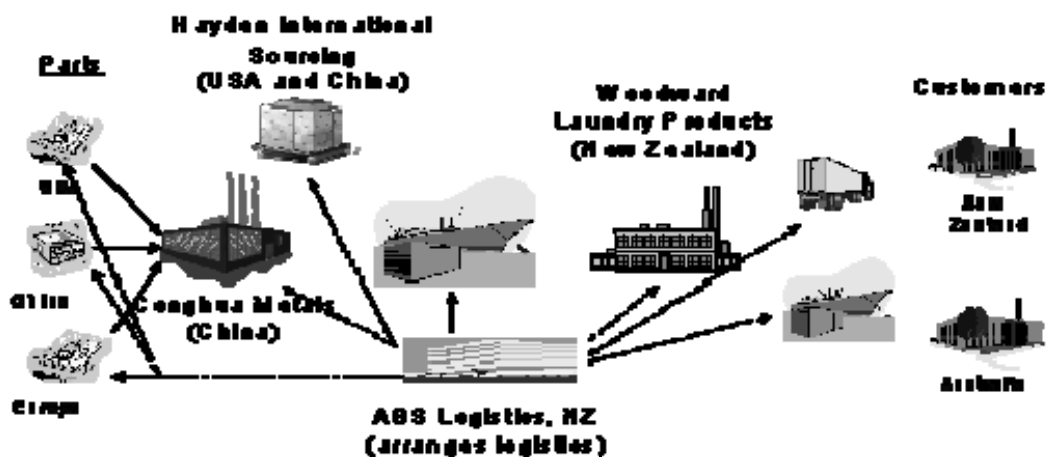
As Woodward’s preferred supplier of international freight services for the last 14 years, ABS Logistics transported and imported components and sub-assemblies to Woodward from Australia, the United States, Europe and Asia. The company subsequently exported finished products from New Zealand to Australia. In 2005, however, Woodward learned that just like in many other industries, the dominant position the company had historically enjoyed was under threat from alternative products sourced from Asian economies, particularly China.

While this threat was not altogether new to Woodward, the company had been able to maintain good business before on the basis of fast delivery and the high quality of its finished products.

However it was becoming apparent that quality and delivery performance alone would not be sufficient for Woodward to protect, much less grow, its market position. Given this situation, the company decided to explore the opportunity to move some or all its manufacturing activities to China.

In early 2006, Woodward chose ABS Logistics International to lead this investigation because of the firm’s wide experience in importing and exporting, and in running international logistics operations. Woodward and ABS Logistics jointly studied a number of sourcing companies with in-depth knowledge of Chinese manufacturers. After a detailed search, the two companies finally appointed Hayden International Sourcing, a North American-owned company, to find a manufacturer capable of meeting Woodward’s needs and assisting its operations. Using Hayden’s detailed knowledge of Chinese manufacturing practices and companies, the three parties selected Conghua Metals Company as the supplier for the bulk of the product range required by Woodward. Conghua Metals was a manufacturer based in the Guangdong province of southern China. **Figure 1** shows a schematic diagram of the supply chain that this multi-firm collaboration ultimately employed.

Figure 1:
The Supply Chains and Its Participants



The issue of Corporate Social Responsibility (CSR) surfaced relatively early in the search for a Chinese manufacturer. ABS Logistics, in particular, realized that it was taking on a whole new set of activities and relationships that presented a variety of risks for the firm.

This case describes the interesting development and evolution of ABS Logistics’ recognition of CSR and the approach that it adopted. ABS Logistics did not only have to address issues of CSR internally; it also had to be sure that the entire supply chain also developed the necessary CSR policies and culture so that the firm could protect its own reputation in the supply chain and in any future business.

The ABS Logistics Group

The ABS Logistics Group was founded in 1980. The transport industry environment in New Zealand at that time was highly regulated, requiring all freight traveling over 150 kilometers to be moved by rail. The market was dominated by several giant transport companies. When

deregulation occurred in 1985, ABS Logistics evolved rapidly to become one of the major firms in the New Zealand logistics sector.

ABS Logistics International was created as a subsidiary of ABS Logistics in 1984. The subsidiary company established a beachhead in Australia in 1992, with an operation in Sydney, followed in the next few years by depots in Melbourne and Brisbane. It invested in Australia in pursuit of its vision to have a single Australasian logistics and freight market.

ABS Logistics became a publicly listed company in June 1998 and later added interests in the United States and Southeast Asia. As of 2007, the firm has already established an office in China to take care of its business with firms exporting to Australia and New Zealand, as well as with firms importing from those two economies to China.

ABS Logistics Limited is a fully integrated service company. The business incorporates a number of different brands dealing with business activities ranging from door-to-door domestic and international transportation and managed warehousing, to specialist divisions offering dangerous goods and temperature-controlled transport and warehousing. Like many other international logistics companies, ABS Logistics focuses on bringing complementary services together to achieve integration of the activities in their customers' supply chains.

ABS Logistics has a simple and logical management philosophy, which is, build a strong team culture, promote from within and reward good work. The firm has a relatively flat organization with little hierarchy or bureaucracy. Everyone is treated as an important link in the firm's chain of activities. The headquarters operates in an open-office plan; even the Chief Executive Officer (CEO) holds office in the open with the rest of the employees.

Hayden International Sourcing Company

Hayden was formed in the mid-1990s when two Americans who had worked for a large multinational firm in China for many years as production coordinators decided to go into business for themselves. Their job which involved working with Chinese-owned contract manufacturing companies which were doing business with their employers gave them considerable experience. Being fluent in Chinese, the two set up their Hayden operation in Hong Kong, China and began soliciting business from smaller western companies that wished to take advantage of low-cost manufacturing options in China.

Sourcing companies are consulting firms that specialize in seeking out firms in Asia, primarily manufacturers, who can meet the needs of buyers looking for low-cost, high quality production. Most of the potential customers of the sourcing companies have relatively little experience in doing business in places like China, little knowledge of local customs and regulations and limited Chinese language skills. Thus, a sourcing company that has all these capabilities can be a very valuable resource.

The presence of these sourcing companies has become widespread. The biggest and most famous of these is Li & Fung.¹ Li & Fung initially started in the apparel industry by developing a network of Chinese manufacturers that could be marketed as sources for large apparel manufacturers in North America and Europe. The firm which has grown very big now offers a whole range of supply chain services beyond sourcing.

¹ F. Victor and J. Magretta, Fast, Global, and Entrepreneurial: Supply Chain Management, Hong Kong Style. *Harvard Business Review*, September-October, 1998, 102-114.

As a sourcing company, Hayden not only participated in the initial identification and negotiation of the arrangement between Woodward, ABS Logistics and Conghua Metals, but also continues to monitor quality, delivery, payment security and logistics.

Conghua Metals Company

A group of workers in a small Chinese town originally put up a manufacturing operation in a small shed just outside of town to make simple metal parts for larger companies nearby. The founders were quite aggressive. They continually sought out more business and developed other capabilities. After several years of growth and numerous additions to the original shed, the group established a formal business entity and named it Conghua Metals Company. By then, the firm already had the capability to make fairly complex metal components and parts. They also had sufficient capacity to produce large orders for both domestic Chinese and foreign customers, primarily other manufacturers.

In order to continue to grow, Conghua Metals had to go farther and farther from their immediate vicinity to attract workers. Today many of the workers come from rural, central China and are housed in dormitories owned by Conghua. This means that they are readily available to work overtime to meet heavy production demand.

The founders of Hayden had established a relationship with Conghua Metals while still working for their previous company. In their experience, Conghua Metals could be counted on to produce low cost parts of acceptable quality on a consistent basis. Thus, when ABS and Woodward contacted the firm regarding potential suppliers in China, Hayden proposed Conghua as an excellent candidate.

ABS Logistics Supply Chain Operations with Woodward Prior to the New Arrangement

The Woodward business traditionally had been predominantly an export account for ABS Logistics. ABS Logistics handled shipments from New Zealand to Australia. Import movements prior to the engagement with Conghua Metals in China all involved components originating in Australia, The United States and Europe.

Woodward's international freight spending with ABS was 65% export and 35% import. On a physical volume basis, the split was 85% export and 15% import. The disparity reflected the fact that export shipments were all short haul to Australia while import shipments were predominately from the Northern Hemisphere. The operational emphasis on the imports focused on meeting planned production deadlines so that finished product assembly could continue without interruption.

Export arrangements targeted short transit sailings to maintain service delivery levels in Australia with minimum inventories. While freight rates were monitored, operators involved in the account focused on supplier management, timely tracking information and physical delivery. Due to the strong market position of almost the entire Woodward range of product, continuity of finished product supply was deemed more important than planning to reduce shipping costs of components.

In order to meet these service requirements, ABS Logistics deployed a customer service representative to receive and collate Woodward orders from suppliers, and to ensure that suppliers meet the expected shipping dates. Any variance or supplier failure was communicated through a weekly status report which highlighted exceptions to the delivery schedules.

New Supply Chain Operations with Hayden and Conghua Metals

The new, prospective arrangements involving a Chinese contract manufacturer required significant effort from ABS Logistics and Woodward. Once Conghua Metals was selected as the supplier, Hayden arranged for Conghua to produce some prototypes of the components to be purchased by Woodward. After initial inspection in China by visiting Woodward personnel, the components were flown to New Zealand for approval by various New Zealand Standards Boards. There it was found that several of the underlying parts procured in China failed to meet New Zealand standards. Thus, Conghua would have to import these parts to China, a task which the company had no experience with. ABS Logistics, through its local China office, provided significant help to Conghua in the firm's efforts to obtain an import license.

Once regular production and shipping began, Conghua as the party that loaded and sealed the containers destined for Woodward was required to complete various bio-security packing declarations for Australia and New Zealand. Again ABS Logistics personnel taught several of Conghua's English-speaking employees how to correctly complete these forms.

One unanticipated outcome of the relationship was that Conghua gained sufficient capacity to produce in one week all the components required by Woodward for three months. As a result, Conghua took over the additional task of warehousing the production at its plant for a certain amount or cost that was unanticipated. This was done to maintain a smooth flow of products over time to Woodward. ABS continues to look for alternatives to this arrangement.

Overall, what had once been a relatively simple supply chain model has evolved into a complex series of activities and movements that requires a significant amount of remote coordination and control. ABS Logistics and Hayden International Sourcing serve as the facilitators that maintain this series of transactions between Woodward Laundry Products and Conghua Metals.

Corporate Social Responsibility in New Zealand

The New Zealand economy is heavily based on agricultural products. The primary exports are dairy products (powdered milk, butter and cheese), forest products (logs, lumber and pulp), meat products (beef and lamb) and fish (both wild and farm-raised). Major imports consist of apparel, machinery and equipment of all types.

CSR initiatives focus primarily on environmental issues: being "green", "sustainable" and non-nuclear. Other CSR efforts relate to energy consumption and "carbon footprints" or the amount of net carbon dioxide produced or consumed by a process. The entire country takes great pride in its reputation as an environmentally sound place in which to work and live.

New Zealand also has strict rules and regulations concerning working conditions, pay and safety for employees in domestic businesses. There is almost no hint of unfair and inhumane treatment

of workers in the economy. On the other hand, there appears to be much less recognition of how purchasing and outsourcing goods and services in other economies might contribute to labor and human rights abuses. Nor is there any strong drive to suggest that companies procuring goods and services from other economies should concern themselves with these issues.

Obviously, numerous companies in the economy, primarily retailers and distributors, purchase significant quantities of goods from Southeast Asian economies and China. Several companies that the author approached for this project indicated that they really had no particular policy on CSR issues related to labor, but probably should begin programs in this area. Thus there has been little public outcry pressuring New Zealand firms to institute strong CSR policies and procedures related to labor and human rights as there has been in North American and European economies.

Corporate Social Responsibility at ABS Logistics

When ABS Logistics was approached by Woodward Laundry Products to lead the effort in helping Woodward outsource some of its production, ABS did not have any explicit CSR policy. However, the firm did have a culture of treating its own workers fairly and rewarding good performance. Woodward was in essentially the same position.

With the advent of its new role, however, the CEO of ABS Logistics (who was an avid runner and user of Nike products) recalled the troubles Nike had when examples of human rights and labor abuses were exposed in the factories of some of the firms that made Nike products. Even though Nike and other firms, especially those in apparel and high technology, put in place strong standards of conduct for suppliers and procedures (audits) for ensuring compliance, there was evidence of many firms professing to meet the standards, but were in fact hiding on-going abuses.² The CEO recognized that ABS Logistics could potentially put its reputation in jeopardy if it became involved in similar cases.

ABS Logistics did have a code of conduct for its employees. This focused on honest and fair treatment of employees and business partners. For example, it prohibited accepting gifts from suppliers and giving gifts to customers. It goes without saying that bribes are illegal in New Zealand. It also called for non-discrimination on the basis of race, gender or sexual preference. However it made no mention of working conditions in the operations of suppliers or customers.

The CEO decided to formulate a specific CSR statement that would guide the company employees in their dealings with outside parties. Calling together a group of senior employees, he began a dialogue within the company on CSR. This culminated in the recommendation to hire a consultant to help, firstly to guide the development and publishing of a CSR policy, and secondly to educate the employees on the nature of CSR initiatives and the implementation of the ABS Logistics CSR policy.

This process took a period of several months, but in the end, all employees received at least three hours of orientation and instruction concerning the policy. Those employees with direct responsibility for customer or supplier relationships participated in another eight hours of discussion on the subject with the consultant, the CEO and the vice-president for Human Resources.

² "Secrets, Lies, and Sweatshops," *Business Week Online*, 27 November 2006.
Website: <http://www.businessweek.com/print/magazine/content/06-48/b4011001.htm?chaqn=gl>.

Given the strong support of senior management, all the employees of ABS Logistics recognized the importance of this initiative. The initiation and development of the relationships with Hayden and Conghua Metals offered a good opportunity to test the strength of this commitment.

Implementing CSR in the Woodward - ABS Logistics Supply Chain

In its relationship with Woodward, it was not sufficient for ABS Logistics to proceed with its CSR initiative independently. ABS had to convince Woodward to support and enhance this initiative if the entire supply chain were to be based on sound CSR principles. Woodward itself did not have a CSR policy regarding labor issues and human rights. The firm had just taken these matters for granted in its New Zealand and Australian operations.

ABS Logistics found itself working to educate Woodward on the same issues it had dealt with regarding CSR. ABS convinced Woodward to establish a sound policy by arguing that the risk of sullyng its good reputation was not worth using just any inexpensive Asian contract manufacturer. It would only be a matter of time before the public in New Zealand and Australia would adopt viewpoints regarding labor abuses similar to those in North America and Europe, especially because China's role in world manufacturing continued to increase.

ABS Logistics also argued that finding a sourcing company committed to CSR was critical to finding a qualified manufacturing partner. This created the search that culminated in the selection of Hayden International Sourcing. Hayden's clients included several North American manufacturers who had sensitized Hayden to CSR issues and standards. Hayden in turn, having numerous contacts and relationships with Chinese manufacturers, made it a point to focus on those firms that were apparently doing the best job of living up to the human rights and labor standards promulgated by organizations such as Fair Labor Standards in the United States.³ With these credentials, Hayden appeared to be a good partner for Woodward and ABS Logistics.

The next step was to find a qualified Chinese manufacturer who would agree to the CSR standards. It was Hayden who suggested Conghua Metals. Hayden was already using Conghua in association with a US manufacturer. Conghua had successfully passed an audit by that customer's representatives recently. Obviously Conghua also appeared capable of producing the components desired by Woodward. Hayden strongly supported a contract with Conghua.

But ABS Logistics was not convinced that all this was enough, and given the revelations cited in *Business Week*, ABS Logistics was probably justified in this skepticism. The firm pressed both Hayden and Conghua for a contract that expressly committed Conghua to comply with ABS Logistics standards of CSR and to allow periodic audits by independent compliance officers.

All parties signed the contract. Woodward, ABS Logistics and Hayden all agreed to exercise continued vigilance over the Conghua operations. Further, ABS persuaded Woodward to agree not to demand extreme price reductions that might tempt Conghua to cheat on the contract. Thus, the operations described above began. So far Conghua has been audited once and has successfully passed the audit.

³ Ibid.

Conclusion

This case describes the rather unique role of a supply chain intermediary, ABS Logistics, serving as a catalyst in the development of a supply chain compliant with good CSR practices regarding fair labor standards and human rights. The role is unique because it is usually the customer, Woodward in this case, that drives such initiatives, if any. This case shows that any member in a supply chain can be the party that sensitizes the entire chain to Corporate Social Responsibility issues.

The good practices illustrated here include having a written CSR policy, inculcating employees in the meaning and application of the policy, persuading both customers and suppliers to also comply with it, and putting in place methods to ensure continued compliance by all parties. But the most important characteristic of an effective CSR policy is the *will* of the firms involved to make sure that everyone lives up to it.

Corporate Social Responsibility in Peru FORZAs Minority Inclusion Program

Peru

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The case was developed with the cooperation of Asociación "FORZA Responsabilidad Social" (FORZA Social Responsibility Association) solely for educational purposes as a contribution to the Project entitled "New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -" conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

The case is based on a Peruvian company called FORZA S.A. which offers Corporate Security Services and its inclusion program for people with disabilities. This program which is focused on the thematic area of human development of people with disabilities, is one of several CSR activities undertaken by the FORZA Social Responsibility Association and consists of offering positions as operators in the Information and Control Center (CIC).

Because FORZA is a service company, its employees (or “collaborators”) are an important part of the supply chain since they are the suppliers of the services that FORZA offers its clients. Thus through its “Different Abilities” program FORZA applies CSR concepts in its supply chain by encouraging people with disabilities to become part of the company, and offering them the opportunity to develop themselves and to grow professionally.

From the legislative point of view there are norms for the inclusion of people with disabilities but in practice, there is widespread exclusion of these people from society as a whole because many have the misconception that people with disabilities are not capable of performing complex procedures. Therefore, society systematically excludes them from participating in organized economic activities. For that reason, FORZA’s project has had a very positive impact, since it not only conforms to the law and recognizes the rights and benefits of all its collaborators, but it also proactively offers positions to people with disabilities who have not previously had an opportunity to obtain employment.

Worldwide there are nearly 600 million people with some kind of disability, a situation which might have been expected to generate more interest and recognition than has been the case so far. The objective is to formulate and implement effective measures through legislative, administrative and executive measures that would allow the progressive participation of people with disabilities in organized economic, social and cultural activities. In developed economies which face slower labour force growth, such recognition is occurring and more executive labour market practices are now being implemented. Developing economies are also taking corresponding measures to develop a more inclusive society.

Peru has been experiencing significant advances in favor of people with disabilities. These are being reflected in affirmative actions aimed at achieving an absolute fulfillment of the right of “equality of opportunities”. Progress has required the commitment of all the social actors (public and private sector). According to a study of the National Institute of Rehabilitation and the Pan-American Organization of Health (INR-OPS) there are over 3.4 million people with disabilities in Peru, of which 27.7% are between 0 and 19 years, 24.7% are between 20 and 39 years, 19.1% are between 40 and 59 years, and 28.4% are more than 60 years old. Unfortunately 75% of people with disabilities do not work.

FORZA is aware of its role as a socially responsible company and is committed to provide equal opportunities for employment. In general, there is still a long way to go to achieve the vision of a truly inclusive society in Peru. But Peru will be nearer to achieving this vision once society begins to see people with disabilities as valuable resources and understand that tolerance of and respect for diversity are fundamental in helping people to achieve their potential as human beings.

Introduction

FORZA: "A Peruvian-owned firm innovating for the world."

FORZA S.A. is a private company offering Corporate Securities Services. A leader in its field, FORZA has as clients more than 50 major companies throughout the economy. It was created in March 1991 by a group of Peruvian businessmen who accepted the challenge to create a new company with an organizational philosophy focused on:

- Specialization in security issues
- Quality management
- Technology applied to its operations
- Staff of professionals, technicians and qualified agents

FORZA began its social responsibility activities on 04 October 2004 by creating a non-profit organization, known as The FORZA Social Responsibility Association, which:

1. Believes that every company has the duty to contribute to the development of its environment, in a permanent way.
2. Searches the security of the human development of poor and extremely poor boys and girls of the community (at the economy-wide level).
3. Aspires to be a company that produces wealth and well-being, and generates sustainable development in its operation.
4. Aspires to maintain its leadership through innovation--FORZA was the first corporate security company to implement a Social Responsibility Management System in Peru.
5. Considers that social responsibility is a strategic management tool that facilitates stakeholders' understanding.
6. Believes that any social responsibility activity has direct impact on the national social agenda.

FORZA is considered, by the PERU 2021 Association, as a socially responsible company. In March 2005 the company was awarded first place in the competition, "Prize to Social Responsibility and Sustainable Development" in the communities, medium-sized company category through its program, "Socially Responsible Children."

Profile of FORZA

*History*¹

FORZA S.A. was founded in 1991 by navy officers to provide high quality integrated corporate security services to firms in different economic sectors, which had seen their financial performance diminished not only because of the difficult economic climate, but also because of a social crisis caused by terrorism and common delinquency. In that climate, FORZA's business model quickly became the preferred choice because of the nature of its service, which was adapted to the needs of each customer.

¹ Website: http://www.forza.com.pe/InfoCorp_historia.htm

FORZAs’ organizational design which is based on experience and professional capacity, has allowed it to grow and consolidate within the Peruvian market, and to continue to foster the economy’s development. Its experience in providing both facility and patrimony security in urban and rural areas, has allowed it to specialize in serving the mining, industrial, energy and oil sectors. After 16 years of successful operations FORZA continues to develop and adapt its services to the needs of its customers.

Vision

“To maintain leadership as innovators and guides in the Corporate Security sector in the economy, giving services of the highest quality in order to increase the operational effectiveness of our customers, thereby contributing to their financial and commercial development and safeguarding their patrimony.”²

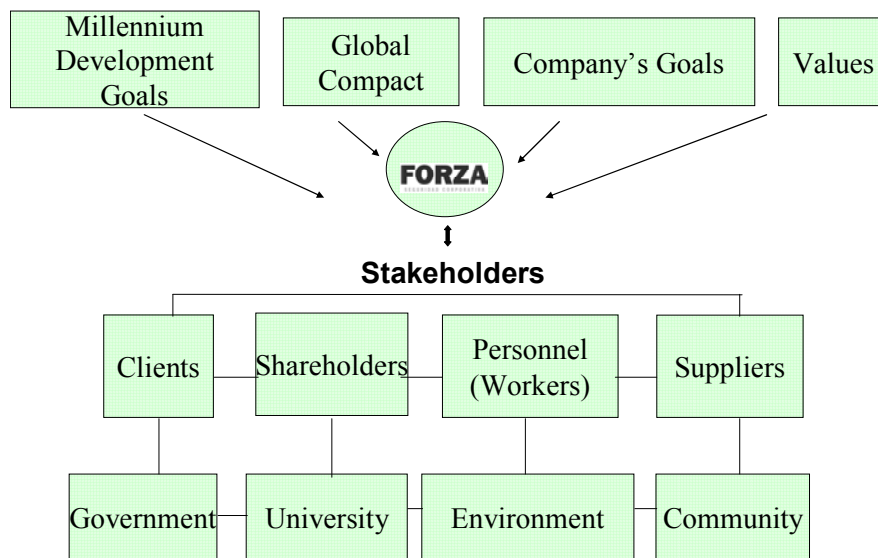
Mission

“To provide the best alternative in Corporate Security Services, meaning a system offering quality, technology and support for the protection of people and patrimony. The system allows the development of strategic plans adapted to the needs of each customer.”³

Corporate Principles and Values

All the activities and projects of FORZA aim to contribute to the accomplishment of the Millennium Development Goals and the Global Compact of the United Nations (**Figure 1**).

Figure 1:
Corporate Principles of FORZA



Source: FORZA

² Website: http://www.forza.com.pe/InfoCorp_mission.htm

³ Ibid.

Strategy

FORZA's approach to inculcate CSR in its work is based on the action lines of the Policy of Social Responsibility of the organization, which has the following elements:

- To respect and impel the cultural patterns (culture, tradition and values) of the communities and all the stakeholders of FORZA surroundings.
- To consider the population as stakeholders to make processes of consultation and communication based on its social, economic and institutional sustainable development.
- To integrate in a progressive way all the actions to accomplish local, regional and national objectives.

FORZA has proved its commitment by establishing an Integrated Management System Policy or IMS, encompassing the following objectives, goals and strategic programs of the organization:

- To increase the managerial and organizational participation in the IMS.
- To strengthen the good practices on social responsibility.
- To obtain better Security, Health and Environment practices.
- To improve client satisfaction.
- To evaluate performance and recognition.

Security Services

"Excellent security services in real time, 24 hours, 365 days a year, in the different regions of Peru."

FORZA protects the physical integrity of people and offers adequate solutions to security problems in every kind of business, with customized services according to the particular requirements of each customer.

People Protection

Personal Protection Services: Composed of qualified security officers who are highly experienced in offensive and defensive driving, the use of weapons, personal defense and first aid. The services offered are: Driver Security Officer, Personal Security Officer and Escort Security Service.

Commuting and Travel Planning Services: B'Safe Travel is a travel agency dedicated to punctuality and absolute confidentiality for any service required by the client. The Personal Protection Service forms an integral part of the services provided by the company.

Facility and Patrimony Protection

FORZA's Corporate Security has the technology, and qualified and skilled personnel to provide services in urban, industrial and rural zones. The types of services provided include:

Surveillance and Access Control: This is a customized service based on the risk assessment and analysis performed by its specialized personnel. The assessment results are delivered to the customer and also include recommendations for the type of security to contract, in order to minimize risks of intrusion and theft.

Electronic Security: The security system is designed using state-of-the-art electronic security equipment (CCTV, alarms and sensors) in combination with surveillance personnel to form an integrated security scheme.

Canine Surveillance: Trained dogs support open, extended facilities, intruder detection, and the detection of foreign objects that may be used against the firm's patrimony and personnel. This service stands out due to its minimal cost and adaptability to any climate or geographic zone.

Security Consultancy

FORZA develops and implements integral security surveys, plans, and projects, according to: Risk Assessments, Security Plans, Electronic Security Designs and Training Programs for Risk Prevention.

Electronic Security

Monitoring Alarm System: The Security System with state-of-the-art technology, allows more efficient protection at all levels, 24/7. Types of services provided include Internal Security Systems against hold-ups and robbery, Perimeter Security Systems, Closed Circuit Television (CCTV), Fire Fighting Systems, Access Control Systems and Alarm Non Access – Remote Monitoring System.

Clients

FORZA has a country-wide coverage that allows it to offer protection both in urban zones and in remote rural zones (See **Table 1**).

- Urban areas: malls, industrial plants, airports and residential zones.
- Remote areas: mining camps, oil camps, power stations, mining pipelines, gas pipelines, electric transmission systems and telecommunications.

Table 1:
Clients of FORZA

Airports	Banks
35-17 Cargo S.A.C.	Standard Bank London Limited
Lima Airport Partner	Banco Interamericano De Desarrollo
Communications	Banco Interamericano De Finanzas
Nextel del Perú	Others
América Movil Perú S.A.C.	Universidad Privada del Norte
Millicom Perú S.A.	Universidad de Lima
Telmex Perú S.A.	Cargill Américas S.A.
Americatel Perú S.A.	Knight Piesold Consultores S.A.
Construction Companies	Walsh Perú S.A.
HV S.A. Contratistas	Corporación Miyasato S.A.
Embassies	Consorcio Transmantaro
Embajada Británica	Iron Mountain
Factories	Antena 3 Perú
Industrial Papelera Atlas	British American Tobacco del Perú S.A.
Asa Textil Sourcing S.A.	Hewlett Packard Perú S.R.L.
Textil San Cristobal S.A.	Punto Visual S.A.
Hotels	Protisa Peru S.A.
Compañía Inversiones Monte Urbano S.A.	Forsac Peru S.A.
Hotelera Piura S.A.	Tecsur S.A.A.
Mining	Supermercados Peruanos S.A.

**Cont. Table 1:
Clients of FORZA**

Minera Yanacocha S.A.	Laboratorios Roe S.C.R.L.
Sociedad Nacional de Minería, Petróleo y Energía	Red Electrica Del Sur S.A.
Mineria Peru Copper Syndicate S.A.	MPG Comunicaciones E.I.R.L.
Oil Industry	Neuf S.A.
The Maple Gas Corporation	Impsat Peru S.A.
Refenería La Pampilla	Asociación Deportiva Los Inkas Golf Club
Grupo Repsol del Perú S.A.	Corporacion Texpop S.A.
PETROPERU S.A. (Oleoducto Piura)	B & W Master Service S.R.L.
Power Industry	Centro Orientación Familiar
Duke Energy International Egenor S.A.	Aeroinversiones Del Peru S.A.C.
Wholesaler	Nutra S.A.
Coca Cola Servicio del Perú S.A.	DHL International S.A.C.
Corporación Inca Kola S.A.	Cordillera De Las Minas S.A.
AGA S.A.	Overseas Bechtel Incorp Suc. Del Perú

Source: FORZA

FORZA's Corporate Social Responsibility

FORZA is committed to the development of the Peruvian economy and is aware of its role as a corporate citizen. It started its Corporate Social Responsibility (CSR) activities in October 2004 through the *FORZA Social Responsibility Association*, a non-profit organization guided by the Integrated Management System Policy–IMS.⁴ The organization has the following Vision and Mission:

Vision

“We will be a recognized institution in promoting the role of CSR, oriented to acquire the sustainable human development of its workers and the surrounding communities.”

Mission

“To contribute to and promote the execution of social development actions and projects for children, their families, our workers, and the community, operating with creativity, innovation, solidarity and environmental awareness.”⁵

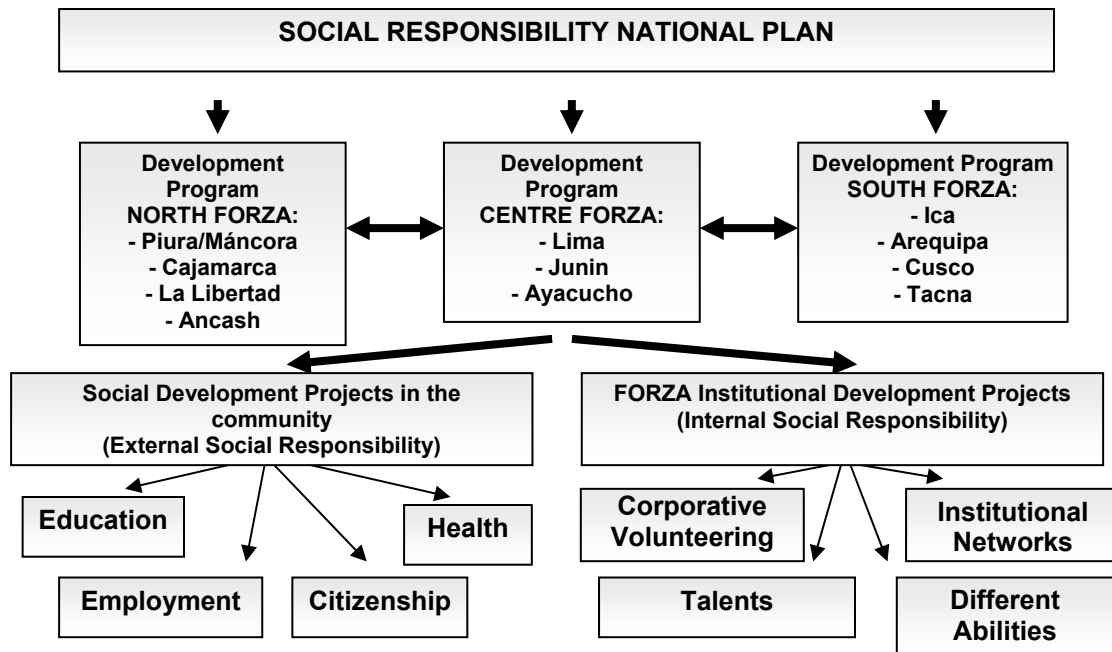
FORZA's Social Responsibility Plan for Peru

The plan covers the northern, central and southern regions of Peru where the company has its operations and implements sustainable development projects with the objective of enhancing the development of children, their families, workers and the community (**Figure 2**).

⁴ See Appendix 1: FORZA Social Responsibility Association

⁵ Website: http://www.forza.com.pe/InfoCorp_respsoc.htm

Figure 2:
Social Responsibility National Plan



Source: FORZA

Integrated Management System Policy - IMS

Customer satisfaction, employees’ health and physical well-being, environment conservation and internal security are the determining factors that have allowed FORZA to maintain its leadership in providing corporate security services. To achieve this, FORZA is committed to:

- Comply with customer requirements and the current regulations applicable to the company.
- Have trained personnel, encouraging their development and participation in the company.
- Set up the measures needed to guarantee the quality of the service, and to prevent security, health, environment and internal protection risks through the implementation of a program of social responsibility for the benefit of the clients, collaborators and community as a whole.
- Possess and maintain a constant system of improvement in service, processes and procedures incorporated in the IMS.

Quality, Environment, Safety, Health and Internal Protection BASC⁶

FORZA works within a highly competitive and demanding environment where its main stakeholders including clients, work force, shareholders and society all have needs that must be fulfilled. To address these needs, FORZA uses management tools applied at the world-wide level including certification in different systems:

Quality Management	ISO 9001:2000
Environmental Management	ISO 14001:2004
Occupational Health and Safety Management	OHSAS 18001:1999
Internal Protection Management	BASC

⁶ Business Anti-Smuggling Coalition is a cooperation program between the private sector and domestic and foreign organizations, created to encourage a safe international trade. It seeks to apply preventive measures intended to prevent smuggling of goods, narcotics and terrorism in legitimate trade. **BASC** is a certification that allows the companies to expand their markets, consolidating their image at domestic and international levels.

FORZA’s “Different Abilities” Project

FORZA is well aware of its role as a socially-responsible company, and has developed the Different Abilities project. This project aims to contribute to the development of a more inclusive culture that provides better social, cultural, economical and educational opportunities to people with physical disability.⁷

The Different Abilities project has been planned for a duration of two years, at which time FORZA aims to have achieved the following objectives:

- To help people with disabilities fulfill their personal development through their social, economic and cultural integration within an equal opportunities framework, that guarantees the exercise of their rights.
- To consolidate and to institutionalize management models with the participation of private companies, people with disabilities and civil society to achieve sustained process throughout Peru and to enable their inclusion of persons with disabilities as role model citizens.

The project focuses on human development as the term is used by the United Nations Development Program (UNDP) and includes two distinct parts: an internal aspect targeting FORZA employees with disabilities and different abilities (who are the direct beneficiaries); and an external aspect focused on children with disabilities from the community of Mancora - Piura⁸ (who are the indirect beneficiaries) (See **Table 2**). The project is executed at the economy-wide level.

Table 2:
Beneficiaries of the “Different Abilities” Project

Beneficiaries	Direct Beneficiaries	People with disabilities (children, teenagers and adults)	
	FORZA collaborators		2 collaborators – Lima
			1 collaborator – Trujillo
			1 collaborator – Arequipa
			* FORZA estimate to have 10 people at National level in the next two years.
	Children from Mancora	50 children	
Indirect Beneficiaries	Families of people with disabilities		
Mothers of the children from Mancora	50 women for the workshops		

Source: FORZA

In April of this year, FORZA S.A. and the Sub-commission of People with Disabilities of the Peruvian Congress began a campaign called “Together for the Sustainable Development of People with Different Abilities”, proposed by Congressman Michael Urtecho.⁹ The purpose of this campaign is to encourage the private sector to consider the participation of people with disabilities in the labor market and to improve their quality of life by fostering an inclusive culture based on

⁷ According to Peruvian Law number 27050, a person with a disability is an individual who has one or more deficiencies demonstrated with the significant loss of some of its physical functions, mental or sensorial, that imply the diminution or absence of the capacity to make a considered activity within normal forms or margins, limiting the person in the performance of a role, function or exercise of activities and opportunities to participate equitably within society.

⁸ Mancora is a beach located on the north limit of the Department of Piura, north coast of Peru on kilometer 1165 of the Panamerican North Highway.

⁹ Michael Urtecho is a Peruvian politician and congressman who has a birth disability. He won the third place in a World Bank Contest for which he received a grant and created “The daily bread from a disability brother” bakery that brings work to people with disability. In June 2004, he won the same contest with another project and is now giving training to people with disability.

an equal opportunities framework.¹⁰ With this campaign, FORZA Social Responsibility Association began to implement the activities related with its Different Abilities Project:

1. Offered positions as operators of FORZA Information and Control Center–CIC. Currently there are four people with some kind of disability working in the Center: two in Lima, one in Trujillo and one in Arequipa.



Gina Muñiz, Responsible for the FORZA Social Responsibility Association with two collaborators with disability.



The next step is to replicate these activities in other cities where FORZA operates (Piura, Cajamarca, Ancash, Junín, Ica, Ayacucho, Cusco and Tacna). FORZA estimates that by 2008 it will have 10 collaborators with some kind of disability.

The selection process for recruiting persons with disabilities is similar to that used for recruiting all administrative personnel, although the process puts more emphasis on the personal abilities of the candidates, especially the capacity to adapt themselves and their commitment to learning. In evaluating resumes, FORZA puts more emphasis on acquired experience because the organization understands that there are few employers who currently provide professional opportunities to people with disabilities. During the technical and psychological evaluation, FORZA determines if the disability is likely to adversely influence the expected performance of the functions of the position. If that is the case and the candidate fulfills the psychological abilities, he or she is maintained in the candidate data base until a new position becomes available. Otherwise the candidate continues with the evaluation process.

2. Donated 11 wheelchairs and 20 pairs of crutches, which were received directly by the beneficiaries.
3. Gave recognition to Carlos Benavente, an operator with disability, for the important goals that he accomplished in Peruvian and international sports events such as marathon and basketball in wheelchair.



Mercedes Cabanillas, President of Peruvian Congress; is giving a trophy to Carlos Benavente.

¹⁰ See Appendix 2: Ceremony at the Congress.

- Started the operations of the educational center for special children called “Divino Niño Jesús” en Máncora, Piura



Collaborators, children and their mothers at the educational centre “Divino Niño Jesús” for special children

FORZA participates actively in this center through its six social responsibility projects: Health, Education, Citizenship, Employment, Volunteering and Institutional Network.

This educational center receives children of all ages with some kind of disability (visual, auditive, motor and mental disabilities) and provides them education for their personal development. In addition, the center offers practical knowledge and skills training to children and their mothers, teenagers and adults in the community. These comprise workshops on subjects such as weaving, Peruvian box drum, psychoprophylaxis for pregnant women, and hydrotherapy for new mothers and babies, among others.



Workshop of Hydrotherapy for mothers and their children



Children at the Peruvian Box Drum Workshop

The results that FORZA expects to achieve with this project are:

- Increased economic and social integration for people with disabilities through their effective placement within the organization, and their professional development both for their own benefit and for the enhanced productivity of the company.
- Their inclusion in society as role model citizens on a sustained basis.
- Fostering the development of values in the children with disabilities to promote their social integration.

Other FORZA CSR Projects

FORZA divides its CSR projects into two kinds, external (Social Development Projects in the Community) and internal (Institutional Development Projects).

Examples of Social Development Projects in the Community

1. Education Project: “Drops with Responsibility...”

This project targets children in poverty. Its purpose is to improve human development by means of education, to achieve an adequate level of knowledge through extracurricular activities, and to develop and encourage social abilities, creativity, values, discipline and coordination.

- “Useful Saturdays”: Workshops of Emotional Guidance for Children, Music and Dance, Painting Contest, Theatre, Birthdays, Mothers Day, Independence Day, Christmas, among others.
- Library

2. Health Project: “Improving my Childhood”

The project targets community members in extreme poverty and aims to promote sustained and improved human development, leading to the achievement of long and healthy lives by means of medical attention provided by FORZA personnel through agreements with laboratories and clinics. It also provides education on preventive medicine and healthy breakfasts for children.

- Daily breakfasts with lessons on cleaning habits and good manners
- Medical attention: FORZA doctor and Human Resources Agreements with laboratories and clinics
- Conferences: Nutrition and Parents School
- Health campaigns in FORZA
- *Wawa Wasi* National Program¹¹ (Ministry of Woman and Social Development, and Fondo de las Americas del Peru - FONDAM)

¹¹ *Wawa Wasi* in Quechua means “House of the girls and boys.” It is the only social program of the Peruvian Government that offers integral attention to early infancy, responding to the necessity of the day care for under four-year-old girls and boys, particularly for those who are in risks and in poverty or extreme poverty situation.

3. Citizenship Project: “I am Peruvian too”

This project has considered community children in extreme poverty as the target population. Its purpose is to permanently improve human development through the improvement of the persons’ legal status as citizens and their active participation in society, by means of their identification and participation in the activities promoted by the community and the Peruvian state.

- My Identity: Birth Certificates and IDs
- Dining room and sport field: construction of community assets implemented in partnership with the Municipality of Surco and the Ministry of House and Construction

4. Employment Project: “Creating Well-Being”

This project targets mothers living in poverty with the purpose of permanently enhancing human development through improved skills and abilities and achieving a decent standard of living through training programs in traditional workshops and establishment of small and medium-sized businesses.

- Quality of life: home crafts workshops (woven, imitation jewelry, embroidery, among others)
- Small and Medium-Size Enterprises (SMEs): formalized SMEs to generate incomes for the families and provided technical training to improve their productivity.

Institutional Development Projects

1. Corporative Volunteering: The personnel of FORZA are committed to the CSR projects and participate in the activities programmed by the company. They also sponsored the projects through monthly contributions and payroll discounts.
2. Talents: One of the CSR projects of FORZA is the support for the innate abilities of employees, their children and the community in areas such as arts, culture and sports.
3. Institutional Networks: FORZA is aware of the importance of belonging to different institutional networks that support the development of the company’s projects. For that reason, there are different ministries and public and private institutions that work with FORZA and support its initiatives. These are the following:

- Ministry of Health: participation in the “Peru, Stop the Tuberculosis” Committee.
- Ministry of Woman and Social Development: Wawa Wasi National Program.
- Ministry of Work: inscription of the mothers on the PROFECE initiative¹².
- Municipality of Surco: several programs
- RENIEC¹³ San Borja: Birth Certificates and IDs.
- Institutions: PERU 2021, Toulouse Lautrec.

¹² The Feminine Program of the Employment Consolidation (PROFECE), a program adscript to the Micro and Small-sized Enterprise National Direction of the Ministry of Work was created in October 1996 and it is oriented to promote market opportunities and consolidate people abilities. PROFECE is the first Official Initiative that aims to solve the problem of income generations of the female population.

¹³ National Register of Identification and Civil State (RENIEC).

Conclusions

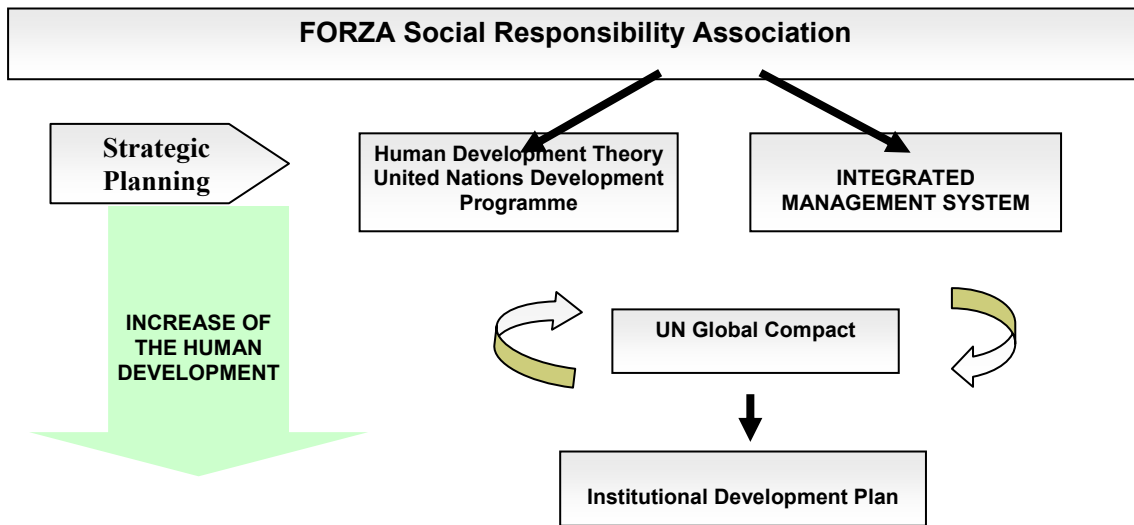
FORZA's CSR programs are viewed as important and having had a positive impact on the results of the company, in the development of the economy and in the satisfaction of the stakeholders' interests.

FORZA's "Different Abilities" Program has proposed a process whereby people with disabilities, typically people who were not previously considered for a position in the formal sector, would become involved in the labor market. People with disabilities are not useless; they can easily do jobs and activities according to their own abilities. For example, a person confined to a wheelchair can do desk jobs effectively, or in FORZA, he could work as an operator in the Information and Control Center, which is an important part of the services that the company offers.

The program aims to increase the degree of economic and social integration of people with any kind of disability, placing them in an appropriate way within the organization, improving their professional development and giving them an opportunity to contribute to the productivity of the company.

To make the broader society aware of and sensitive to the abilities that persons with disabilities can offer is a challenge that FORZA has considered since its project began. FORZA has chosen to champion placement of people with disabilities within the company to demonstrate that such individuals can successfully participate in the labour market within the formal sector of the economy. FORZA understands the importance of the active participation of the private sector in CSR initiatives. The role of government is to create an environment that encourages this progressive behavior including the provision of incentives for companies to include people with disabilities in their businesses.

**Appendix 1
FORZA Social Responsibility Association**



Source: FORZA

**Appendix 2
Ceremony at the Congress**



Wilson Gómez-Barrios R., Congressman Michael Urtecho, Mercedes Cabanillas President of Peruvian Congress, Vice President Luisa María Cuculiza, Congresswoman Alda Lazo and Congressman Luis Galarreta



Wilson Gómez-Barrios R., Congressman Michael Urtecho, Mercedes Cabanillas President of Peruvian Congress, Vice President Luisa María Cuculiza and Congresswoman Alda Lazo.



Wilson Gómez-Barrios R. signing the Commitment Act



Congressman Luís Galarreta, Wilson Gómez-Barrios Rincón (Executive President of FORZA), Congresswoman Alda Lazo and Vice President Luisa María Cuculiza.

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AMANCO DEL PERÚ S.A.

CASE: “Amanco for a better Peru”

Peru

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The case was developed with the cooperation of Amanco del Perú solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective -” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author and the Asia Pacific Economic Cooperation.

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Executive Summary

Corporate Social Responsibility (CSR) is an approach to management that incorporates the organization's relationship with the community, its collaborators and the environment. It is based on a set of unique values and principles that are incorporated in the strategic plan of the organization, generally in its mission and vision. In this sense CSR becomes part of the organization's soul, because it represents its will to share benefits and profits with its stakeholders. CSR is driven by conviction to change society for the better and contribute to its long-term development.

CSR is not only about conviction, however. Increasingly, it is recognized not as a fad but as a necessary condition for organizations to remain competitive in the global marketplace. Customers search out brands associated with environmental stewardship and having responsible relationships with the communities in which they operate and with society as a whole. For this reason, many organizations have recognized the importance of integrating CSR into their corporate strategies. This is the case of Amanco, the subject of this case.

Amanco is the Latin American leader in the tube systems business and also in *construsistemas* (construction systems) in Central America, despite difficult economic conditions in almost all the regional markets that it serves. Amanco is recognized as one of the leading organizations worldwide to have introduced CSR throughout its operations.

The success that Amanco has achieved has been heavily influenced by the socially-responsible actions that the company has taken, which have allowed it to refine the management of its costs, assure the quality of its executive team and promote the enthusiasm and passion of its employees to achieve sustainable development. One of the principal innovative tools that Amanco has employed is the Sustainability Scorecard, which has helped the organization to structure its activities along five dimensions: financial, clients, process and technology, social and environmental, and human resources. This framework has facilitated the achievement of "triple results" encompassing positive social and environmental outcomes as well as high economic valued-added.

The program "*Amanco por un Perú Mejor*" (Amanco for a better Peru) was initiated in 2004 with the objective of enlisting all of the organization's collaborators as its *embajadores* (ambassadors) for CSR in Peru, to disseminate the key concepts to communities through the interactions of interested and committed people. This program encompasses three pillars, Progress, Health and Attitude, and each of them has been developed through strategic alliances with civil society and key government organizations.

Amanco Group

The Company

Amanco del Perú is one of the most important companies in the construction sector in Peru. It forms part of the Amanco Group, which, in turn belongs to *Grupo Nueva* (New Group), an international holding company that operates in 15 American economies with sales of over US\$ 1.240 million and employment for 16,000 people in its operating businesses, the forest products and construction equipment sectors.¹ As a result of this connection the Amanco Group debt is rated as investment grade.

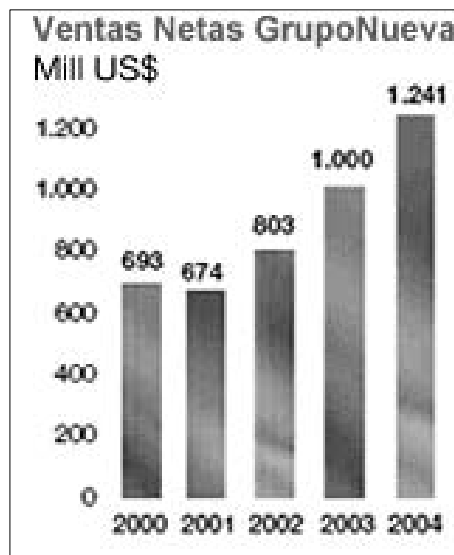
¹ The 2004 consolidated net sales of *Grupo Nueva* reached US\$1241 million, growing by 24% compared to 2003.

The Amanco Group headquarters is situated in San José, Costa Rica; it does not have a separate board and is accountable to the executive president of *Grupo Nueva*, who concurrently is the executive president of the group board, comprising external directors. Amanco shares the same vision, values, corporate principles, policies and programs with the Masisa Group for the management of its financial, environmental and social resources.

The Amanco Group is a leading supplier of lead tube systems in Latin America with over 50 years of experience in the region. It has 6,200 employees which it refers to as “collaborators” and 23 industrial plants, producing 29 products for sale across Latin America and the Caribbean.

A business unit headquartered in Sao Paulo, Brazil is dedicated to the production and commercialization of tube systems, *construsistemas* (construction systems) and *geosistemas* (geosystems). This company has operated in Brazil since 1997 with sales in 2004 of US\$1.2 billion (**Figure 1**).

Figure 1:
Total sales of Grupo Nueva: 2001-2004



Source: Annual Memory of Grupo Nueva

Amanco operates the following core businesses:

- **Tube Systems:** Pipes, connections and accessories to lead water, sewage system, irrigation, electric conduction and optical fiber, focus on the around segments, infrastructure and irrigation. Amanco has a market presence in 13 economies of Latin America.
- **Construsistemas (Construction systems):** Cement Products, wood commercialization, gypsum and steel for light construction. Amanco has a strong presence in Central America.
- **Geosistemas (Geosystems):** Integral engineering synthetic solutions for civil construction. Amanco has strong presence in Central America, Panama and Colombia.

Vision, Mission, Values and Social Responsibility

The company's vision is "to be recognized as an organization that creates economic value by operating based on a framework incorporating ethics, efficiency and social responsibility, in a way that contributes to enhancing the life quality or life standards of people."²

Its mission is to "produce and commercialize tube systems or integral solutions for the transport of fluids as well as *geosistemas*, operating in construction markets, agricultural and mining infrastructure."³

The company promotes the following values:

- No discrimination
- No child labor
- Liberty of association
- Compensation
- Social security
- Labor stability
- Internal communication
- Social responsibility projects

For the Amanco Group, CSR is defined as: "being corporate citizens who interact in a responsible way with the community, contributing to its development and valuing the professional and human growth of the collaborators and the social economic environment of their businesses, while working for increased efficiency and assuring the long-term sustainability of their company for the benefit of all the stakeholders, through the correct and systematic management by objectives and measurable results."⁴

Structure and Enterprise Strategy

Amanco represents a company that has integrated CSR throughout its organization. This is apparent in its organizational structure and enterprise strategy, which are directed towards the achievement of triple results incorporating economic, social and environmental values. In Peru, Amanco is the only company that has developed an integrated management model based on social responsibility, which demonstrates the leadership and commitment of the organization to CSR.

In 2003, there were major changes within Amanco and the top management was consolidated into a single position. This was done to generate a clear strategic vision for the company and integrate the management of its operations.⁵ Amanco operates with an executive president who coordinates directly with regional managers in areas or markets where the company is present.

With this structure (See **Appendix 1**), *Grupo Nueva* delegates responsibility for social and environmental outcomes to business units in the regions where it operates, based on the philosophy adopted by its top management. The group places heavy emphasis on the alignment of key managers to the achievement of corporate goals.

² Information provided by *Amanco del Perú*.

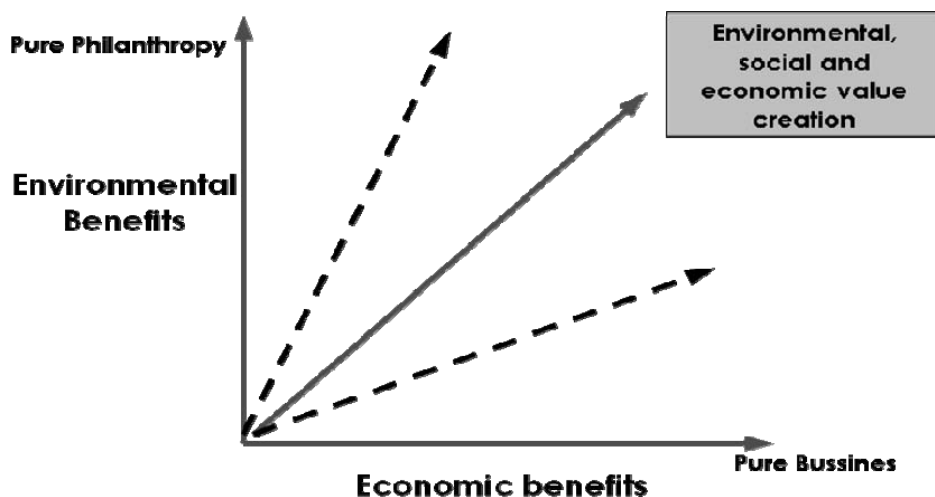
³ Ibid.

⁴ Website: <http://www.amanco.com>.

⁵ See Sustainability Report of 2002-2003. Website: <http://www.amanco.com>.

Amanco's strategy is to conform to sustainable development principles because it wants to integrate the generation of economic, social and environmental value into its enterprise management (See **Figure 2**).⁶ Amanco believes that this strategy has allowed the company to achieve success on a sustained basis in a highly competitive global market.

Figure 2:
Enterprise strategy of Social Responsibility



In 2003, Amanco issued an Enterprise Principles Declaration, with the specific objective of transforming the company's mission and vision into practical directions for its collaborators daily work.⁷

Every two years, Amanco publishes a Sustainability Report based on the Global Reporting Initiative guidelines, thus presenting its social, economic and environmental development in a transparent way to its stakeholders. In March 2003, the Executive President of *Grupo Nueva*, Julio Moura, publicly stated the group's commitment to the Global Compact principles. *Grupo Nueva* and all of its affiliate companies are committed to fulfill all the directions contained in Kofi Annan's 1999 initiative.⁸

The Triple Result and the Sustainability Scorecard⁹

Amanco's focus on a triple result is the strategy through which the company intends to create economic, social and environmental value.¹⁰ This strategy is reflected in the Sustainability Scorecard¹¹ which allows the balance between all the objectives.

⁶ Information provided by Jimena García Vela, responsible for the Social Responsibility and Communications Area of Amanco del Perú.

⁷ See Sustainability Report of 2002-2003. Website: <http://www.amanco.com>.

⁸ United Nations- Global Compact. Website: <http://www.unglobalcompact.org>.

⁹ See Appendix 2.

¹⁰ Website: <http://www.amanco.com>.

¹¹ Instrument adapted by Amanco after Balanced Scorecard of Kaplan and Norton, to reach the economic, social and environmental value.

This Scorecard represents an important tool for the evaluation and control of social and environmental development. This model is based on the Balanced Scorecard created by Robert Kaplan and David Norton, recognized experts in enterprise management. Amanco has chosen to monitor progress using a recognized tool of modern management, in order to demonstrate that CSR initiatives support the creation of value in businesses in a more sustainable way, and to have an impact in the generation of more benefits through higher incomes, lower risks, and enhanced productivity, innovation and brand image.¹²

To achieve the triple result, Amanco articulates five fundamental dimensions for the development of the company's operations and the measurement of its progress. These are:

- Finances
- Clients
- Technology and processes
- Social and environmental
- Human resources

The human resources, social and environmental management and process and technology dimensions are the operational components. Each is associated with strategic goals that disaggregate into important initiatives and vital actions assigned to the whole organization, with the purpose of achieving a defined strategic course.

The activities initiated in these three dimensions have a direct effect on the clients' dimension, which in turn, influences financial performance and consequently the achievement of the triple result.

Financial Dimension

In terms of outcomes achieved, the company has achieved reasonable income growth considering the market conditions in which it has operated, and specifically the crisis conditions in many Latin American economies.

The specific objectives of this dimension are:¹³

- Guarantee the financing of the business strategy by reducing costs and risks.
- Increase the incomes in a sustainable and profitable way.
- Reduce operational costs.

In terms of business strategy, long term financial success depends on how the business achieves its commitments to sustainable development and CSR. The activities developed by Amanco to attain this anticipate the creation of economic value and the improvement of living standards.

Client Dimension

Amanco is convinced that its consumers prefer the products and services of companies that consistently offer excellent service and quality, are recognized as worthy of consumer confidence and behave as exemplary corporate citizens. This is why Amanco has introduced this variable into its strategy, focusing on continually offering its clients better products and services.

¹² See Sustainability Report of 2002-2003. Website: <http://www.amanco.com>.

¹³ See Sustainability Report of 2002-2003. Website: <http://www.amanco.com>.

Amanco is aware that one of the most important challenges facing organizations is the need to anticipate and satisfy clients' changing needs. To achieve this, the company must be able to adjust quickly to change, which in turn requires on-going commitment of all of its collaborators.

The specific objectives of this dimension are:

1. Reinforce Amanco's brand.
2. Innovate with products that brings big margin.
3. Satisfy clients.

Processes and Technology's Dimension

The main goal is to improve efficiency and the best way to achieve this is through innovative products, complete solutions and an excellent service, a trustful environment and high world quality standards. Amanco is continually working to improve its products' efficiency.¹⁴ To achieve this, the company has adopted a *Process for the Creation of Products (PCP)* which guarantees a more effective way of introducing new products or improving old products that results in client satisfaction and generates low environmental impact.¹⁵

Within this dimension, the company also monitors processes that assure the improvement of the productivity of its sales force, including Customer Relationship Management (CRM) and E-Business projects. It also tracks the complexity of handling demand, communication and shopping generation, among others.¹⁶

The specific objectives of this dimension are:¹⁷

- Optimize the local and corporate financial planning.
- Improve the fixed assets management and reduce the working capital.
- Ensure effective communication with high priority groups.
- Optimize investigation processes and the introduction of new products.
- Manage risk.
- Improve service process and relationship with clients.
- Improve supply processes.
- Optimize plant capacities.

Social and Environmental Dimension

The principal objective of the social and environmental dimension is to provide responsible management of people and the environment. The specific objectives of this dimension are:

- Fulfill the requirements of international quality, health, security and environmental standards.
- Manage the social impact's system.
- Minimize the environmental impact by improving the eco-efficiency indicators.

¹⁴ Amanco's clients value the innovative products. In 2002 some 10.9% of the total sales came from these new products and in 2003 the percentage was 12.3%.

¹⁵ During 2004, the sales of the innovative products accounted for 22.1% of the total sales.

¹⁶ Website: <http://www.amanco.com>.

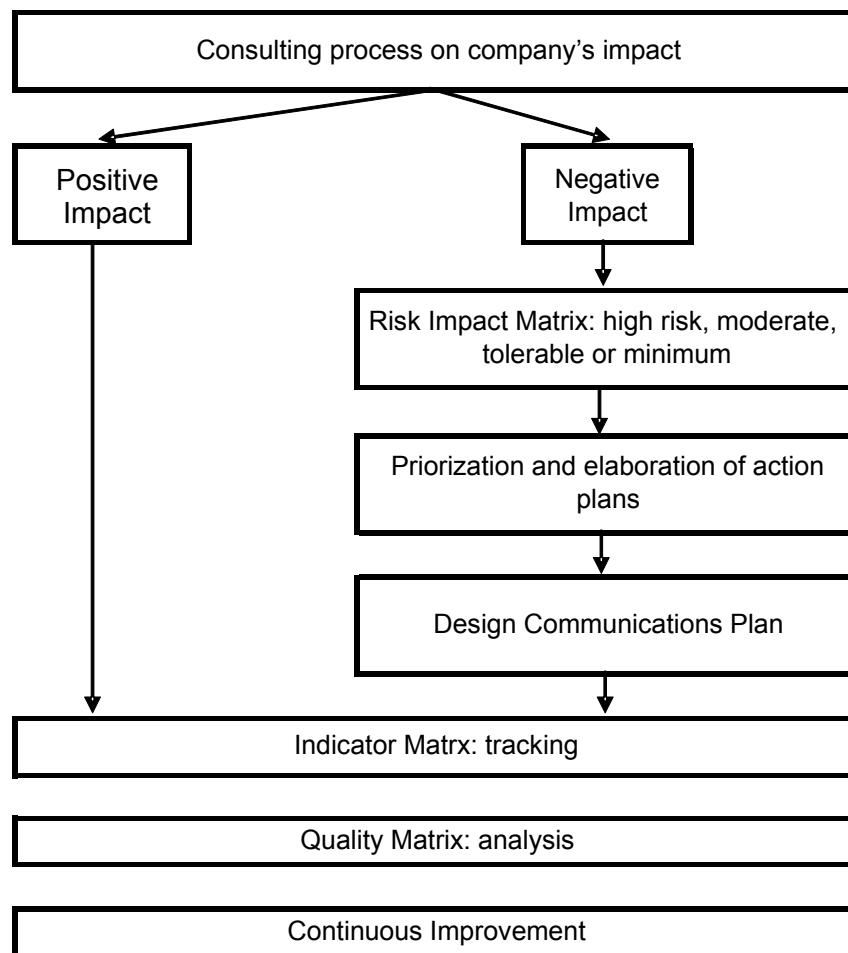
¹⁷ See Sustainability Report of 2002-2003. Website: <http://www.amanco.com>.

To improve Amanco’s relationship with its stakeholders, the company has designed a communication and consultation guide to support dialogue with key stakeholders. Through surveys, dialogues, and face-to-face communication and consultation with key interest groups, Amanco has monitored both positive and negative impacts of the company’s operations.

When potential negative impacts are identified, a risk matrix is created to measure the probability level of occurrence and the risk level. The result is a classification of potential levels of risk as **high moderate, tolerable** or **minimum**. Based on this analysis, the follow-up actions are prioritized and documented in an action matrix.

A communication plan is developed, articulating priority subjects, key messages and target stakeholders. Finally a set of indicators is developed to measure progress. A quality matrix identifies procedures that generate negative feedback, the company’s response and continual improvement processes (**Figure 3**).

Figure 3:
Dialogue and Communication Process with Stakeholders



Source: Amanco of Peru, Elaborated by author.

In 2004, the company conducted a series of consultations every three months with clients and suppliers and once a year with the community. It also conducted regular consultation sessions with their collaborators within the company (**Table 1**).

Table 1:
Amanco Del Peru's Consultation Methodology (Results of Year 2004)

Stakeholder	Frequency	Actual	Estimated	Difference
Clients	Quarterly	524	457	15%
Suppliers	Quarterly	149	90	66%
Community	Annual	64	60	7%
TOTAL		737	607	21%

Source: Amanco del Perú S.A.
Elaboration: Amanco del Perú S.A.

Likewise, Amanco has developed other community projects, such as one called “Perception of Value,” which tracks the community’s perceived value of the programs developed as a result of the consultation process. Amanco has also developed a “Social Responsibility Index” which measures how stakeholders perceive the level of the company’s commitment to contribute to societal goals and to environmental stewardship.

The 2004 consultation sessions show that 64% of Amanco’s neighbors surveyed were satisfied with the impact that Amanco had in their community and with their employment with the company. In terms of the social responsibility index, 73% of Amanco’s clients showed a positive attitude towards the company.

Environmental Management

Recognizing the importance of responsible care for the environment, the company has undertaken the following activities:

- ISO 14001 certification in all of their operations (2003)
- ISO 9000 certification in all of their operations (2003)
- Use of new stabilizers of Can in 20% of the manufactured products (2002)
- Elimination of pigments that have heavy materials (2002)
- Increase in savings amounting to US\$1.3 million as a result of the eco-efficiency
- Certification under the OHSAS 18001 regulations in all their operations, except for the Brazil’s northeast plant

Human Resource Dimension

The main objective of the human resource dimension is to build a unique and identifiable Amanco culture based on its business strategy. To achieve this, the company has the following specific objectives:

- Develop strategic competences of their collaborators.
- Create a culture that promotes the company’s values.
- Assure disciplined communication, alignment and execution of the strategy.

For the company, this alignment is very important in generating the responsiveness necessary to achieve their strategic objectives. Hence, the Hcreation of a culture of mutual respect for all collaborators is critical in order to:

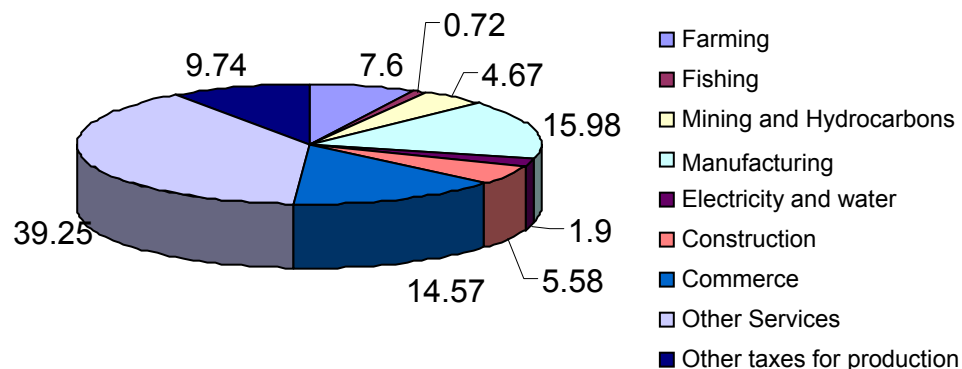
- a. respect the individualism and integrity of each other,
- b. promote the group working,
- c. develop a working environment that promotes the maximum synergy among all the collaborators, and

- d. offer opportunities for professional development and qualification, and motivational programs for the improvement of skills of collaborators.

Developments in the Construction Materials Sector

The construction industry has played an important role in Peru's overall economic recovery in recent years while the activity in the sector is sensitive to overall aggregate demand. As shown in **Figure 4**, construction accounted for 5.58% of GDP in 2003. Its buoyancy in recent years has supported Amanco's strong sales growth.

Figure 4:
2005 GDP by Economic Activity (Percentage Structure)



Source: National Institute of Statistics and Computer Sciences.
Elaborated by author.

During the first trimester of 2005, the construction sector continued to expand for the fifth consecutive year due to the increase in residential construction. This was supported by projects such as “*Mi vivienda*” (My Own House) and “*Techo Propio*” (My Own Ceiling) as well as with investments in the public sector, strong commercial investments in the financial centers in Lima, and robust road construction (See **Appendix 3**).

Opportunities and Risks

As a leader in tube systems, Amanco has been able to take advantage of market opportunities arising from strong construction demand in Peru, including the following:

- Interest of Besalco's contractors to participate in Peruvian road construction concessions.
- *Mivivienda's* (program that gives credit to people who cannot afford their own house) credits had doubled up and construction is expected to follow the same trend.
- Construction of three power centers that link two important companies, Totus and Sodimac.
- Investments in hotel construction by the Spanish Marsan's Group.
- Government investments in the scholar infrastructure.
- Japan's loan allotted for the improvement of irrigation channels.

Supply Chain Considerations

Amanco operates in a sector where service quality standards vary considerably. Many suppliers cannot guarantee even minimum quality standards of the products they offer. Amanco has been able to capitalize on its ability to guarantee the quality of its products and services which is supported by its responsible behaviour.

Amanco has also focused on developing the capacities of its clients (i.e. hardware dealers) through different qualifications programs organized by their own personnel. In this way, Amanco can strengthen their capacity to provide guarantee to the end users by helping them to maximize (through the distribution channel) the benefits of their products.

Social Responsibility Programs

Amanco has developed a number of programs aligned with the results of the periodic consultation sessions that they made with their stakeholders.

“Collaborators” (Employees):

Amanco works to strengthen health and security standards based on ISO 18001. The Dupont Program is intended to sensitize employees on security matters. The Ambassadors Program developed by the company encourages its collaborators to share the company’s CSR philosophy with all the interested members of the Peruvian public. An internal recycling program encourages the recycling, through specialized companies, of waste generated in the production plant and in the management area.

Amanco has developed a methodology using internal consultants to disseminate information about the company’s performance and employee perceptions in an informal environment. The company also encourages voluntary service to the community.

In order to inform employees’ families about the company’s philosophy, activities such as “*Conociendo Amanco del Perú*” (“Getting to Know Amanco Perú”), have been developed. In this activity, relatives of Amanco’s employees are invited to a one-day plant visit to observe company operations.

Amanco also offers a “*Taller de Generación de Ingresos*” (“Generation of Income Workshop”) consisting of courses in baking, handicrafts and other skills which employees can use to help generate additional income for the family.

Community:

Through its regular programs of dialogue, communication and consultation, Amanco meets with members of the nearby communities, such as the proprietors association (*COVESA*), the school administration, the parents association, the church and the medical center’s doctors, among others. A Job Program gives priority to people who live near the plant’s zone to be employed by the company. The Security Program involves working together with neighbors to improve security and prevent security-related incidents. Through an Education Program, the company has donated computers and other equipment and materials to students. The company has also offered leadership and sales training to graduating students with the objective of sharing with them Amanco’s philosophy as well as providing them practical information on managing a company.

Environment:

Amanco focuses first on the zone environment in which the company operates. A major project focuses on improving the environment adjacent to the plant which is implemented in collaboration with the local community. As part of its on-going environmental management activities, Amanco takes annual measurement of noise, dust and gases levels, the results of which are communicated to its neighboring communities.

The company offers training on plumbing and water treatment to develop vocational skills of participants and at the same time increase their awareness of the importance of good water management practices. The company has pursued a number of other actions focused on addressing water problems, as follows:

- Together with ONG *Ecociudad*, the company has implemented an experimental project to re-utilize lavatory and shower water in some of the parks of the community. The pilot project which covered three parks in Villa El Salvador will be replicated in other locations.
- To build awareness of the consequences of the emerging shortage of water in Peru and beyond and to encourage collaboration with the community the company has implemented a campaign entitled “Latinoamérica tiene sed” (“Latin America is thirsty”),

The Company wishes to build awareness not only of society in general but also of the industries that use large amounts of water in their operations. Therefore Amanco is creating projects jointly with such companies to improve the quality of water and also improve the quality of life for society as a whole.

Clients and Suppliers:

Amanco has developed consultation processes that are conducted every three months to evaluate both Amanco’s service levels and commitment to serve society through its operations. The company also organizes regular conferences related to technical plumbing qualifications.

Suppliers are considered as strategic partners of the company and Amanco’s corporate values are laid out in its written suppliers’ policy.

Amanco por un Perú mejor (Amanco for a better Peru)

Beginning in 2004, Amanco has developed and implemented a program called “*Amanco por un Perú mejor*” (Amanco for a better Peru). The program’s core purpose has been to involve the entire group of Amanco’s employees (“collaborators”) in implementing the CSR strategy of the company.

Program Target:

The primary goal of the program is to make Amanco’s collaborators or employees the main promoters of social responsibility in Peru by involving them in the full range of CSR programs.

This program also looks for various interest groups to become part of the company's ethics philosophy, efficiency and corporate social responsibility.

The target as defined by Amanco is the following:

“Contribute to the improvement of the quality of life and competitiveness of the group of micro- entrepreneurs that are in the hardware dealing and plumbing business and which forms part of Amanco's supply chain.”¹⁸

The program assesses its results based on the following specific targets:

- To fortify the technical and enterprise capacities of a group of plumbers and hardware dealers related to Amanco.
- To support these people in improving their quality of life through a healthier life.

Strategic Variables:

The activities developed by the program are classified in terms of three important variables, which represent a fundamental aspect of Amanco's CSR strategy. These are **progress, health and attitude**.

Progress:

This is defined as the company's contribution to the improvement of the competitiveness of Amanco's supply chain, including suppliers, collaborators, clients, independent plumbers and the community at large.

To help ensure achievement of this target, Amanco created a strategic alliance with *PROMPYME* (Peruvian Center of Promotion of the Small & Medium Enterprises) and *Fundes Chile*, a Latin American organization situated in Chile that is dedicated to support micro entrepreneurs with specially designed courses and workshops. *Fundes Chile* had qualified over 40,000 companies in different economies of Latin America. These institutions assumed the responsibility of developing qualifications for entrepreneurs for Amanco.

The alliance with *PROMPYME* intended to strengthen the technical and entrepreneurial competence and capabilities of Amanco's clients. In order to achieve this objective, *PROMPYME* worked with a program created by the Peruvian government called “*Perú Emprendedor*” (“Entrepreneur Perú”), which helped to finance 75% of Amanco clients' qualifications. This way, the company guaranteed that every client received 12 qualifications and four types of technical assistance, which could be used either by the proprietor of the enterprise or by its employees.

The alliance with *Fundes Chile* made possible the offering of six qualifications to 240 clients. A training of trainers approach was adopted so that for every qualification that was offered, a group of Amanco employees were trained to teach an entire group of interested clients. Some also trained other people who worked for Amanco, as well as suppliers, clients and members of the community.

Health:

The purpose is to improve the health of Amanco's stakeholders in order to increase their productivity and to create a better working environment among employees. To achieve this,

¹⁸ Amanco del Perú “Profile of the program Amanco for a better country”. April, 2005.

Amanco signed an alliance with Catalyst, a partnership of five non-governmental organization (NGOs) that supports different programs related to health. It counts on the financing of the USAID (United States Agency for International Development). As part of the benefits of this program, participants could access cheaper medical services and tests or examinations.

Attitude:

Amanco's purpose is to foster a positive attitude and increase the level of commitment for CSR among the company's stakeholders. Throughout the program, concepts related to social and environmental impact management and corporate social responsibility were reinforced. With the participation of The Avina Foundation, a social responsibility qualification was developed. The Avina Foundation was created by the Switzerland industrialist Stephan Schmidheiny, with the objective of generating alliances or associations among leaders of civil society on sustainable development in Latin America and Spain.

Amanco's actions had a profound impact on stakeholders' perceptions about the company. In late 2004 alliances were formed with *Fundes Chile*, Catalyst and *PROMPYME*. During the initial stages of implementation, 20 ambassadors were trained to qualify other people; 100 of the best hardware dealers were qualified along with more than 80 suppliers, 60 collaborators and 60 young people from a neighboring community. It is important to note that as part of their initial commitment, the collaborators assumed responsibility for providing qualifications to Amanco's stakeholders.

Alliance with PROMPYME:

The purpose of this alliance was to promote CSR based on models previously developed and applied by *PROMPYME* and Swisscontact in order to improve the competitiveness of the Peruvian economy. This included the development of pilot projects, in which the best CSR initiatives were co-financed by companies in the private sector. The intent was to create a demonstration effect to legitimize improvement of enterprise competitiveness for local economic development. They also agreed to provide qualifications to 100 hardware dealers and to the independent plumbers associated to them.¹⁹ The main objective was to improve the skills of these people and to develop sustainable sale strategies for businesses.

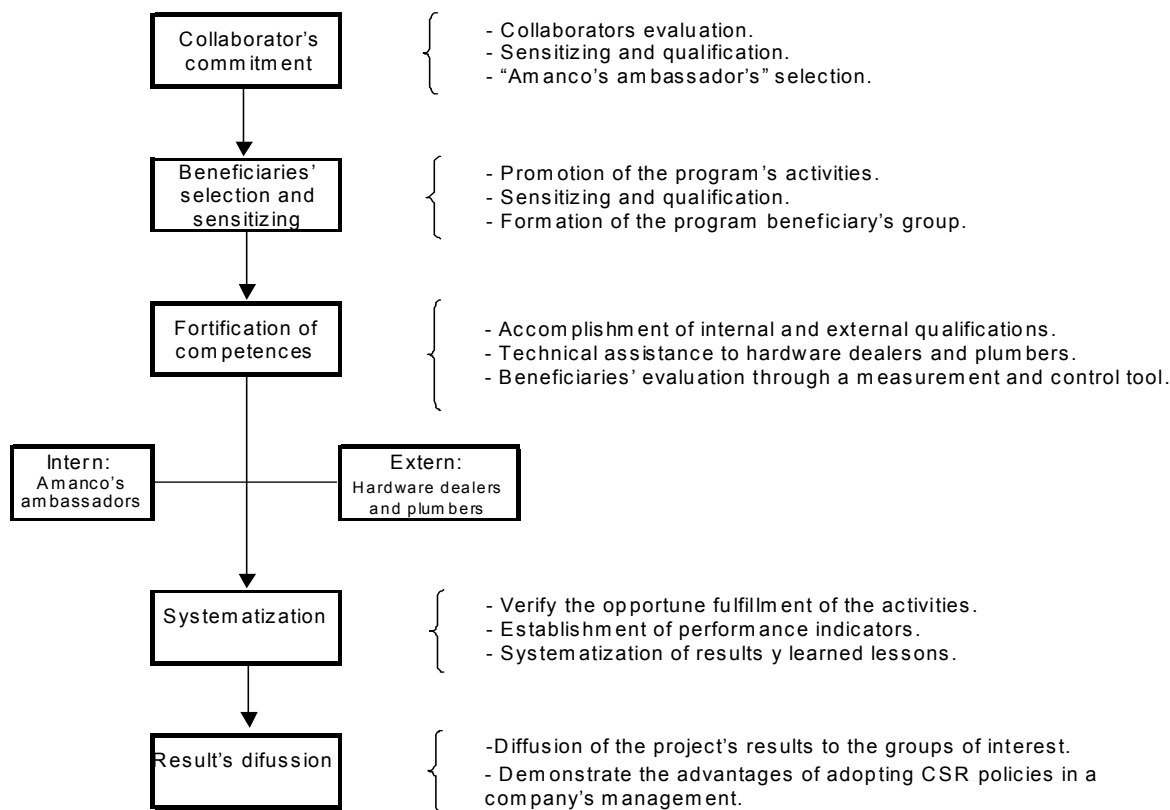
"Amanco for a Better Country" Activities:

The activities developed by Amanco within the context of this program involved a number of stages, which are shown in **Figure 6**.²⁰

¹⁹ This group of beneficiaries have an average journal of 40 soles (13 dollars approximately). Around 80% of this group have no technical education and the majority of them have only finished preliminary school.

²⁰ See Appendix 4: Activities of the program "Amanco for a Better Country."

Figure 6:
“AMANCO FOR A BETTER PERU” ACTIVITIES



Source: Amanco del Perú S.A., Elaborated by author.

Through their participation in activities developed by the company to sensitize, qualify and inculcate the company's social responsibility strategy among its collaborators, participants could be selected and evaluated on the basis of the kind of relationships that they had developed with Amanco's stakeholders. Following the initial screening, the company proceeded to qualify the selected collaborators in subjects related to the CSR strategies as well as in relation to the economic, social and environmental development needs of the stakeholders.

With the objective of generating greater interest among its clients about this CSR initiative, Amanco began a sensitizing process concerning the importance of the CSR to the company's strategy, based on the development of its value chain. Finally, they developed an action plan that included terms, activities and strategies for the qualification of the company's clients.

Next, Amanco developed a process of selection and sensitizing of beneficiaries, with the objective of informing Amanco's clients of the benefits of obtaining the qualification they were going to offer. In this way, they involved key beneficiaries in a manner that contributed to the development of the CSR strategy. The key was to demonstrate to the participants the principal benefits that they would obtain from the qualifications. The next activity was the reinforcement of the hardware dealers' and plumber's capacities through both formal qualifications and technical assistance to strengthen the competitive position of these groups. Subjects addressed included social responsibility, health, water management, ethics and customer service, among others.

Amanco articulated an evaluation tool that compiled information and generated individual diagnoses of the participating companies and plumbers, including information about production, technology, management, income management, and customer service. This same tool was used to

establish the baseline situation prevailing within the participating hardware dealers' stores and plumbing businesses.

In addition to their participation in external training, Amanco's ambassadors also took part in some free intern qualifications. The full list of courses offered included the following (**Box 1**):

Box 1:

Amanco's Intern Qualification:

Hardware Dealing: Ambassadors Program

- Fundes qualifications
- Occupational health course (developed through the Catalyst's alliance)
- Corporate Social Responsibility Course (At the end of the 2004 qualifications circle)

Plumbers: Technical Team

- Amanco's products course
- Occupational health course (developed through the Catalyst's alliance)
- Water management course
- Corporate Social Responsibility Course

Amanco's External Specialized qualification:

Hardware dealing: PYME Bonus

- Course on taxes
- Course on the control of inventories
- Course on customer service
- Course on computer sciences
- Course on marketing.

Plumbers: *Fundes*

- Technical course on plumbing
- Ethics course
- Course on customer service
- Basic course on costs (budgets)

The program was carefully and systematically monitored to verify if activities were completed and to track performance indicators based on a logical framework. The main results and lessons learned were recorded for application in future projects.

Finally, the process ended with the diffusion of the project's results (see Appendix 5) to demonstrate the advantages of adopting CSR strategies by both large and medium-sized corporations.

Lessons Learned

In today's competitive world, companies must fight to survive in the global market in which they operate. "*Amanco del Perú*" provides a clear example that a company can be successful by incorporating social responsibility principles into all their management policies.

The most important lessons that can be learned from the present case are:

- Corporate social responsibility represents Amanco's way of life and it has made Amanco a unique company in Peru. This company has integrated CSR into all its key management activities and through this process, it has guaranteed the sustainability of the company.
- When a strong commitment to CSR exists at every level of the company, it is easy to obtain favorable economic results.

Amanco's CSR focuses mainly on its people, which it refers to as its collaborators instead of employees. The working environment has improved through such practices as rewarding people's good work, promoting from within, and conducting annual surveys of collaborators' perceptions.

The company's collaborators are constantly stimulated, which facilitates alignment with the philosophy of the enterprise. For this reason, Amanco has designated its employees to act as ambassadors for the company in its relationship with the broader society.

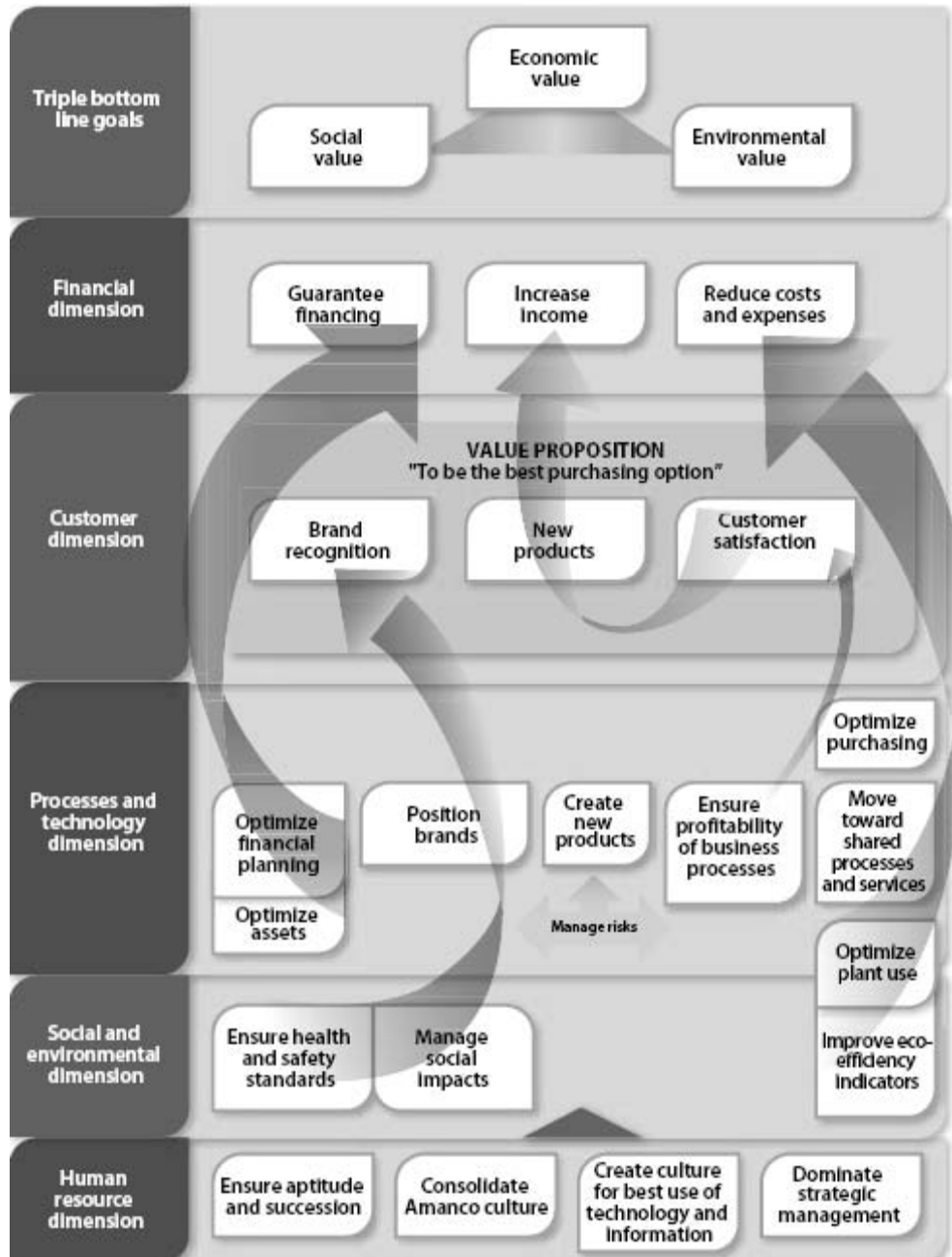
- Amanco has built its client capacities by offering them training to enhance their skills and develop specific qualifications. The clients not only benefit themselves but also develop the economic sector to which they belong.
- Clients value companies based on their perceptions of ethics and responsibility. But this is not enough as these characteristics must be accompanied by good quality products, competitive prices, opportune deliveries and excellent customer service.
- The way to involve the clients in the responsible vision of the company is through communication and dialogue. On-going communication of developments affecting the enterprise executed through a professional public affairs department is critical. This is why Amanco has its own Social Responsibility and Communication unit to publicize CSR programs and achievements.
- Being part of a larger group enterprise has facilitated management at Amanco, not only in improving common services such as materials procurement, but also in sharing good practices and experiences.
- Amanco tracks its performance carefully using a variety of indicators that measure progress in the specific areas of value creation. At present, Amanco does not track indicators that specifically measure productivity within the overall supply chain. Nonetheless there is a general perception that the company is undertaking activities that are improving the efficiency of the supply chain.
- The best approach to living in harmony with neighbors is through communication. Companies must make it their business to know the expectations and the problems of the communities in which they operate and should have regular consultations and efficient communication methods. Amanco has demonstrated its commitment to interact well with its communities.

Appendix 1
Corporate Governance

GrupoNueva's model of Corporate Governance



**Appendix 2
AMANCO'S Strategic Map**



Appendix 3 Strategic Indicators and National Production Volatility within the Construction Sector

Strategic Indicators (Var. %)

	2002	2003	2004	2005 ²¹ (Projected)
VAB	7.9	4.2	4.7	5.2
Cement Internal Consumption	8.4	3.3	5.5	6.3
Local Distributions	8.5	3.1	5.7	4.4
Construction advance	25.0	46.3	-8.5	45.2
Materials Prices	0.7	3.0	12.5	3.5
Cement Prices	-0.2	1.8	-0.5	-1.1
Materials Import	61.7	-27.1	4.3	1.9

Source: Historic data of INEI, ASOCEM, SUNAT, MIVIVIENDA, SBS.

National Production Index Variation (%) Construction sector, 2003-2004

Year	June	
	Monthly	Accumulated
2003	10.4	5.0
2004	5.5	5.7

Source: INEI-Economic Indicators of Technical Direction

Appendix 4 Performed Activities in the “Amanco por un Peru Mejor”

Objectives	Performed Activities
Employees Commitment	Collaborators evaluation and selection Collaborators training Client interest generation Action plan elaboration
Beneficiary selection and sensitization	Incentives Program Sensitization event for Hardware MYPE Compromise sensitized MYPEs Select Hardware MYPEs Convoke, sensitize and commit plumbers to form work groups (with MYPE help)
Strengthening of capacities	Design evaluation tools Evaluate committed MYPEs Design training and technical assistance plan Identify suppliers Commit “Peru Emprendedor” PYME bonds Organize hardware stores into groups Implementation of training plan Evaluate MYPE capabilities
Strengthening of plumbers capabilities	Design evaluation tools Evaluate sensitized plumbers Design training and technical assistance plan Implementation of training plan Evaluate plumbers' capabilities
Monitoring and systematization	Monitoring of project management Impact monitoring Systematization of results
Results Diffusion	Graphic and audiovisual material production Incorporate MYPE information into Website: http://www.mypeplaza.com Execution of diffusion events
Health campaign	Health training Health Exams

Source: Amanco del Perú. “Perfil del Programa Amanco por un Perú Mejor. Abril 2005
Elaborated by author

²¹ Projected

Appendix 5
Program Achievements
“AMANCO POR UN PERÚ MEJOR”

TRAINING	
	2005
Company Training with Fundes	
Clients	204
Collaborators	70
Suppliers	80
Community	70
Company Training with Prompyme	
Clients	22
Company Training with Catalyst	
Collaborators	60
Clients	15
Community	September
Ambassadors	
Train Ambassadors	32

CONSULTS		
	2004	2005
Opinion Poll		
Community	70	Octubre
Clients	317	271
Suppliers	121	70
Discussion Tables		
Community	4	70
Clients	2	6
Suppliers	2	4

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Corporate Social Responsibility in Supply Chain Management:

A Case Study on NTUC FairPrice Cooperative Ltd

Singapore

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Executive Summary

NTUC FairPrice Cooperative Ltd is the leading supermarket retailer in Singapore. The company is known as a “supermarket with social conscience.” Its supply chain activities focus on developing effective strategies to improve product quality and safety by working closely with its suppliers in implementing standards and good CSR practices.

Singapore imports 95% of its vegetables from other economies since the local farms cannot meet the local demand. FairPrice itself imports about 80% of its vegetables. Sellers need to ensure that the vegetables are safe for consumption and its supply is ample.

FairPrice invested in a fresh food distribution center in 2002 to enhance its ability to move its stock faster and maintain freshness quality. The Good Agricultural Practices for Vegetable Farming (GAP-VF) certification ensures that local suppliers meet the standard but the certification does not cover overseas suppliers. FairPrice needs to encourage these overseas suppliers to adopt similar standards.

The standard applied to organic vegetables is even higher. FairPrice works with Agrifood Technologies Pte Ltd to develop an in-house certification program that would provide assurance of the integrity of the organic produce.

FairPrice participates in the Pekan Baru project, a collaboration of the Indonesian and Singapore governments. FairPrice purchases 50 tons of vegetables per week from Pekan Baru. As the sole importer of the vegetables produced in Pekan Baru, FairPrice provides more work and income for more than 500 farmers and many operators along the supply chain.

The project also involves technology transfer which helps the farmers to implement good agricultural practices and get higher yields of better quality vegetables. Pekan Baru farmers learned the technology on cold chain management which makes it possible to maintain the freshness of vegetables while being transported from the farm to FairPrice distribution centers.

With quality assurance, FairPrice packages the vegetables under its house brand, Pasar. Branding the vegetables under Pasar has helped to market and increase demand for vegetables from Pekan Baru since FairPrice is a trusted brand in Singapore.

CSR is a journey and FairPrice continues to strive to be the best place to shop, the best place to work, and the best corporate citizen.

Introduction

In the retail sector, companies compete for the consumer’s money by looking at the marketing mix of 4Ps – Product, Price, Place and Promotion. These are traditionally the four factors that retailers consider in their marketing strategy. However, due to globalization and better consumer awareness, retailers need to address another 3Ps - People, Planet and (not only) Profit.

Consumers no longer just buy what is displayed on the retail shelves. They are asking questions as to how the products have been produced, and what has been their impact on society and the environment. For retailers to compete effectively in the market today, they need to assure consumers that what they put on the retail shelves are ‘ethical products’.

In the supermarket retail industry, product quality (e.g. freshness, taste) and safety are two of the key concerns. If consumers in Singapore are in doubt about the product quality and safety of any retailer, they have alternative sources such as vendors in local fresh produce markets. Hence, to

compete effectively, supermarket retailers need to look at how and not just what they are doing in business. By examining the opportunities and challenges in the context of Corporate Social Responsibility (CSR) within the supply chain, businesses can sharpen their competitive edge and be good corporate citizens.

Company Profile

Established in 1973 by the labour movement, NTUC FairPrice Cooperative Ltd has grown from its first shop set up to moderate the price of sugar and rice to being the leading supermarket retailer in Singapore. It employs over 5,000 and runs a retail network of 216 outlets comprising 76 FairPrice supermarkets, one FairPrice Finest, two FairPrice Xtra (Hypermart), three Homemarts, 19 FairPrice Xpress and 116 Cheers Convenience Stores. FairPrice's founding mission was to moderate the cost of living for the ordinary households in Singapore. Over the years, FairPrice's mission has evolved to its present mission which is to moderate the costs of a good life. Essentially, FairPrice's aim is to be:

- the best place to shop,
- the best place to work, and
- the best corporate citizen.

To be the best place to shop, FairPrice focuses on maximizing consumer satisfaction which is based on its brand promise of delivering value, quality and service. Key to this commitment are its procurement practices. FairPrice's product sourcing takes into account consumer feedback and needs, and market trends. It sources from established and reputable companies. It always tries to diversify its sources of supply, particularly for essential items. It also develops its own range of house brand products to offer consumers an alternative to national brands.

FairPrice plays a strong role in establishing the price of essentials in Singapore. During the avian flu outbreak that resulted in the ban of egg imports from the region, FairPrice responded swiftly to the crisis by putting in place precautionary measures to curb profiteering. To prevent arbitrage, FairPrice took unpopular but necessary measures in restricting the purchase of eggs. To further alleviate the egg shortage, it imported Australian and New Zealand eggs as alternatives. Even after the ban on Malaysian poultry imports was lifted, FairPrice continued its efforts in working with business partners to peg chicken and egg prices at a reasonable level. Through this, FairPrice helped restore egg prices to pre-ban levels.

To be the best place to work, FairPrice is a unionized employer that has good labour-management relationship. FairPrice takes a holistic approach in providing for employees well-being and opportunities for growth and development. FairPrice received the Work-life Excellence Award 2006 conferred by the tripartite committee on Work-life Strategy Singapore, in recognition of its programs to help employees balance personal commitments and work responsibilities.

FairPrice contributes to the community through its own initiatives such as its annual Used Textbooks project, its Million Dollar Food Voucher Scheme for the needy and the provision of study grants to children of needy members. It also engages its network of suppliers to support its community efforts such as Heartstrings Buys, a fund-raising drive for the Community Chest.

To promote environment protection, FairPrice launched the 'Love Nature' reusable bags to encourage its customers to reduce their reliance on plastic bags when shopping for groceries and necessities. In addition, the company participated in the 'Bring Your Own Bag Day' to encourage

shoppers to bring their own shopping bags instead of using plastic bags. Cashiers at the retail stores have been trained to pack more items in each bag to reduce the consumption of plastic bags.

As a good corporate citizen, FairPrice was cited as the “supermarket with a social conscience” by the Far East Economic Review in a 2000 survey report. In September 2005, FairPrice signed the UN Global Compact (UNGC) to support the initiative of the Singapore Compact movement to establish a UNGC network in Singapore and help raise awareness among more companies of the key principles of CSR which it upholds. FairPrice was also conferred the President’s Social Service Award in 2005 in recognition of its contributions to society. As a responsible food retailer, FairPrice is both a Case Trust accredited member and a Food Safety Partner of Agri-Food & Veterinary Authority (AVA) the economy-wide food safety authority of Singapore. FairPrice also supports pro-family initiatives and prides itself as a pro-family business retailer.

It was voted one of the best loved pro-family retailers in the Singapore 2006 contest organized by the Ministry of Community Development, Youth & Sports. In another survey conducted by the Reader’s Digest in 2006, FairPrice was voted in by consumers and won the Trusted Brand Gold Award for the supermarket chain category in Singapore.

The Supply Chain

Singapore has only 256 licensed farms covering 746 hectares¹ which cannot supply enough fresh meat, fruits and vegetables to meet the demand of its population of 4.4 million. Singapore imports 95% of its vegetables worth S\$314 million since local farms can meet only 5% of the demand for vegetables. It imports vegetables from Australia, China, Indonesia, Malaysia, Thailand, The United States and Viet Nam. With Singapore’s high dependence on imported fresh vegetables, local sellers such as supermarkets need to ensure that the imported food is safe for consumption and its supply is ample.

FairPrice invested S\$25 million on a 130,000 square feet fresh food distribution center in 2002 to better manage its supply chain for fresh food. The setting up of the fresh food distribution center enhances the ability of FairPrice to move its stock faster and maintain freshness quality.

The distribution center also provides the right infrastructure to improve the handling process of fresh food, thus reducing spoilage. Good temperature management and storage management are critical in maintaining the quality of food and preventing cross-contamination. FairPrice is committed to maintain a high standard of food safety and hygiene at the fresh food distribution center by getting the center to be Hazard Analysis Critical Control Points (HACCP) certified.

From the distribution center to the retail stores, FairPrice uses refrigerated trucks to transport the vegetables. At the store, temperature checks are conducted again before putting the vegetables on the retail shelves.

FairPrice works with the relevant authorities to develop standards. One such initiative is the implementation of the technical reference standards on cold chain management for chilled pork in 2005. The standard was developed by AVA and SPRING Singapore, the economy-wide standard body, together with FairPrice. It provides strict receiving, storage and display guidelines to ensure that the quality of the pork is not compromised. With the implementation of the standard,

¹ Good Agriculture Practices for Vegetable Farming, Agri-Food and Veterinary Authority of Singapore. November 2006.

consumers are assured that they are purchasing safe and fresh pork from FairPrice. The standard is now applied industry-wide.

On 07 September 2007, SPRING Singapore, working with AVA and the relevant stakeholders, launched the Technical Reference (TR) on Cold Chain Management for vegetables (TR 24: 2007) to ensure their freshness and safety. FairPrice was among the first supermarkets to work with the standard body to pilot and test the TR guidelines. FairPrice is now looking into the implementation of the guidelines to narrow gaps in the supply chain of fresh vegetables.

Occupational safety and health at the distribution center is also a critical issue. Since the temperature of the cold storage rooms at the center can be as low as sub-zero degree Celsius, FairPrice provides proper clothing to keep employees warm. In addition, FairPrice does not allow employees to work more than 20 minutes inside the frozen warehouse that has temperature of sub-zero degree Celsius; another team takes over every 20 minutes.

With FairPrice managing its own supply chain from distribution center to the retail stores, the company ensures that its operations are of high standard for both consumers and employees. However, FairPrice also wants to make sure that within the supply chain, its suppliers are able to meet its stringent standards in producing and managing fresh vegetables. They also have the challenge of making sure that the process of producing food products is in line with CSR principles.

FairPrice imports about 80% of its vegetables from diverse sources in China, Indonesia, Malaysia, Singapore and other places. In Singapore, FairPrice works with its local suppliers to encourage them to adopt Good Agricultural Practices for Vegetable Farming (GAP-VF) developed by AVA. Local suppliers voluntarily participate to be GAP-VF certified inasmuch as the benefits of business growth outweigh the cost of certification.



The objectives of GAP-VF certification scheme are:

- To promote a globally recognized food safety system at source,
- To promote shared responsibility in food safety, and
- To provide a form of product differentiation mechanism and sharing benefits with stakeholders.

Though the primary objectives of GAP-VF focus more on the food safety issues, it also includes factors that take environment issues into consideration. An environment impact assessment needs to be carried out to determine if the land is suitable for farming. If not suitable, the farmers would be advised to implement appropriate preventive measures. The farm would also need to construct the farm structures and layout in accordance with national regulations for safe buildings and sustainable environment. While farming, the environment must not be polluted by the use of farm chemicals and any unwanted agrochemicals must be properly disposed of in accordance with the national regulations.

The standard also provides guidance on the usage of agro-chemicals such as pesticides and fertilizers to prevent contamination and integrate pest management (IPM) and nutrient management so that the farmers can carry out sustainable farming. If the soil becomes toxic, the land would no longer be used for farming and this would affect the livelihood of the farmers and workers. **Table 1** summarizes the components of GAP-VF standards.

The adoption of GAP is a global movement of growers who wish to develop opportunities in export markets. FairPrice works closely with its foreign farm suppliers to adopt similar GAP-VF standards in ensuring a supply of good quality vegetables for export to Singapore. The increase in

purchases from FairPrice is a good incentive for encouraging these foreign farmers to adopt good agricultural practices which are critical in ensuring safe food production and environmental sustainability in Asia.

FairPrice does not focus on vegetables alone. As a retailer, a lot of products on their shelves are pre-packed. For these pre-packed products, FairPrice conducts factory audits on factories to ensure that food safety is adopted in their preparation process and premises using the criteria enumerated in **Table 2**.

Table 1:
Components of GAP-VF Standard

Components
Farm Location
Farm Structure
Farm Environment
Farm Maintenance
Farming Practices/Methods/Techniques
Farm Management

Source: Agri-food & Veterinary Authority of Singapore

Table 2:
10 Criteria of Factory Audit by FairPrice

Factory Selection
Receiving and Storage
Processing Area
Machine and Equipment
Weighing Scales
Product Safety
Personal Hygiene
Pest Control
Documentation
Risk Level

The process of ensuring food safety in the premises is one of the key areas of focus. FairPrice audits the plants on their cleanliness and hygiene to make sure that the food chain flow is compliant with the relevant food safety standards. In addition, the company conducts audits to determine if the workers are properly trained to handle the products. Thus FairPrice observes the whole process, from preparation to product packaging, to ensure product safety.

Evaluating the above and other factors, the auditors rate the suppliers as low risk, medium risk or high risk. If companies are assessed to be in the high risk category, FairPrice advises them to address the relevant factors before they supply products to FairPrice.

In recent years, the demand for organic vegetables has increased despite their higher cost. Organic vegetables cost more than three times the price of non-organic vegetables. In its desire to provide fair market prices for consumers, FairPrice applies higher standards for organic vegetables than for non-organic vegetables.

Organic products need to adhere to certain organic principles and standards to be considered as authentic. According to the International Federation of Organic Agriculture Movements (IFOAM), the four principles of organic agriculture are as follows:²

- Principle of health
 - Organic agriculture should sustain and enhance the health of soil, plant, animal, human and planet as one and indivisible.
- Principle of ecology
 - Organic agriculture should be based on living ecological systems and cycles, work with them, emulate them and help sustain them.

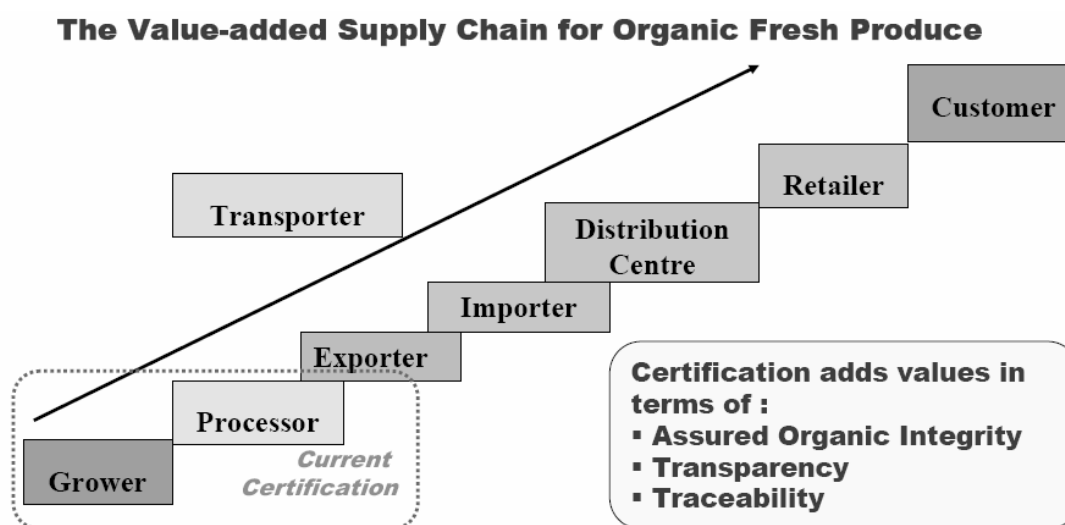
² Website: <http://www.ifoam.org>.

- Principle of fairness
 - Organic agriculture should build on relationships that ensure fairness with regard to the common environment and life opportunities
- Principle of care
 - Organic agriculture should be managed in a precautionary and responsible manner to protect the health and well-being of current and future generations and the environment.

In essence, organic vegetables need to adhere to CSR principles. FairPrice only purchases organic vegetables which are certified by the relevant certification bodies such as Australian Certified Organic Private Limited, the United States Department of Agriculture (USDA) and Organic Thailand, Ministry of Agriculture.

However, as most of the certification schemes cover only up to the processor stage (**Figure 1**), the integrity of the organic vegetables may be affected while in transit among the different players of the organic supply chain. FairPrice is working with Agrifood Technologies Pte Ltd to develop an in-house certification program known as NTUC FairPrice Organic Certification Program (NOCP) to close this gap. The certification adopts accepted organic guidelines from IFOAM and CODEX to suit the regional context. The certification provides assurance of the integrity of the organic produce on the retail shelves.

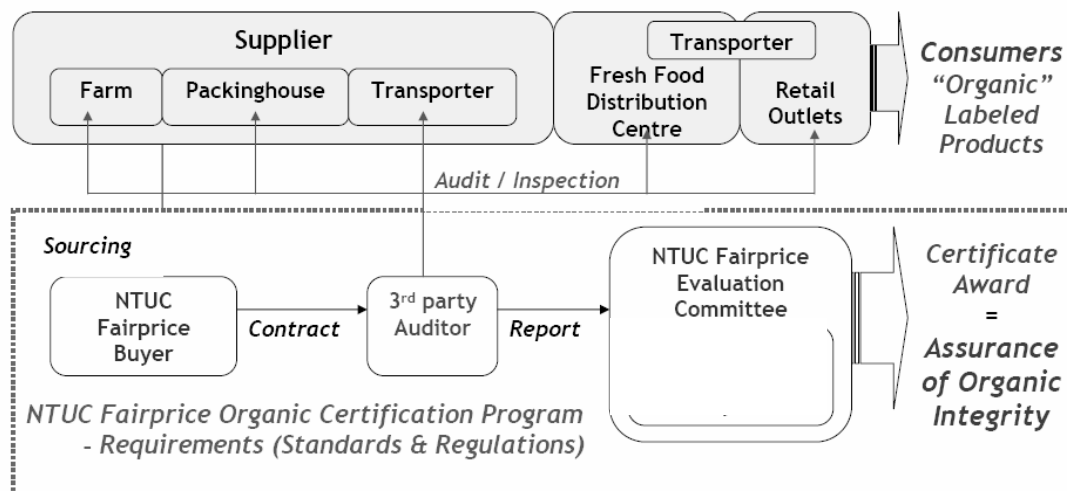
Figure 1:
Supply Chain for Organic Fresh Produce



Source: Agrifood Technologies Pte Ltd

In the certification process (**Figure 2**), FairPrice engages a third party auditor to audit and inspect the supply chain of organic vegetables from the beginning to the end. The auditor inspects the farm and the processing plant, even if the suppliers may have already complied with other standards. The auditor also checks on the process of transporting and handling of organic vegetables to the distribution center and then the retail stores. The auditor submits a report to the FairPrice evaluation committee which awards certification to the organic vegetables.

Figure 2:
NTUC FairPrice Organic Certification Programme Requirements



Source: Agrifood Technologies Pte Ltd

Through various efforts, FairPrice has improved its supply chain management of vegetables to deliver fresh and safe vegetables to consumers. FairPrice, as a good corporate citizen, has also taken part in a government-to-government collaboration between Singapore and Indonesia which has made positive impact on the community.

The Pekan Baru Project

In 2000, the Singapore and Indonesian governments collaborated to establish a vegetable project in Pekan Baru, Riau Province, Indonesia. The main objective of this project was to transfer technology on protected cultivation of leafy vegetables from Singapore to Riau farmers so that they could export vegetables such as *xiao bai cai*, *bai cai*, Chinese cabbage and *cai xin* to Singapore. This project would allow more diverse food supply sources for Singapore which had experienced food shortages due to supply shocks, such as flood and adverse weather.

Pekan Baru was selected as the site for the project because it was centrally located within Riau's traditional harvesting grounds of vegetables. It also had available land and labour, as well as a favorable environment for vegetable cultivation which made it ideal for agricultural purposes.

On 22 October 2001, the governor of Riau Province, Saleh Djasit and AVA chief executive officer, Dr Ngiam Tong Tau, signed a Memorandum of Understanding (MoU) for the vegetables project. The MoU entailed transfer of agriculture technology and cultivation techniques from Singapore agricultural technicians to their Indonesian counterparts.

The Riau Province Agricultural Services, Dinas Pertanian Tanaman Pangan (DPTP) and AVA were tasked to provide technical assistance on good agricultural practices and post harvest technologies to farmers in Pekan Baru for the production of quality vegetables for exports.

FairPrice was the sole importer of fresh vegetables from the Pekan Baru farms, purchasing 50 tons per week of fresh vegetables from the area.

Case Study: Singapore

The Pekan Baru project created more work and income for more than 500 farmers and many operators (packers, transporters) along the supply chain. Each farm in Pekan Baru was about 2,000 square meters and there were five farms within one hectare net-protected planting area. The farmers usually worked independently of each other. AVA encouraged the farmers to adopt good agricultural practices similar to GAP-VF because product quality is one of the primary concerns of bulk purchasers like FairPrice.

The seeds used for the crops were imported from Singapore. Farmers were taught to build their own net covered growing houses for protected crop cultivation which prevent insect infestation and protect vegetables from direct rainfall that could damage the leaves and expose the crops to diseases. Thus, the overall benefit was a reduction of agro-chemical usage and the production of high quality and safe vegetables for export. Farmers were also taught IPM and crop rotation and how to harvest and grade the crops. Hand-holding programs were held to teach the farmers proper techniques of farming.

With better farming techniques, farmers at Pekan Baru have been able to improve farm productivity and sustainability and lessened the likely occurrence of soil depletion with crop rotation.

Another key area of technology transfer was the setting up of the agri-processing center at Pekan Baru. Through AVA, Indonesian farmers covered by the project, learned cold chain management technology which is critical in maintaining the freshness and safety of vegetables. Investing in cold chain management technology has reduced spoilage, improved the quantity of vegetables that could be sold, and increased the income of farmers.

All the harvests from the farms are labelled with each farmer's name and area. Refrigerated trucks collect the vegetables from the farms and transport them to the processing center.

At the processing center, workers trim and sort the vegetables in the packing room where temperature is maintained at 18 degrees Celsius. All workers in the packing room are properly protected with warm clothing. After packing, the cartons are properly labelled, sealed and stored before being transported to Singapore.

The use of total cold chain management makes it possible to transport fresh vegetables from the farm to the FairPrice distribution center for more than 20 hours without affecting their quality.

As a whole, the Pekan Baru project has benefited various stakeholders: Indonesia and Singapore economies, farmers at Pekan Baru, the environment, the consumers and FairPrice.

Indonesia and Singapore

Former Singapore Minister for Trade & Industry, BG George Yeo, had said that the project opened a new area of cooperation between Indonesia and Singapore (EDB, 2002). Indonesia benefited from exporting vegetables to Singapore, while Singapore benefited from diversifying its food sources.

Farmers at Pekan Baru

The project had created work opportunities for the local community farmers, packers and transporters. In addition, the farmers have gained knowledge of good agricultural practices and can get higher yield of better quality vegetables. With better farming techniques and post-harvesting skills, the farmers can produce more vegetables and reduce spoilage. Furthermore,

FairPrice purchases directly from the agri-processing center which minimizes the use of middlemen. As a result, the farmers can generate higher income.

Environment

By adopting good agricultural practices such as crop rotation, IPM and protected crop cultivation, farmers are able to carry out more sustainable farming. Teaching the use of netted houses for crop protected cultivation on the farms, and proper pest control reduces the use of pesticide which has negative impact on the soil and vegetables.

Consumers

Consumers can now be assured that they can purchase fresh and safe vegetables from FairPrice. They also know that they are supporting a community by purchasing the vegetables from FairPrice. With FairPrice's commitment to provide best products at best prices, consumers know that what they purchase from FairPrice is always value for money.

FairPrice

FairPrice needs reliable supply of fresh vegetables since local sources alone cannot meet the daily consumer demand. With lessons learned from the Nipah virus in the late 1990s, FairPrice needs various sources of fresh food products. Through its participation in the Pekan Baru project, FairPrice was able to find new and steady supply of vegetables. Being one of the main buyers from Pekan Baru, FairPrice has encouraged the suppliers to improve the quality of vegetables.

With quality assurance in place, FairPrice has the confidence to package the vegetables from Pekan Baru under its house brand, Pasar. Branding the vegetables under Pasar has helped to increase demand for vegetables from Pekan Baru since FairPrice is a trusted brand in Singapore.

Conclusion

Through its participation in the Pekan Baru project, FairPrice added another source of high quality and safe fresh vegetables. FairPrice understands that they have a stake in the success of the project.

The various assistance provided to the farmers at Pekan Baru has enabled them to produce quality vegetables to complement supplies from other sources like China and Malaysia. FairPrice can explore further opportunities to work with the farmers and help them to be more productive and earn more income. With the increased demand for organic fresh vegetables in Singapore, the farmers at Pekan Baru may also practice organic farming in the future.

FairPrice has been in the forefront of various initiatives such as developing standards and supporting community projects. The company has recognized the strategic value of being a good corporate citizen. By identifying the gaps in their supply chain, FairPrice has been able to improve it and thus win the trust of the consumers.

While FairPrice's core mission continues to be to moderate the cost of living, it is also committed to look after the people, the planet, and then the profit. CSR is a journey and FairPrice continues to strive to be the best place to shop, the best place to work, and the best corporate citizen.

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Somboon Group (SBG) of Companies in the Auto-parts Industry in Thailand

Thailand

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The case was developed with the cooperation of Somboon Group solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective –” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author(s) and the Asia Pacific Economic Cooperation.

Executive Summary

The focus of this case is the Somboon Group (SBG), a Thai automotive parts manufacturer that supplies major automobile assemblers, primarily but not exclusively Japanese companies, and serves the after-market. SBG's experience illustrates the critical importance in international business of Corporate Social Responsibility (CSR) which encompasses safety, human rights, social aspects and the environment. All of SBG's business partners throughout the supply chain are required (both directly and indirectly) to implement CSR practices. The case study explores the critical success factors in securing support for CSR from the top management of all SBG business partners. They have taken note of SBG's position that an investment in CSR-related activities should not be regarded as an expense, but rather as an investment that provides sustainable long-term benefits.

SBG realizes that success in today's business strongly depends on effective cooperation from every component in the supply chain. The company has therefore addressed challenges and pressures from both the upstream and downstream parts of the supply chain. SBG strives to be a highly valued member of its supply chain not simply to survive in business but to continually increase customer satisfaction and take on its responsibilities to society and the environment.

The results have been gratifying. SBG is not only recognized as a creator of value by its business partners but also as a company with a very strong public image. SBG is well respected by both the private and public sectors in Thailand. Employee turnover at SBG is very low and no labor union exists.

SBG Profile

Somboon Group (SBG) is a Thai conglomerate which plays a major role in the automotive parts industry in Thailand. It has more than 46 years of experience with Japanese high-tech manufacturing processes.

SBG started in 1941 as an automotive understructure parts agent called Yongki Limited Partnership in Thailand. The Somboon Group was founded by Mr Somboon Kitaphanich who wanted to manufacture his own automotive parts. As a result, he established the first Thai-owned leaf spring factory near Bangna intersection, Bangkok in 1961. The company has steadily grown through the past 46 years and has been known as a leading automotive parts maker in Thailand.

The SBG Group consists of three companies with more than 1,700 staff members and about 600 million THB registered capital. These are the following:

1. **Somboon Malleable Iron Industrial Co, Ltd (SBM).** Founded in 1975, SBM operates ductile and gray iron casting foundry with parts machining. SBM produces various automotive parts from many grades of FC and FCD materials. The main products are drum brake, disc brake, hub, exhaust manifold, flywheel, bracket and gear box.
2. **Bangkok Spring Industrial Co, Ltd (BSK).** Established in 1976, BSK is a well-known full line spring manufacturer which currently produces leaf spring, hot and cold coil spring, stabilizer bar, torsion bar, valve and push rod for domestic and overseas Original Equipment Manufacturer (OEM) customers and after-market.
3. **Somboon Advance Technology PCL (SAT).** In 1995, SAT established itself as the market leader in rear axle shaft manufacturing in Thailand. SAT's products are made for

a one-ton pick-up manufacturer. It operates under fully automated robots with CNC machines running in one of the most advanced production lines in Southeast Asia.

SBG's subsidiaries have received several quality awards from major automotive manufacturers including the Quality Award (Zero Defect) from Mitsubishi Motor (Thailand), the Toyota Production System, Quality Control Cycle Award, and the Quality Assurance Award from Hino in 2006. The milestones in SBG's history are presented in **Box 1**.

Box 1:

Company Milestones

- 1941: Mr Somboon Kitapanich founded Yongki Limited Partnership as an automotive parts sale agent
- 1952: Somboon Spring Limited Partnership was founded as a pioneer in automotive spring manufacturing in Thailand
- 1975: Somboon Steel Casting Manufacturing Co., Ltd was founded
- 1977: Bangkok Spring Industrial Co., Ltd was founded as an Original Equipment Manufacturer (OEM)
- 1995: Somboon Advance Technology Co., Ltd was founded
- 1997: ISO 9002 Quality Control Award
- 1998: QS 9000 Quality Control Award
- 1999: ISO 14001 Environmental Management System Award
- 2000–2003: Economic hardship causing financial and management reorganization. In 2004, stock holders agreed to privatize, increase registered capital, and issue 74 million shares to the public.
- 2005: Registered in the Stock Exchange of Thailand on 31 January 2005 with ISO/TS16949 Quality Control Award

The SBG founder, Mr Somboon adheres to the following philosophy of living and running a business:

Alcohol and cigarettes should be avoided as they are no good for no one. We shall instead focus on our work; do all the best we can...if someone could do it, you as well could. Most importantly, we must be supportive to the ones in need. And finally, morality is the key to successful management, while treating all as if they are your family members.

Mr Somboon Kitapanich is strongly confident that as a pioneering company, SBG's operations would largely depend on how its employees contribute to its success, which in turn would be dependent on whether they are paid reasonably and fairly. On top of that, their family members must be able to live decent lives and enjoy good health. Therefore, Mr Somboon has always looked after his people and their family members as if they were his own. In fact, he has long been practicing CSR both within SBG and in the company's relationship with suppliers and customers long before the CSR concept became the buzzword in business management.¹

Everyone from management to blue-collar employees in SBG followed Mr Somboon's philosophy, resulting in corporate uniqueness, security, corporate loyalty, and compassion. No labor union ever existed in the past 46 years of the company's operations.

Due to the heavy industrial nature of its operations, it is almost inevitable for an automotive parts manufacturing plant like SBG to generate some environmental impacts. Fortunately, the SBG founder himself has been well aware and cautiously responsive to this concern from the very

¹ Mrs Kasamon Kittiampon, General Manager - Administration and CSR, Somboon Group.

beginning. The precautionary measures taken by SBG minimized environmental effects over the past several decades of its operation.

The company focuses its CSR programs on the reduction of air, sound, and chemical pollution in the surrounding communities. It is clearly articulated in the Corporate Mission that environmental responsibility must be an important component of the automotive supply chain in order to satisfy SBG's customers and all its business partners, as well as encourage its employees to be environmentally and socially responsible by participating in several CSR activities. To ensure that its operations are seen as environmentally responsible, SBG has engaged a group of agents to visit communities near its facilities at least once or twice every two months to collect information on any pollution that SBG may have inadvertently caused.

The company has a strong commitment to improve employees' morale, standard of living, and physical and mental health by paying reasonable wages and involving them in the company's community service programs. Getting the employees involved in community service programs enhance their awareness of social responsibility and at the same time maintain good business ethics.

SBG always considers social and environmental benefits as integral parts of the company's successful operations. SBG encourages the employees to be involved in charitable activities as their way of giving back to society. The company sponsors various independent social programs through a volunteer group that performs charitable work for the public and those in need. Employees are encouraged to join CSR activities during the holidays to help improve the environment in nearby communities, construct public places, renovate school buildings, donate money or essential items and organize activities for children or AIDS foundations.

SBG's vision is to be an employer of choice by improving the quality of life of employees and their families. The company strives to be a neighbor of choice for surrounding communities by expanding company activities to cover social and environmental aspects.

It is a challenge for the current [second generation] management team to attain the founder's objectives especially with regard to employees' welfare as well as the company's vision "to be a leading auto parts manufacturer of world-class standards with an aim to enhance product value and contribute to society."

The current management team has consistently and professionally handled associated activities. Financial assistance has also been systematically and fairly provided. SBG has been providing excellent benefit packages to its employees, including scholarships for employees to obtain their masteral degrees and 100 scholarships annually for children of employees to complete their college degrees. This has developed the employees' mentality to be generous, environmentally friendly, and responsible to society. In the face of Thailand's economic crisis in 1997, SBG still stood by its mission and continued its leading role in CSR implementation.

SBG in the Supply Chain

The advanced manufacturing technologies used in SBG are supported by leading Japanese companies. SBG purchases raw materials from local and international suppliers, including those in China, India and Japan. At the same time, the automotive parts manufactured in SBG are supplied to several customers both locally and overseas, including Australia, Indonesia, Japan and

Malaysia. Some of the main customers include Mitsubishi Motors, Toyota Motors, Honda Automobile, Isuzu Motors, Hino, Nissan and Auto Alliance.

Upstream Chain - Suppliers

Since SBG subsidiaries are public companies registered with the Stock Exchange of Thailand, all activities, including purchases of materials, must be conducted under the court of law and strictly in accordance with corporate governance set forth by the Board of Trustees of the Stock Exchange of Thailand.

Overseas suppliers such as China, India, Indonesia and Japan account for approximately 85% of the value of materials purchased by SBG while local suppliers provide the remaining 15%.² Despite the relatively small proportion of local suppliers in SBG's supply chain, they are given priority attention by SBG. The more than 100 local suppliers are trusted to provide raw materials, spare parts and components, stationery, and other key inputs to SBG.

Generally, quality, price and delivery are the priority concerns in most businesses, but SBG also adds environmental control as one of its top priorities. In particular, all SBG suppliers must comply with the following requirements:

1. All packing materials must be environmentally friendly and reusable.
2. All heavy metals component mixture, e.g., lead, cadmium, chromium, and mercury, must be declared from the manufacturers. Any supplier/manufacturer that does not comply with the environmental-friendly limit will be notified to get the problem fixed.
3. All suppliers (especially local ones) must be legally registered and operate under good governance. They must also possess reliable internal management and control, e.g., sales figures, turnover rate, safety system, major clients, etc.
4. Environmental control system must be enforced.
5. No employee or executive of SBG can be a shareholder of any of the suppliers.

Downstream Chain - Customers³

SBG has manufactured automotive parts (e.g., RR, axle shaft, leaf spring, stabilizer bar, coil spring, disc brake, drum brake, exhaust manifold, flywheel) specifically for automotive manufacturers both as Original Equipment Manufacturer (OEM) and those in the Replacement Equipment Market (REM). Some of SBG's customers include Mitsubishi, Honda Cars, Toyota, Isuzu, Nissan, Hino, Mazda, Ford, Honda Motorcycle, Volvo and General Motors. These world-renowned companies pose stringent requirements on SBG as one of their suppliers. Most clients require SBG to strictly follow their own regulations, and in most cases, require certification in some important aspects such as the following:

- ISO 9001:2000
- ISO/TS16949
- ISO 14001:2004
- Reusable pallets without oil or dirt contamination
- Secured packaging to avoid potential accidents during delivery
- Covered delivery truck to avoid accidents
- Delivery truck must be in good condition, with no visible smoke or oil leakage

² Mr Wichai Srimawan, Vice President, Procurement & Logistics, Sombon Group.

³ Website: <http://www.satpcl.co.th/product.html>.

- Maximum speed within the premises not to exceed 20 km/hr
- Engine must be turned off during stops within the premises

Some clients have imposed additional requirements on their suppliers. For example, while at the delivery sites, SBG is required to take back all the containers and packaging materials, and is not allowed to leave or dispose of them at the customer's site. Any act that may cause pollution is strictly prohibited. All SBG delivery personnel are educated and trained on safety and environment awareness that must be observed within the customer's premises. On the other hand, some clients require all their suppliers to attend their workshops and trainings on chemical and flammable or hazardous substance storage, and fire emergency procedures.

All of SBG's international clients regularly and seriously exercise CSR. They do not only aim to become good corporate citizens themselves but they also want companies such as SBG to be good corporate citizens before they could qualify as their partners.

Challenges from the Downstream Chain – Toyota

Toyota Motor Thailand Co., Ltd. is one of the leading automobile manufacturers in Thailand, with a current market share of about 40%.⁴ For the past 40 years, customers have placed their trust and confidence in this company and its products.

In the past, fatal accidents occurred frequently at Toyota Motor Thailand, causing serious injuries to a number of staff, and eventually a shutdown of the whole production line.⁵ Consequently, Toyota had to revolutionize its production and management in 2005 by introducing a "Completely Check Completely Find out (CCCF)" concept that places Safety as the top priority, with the belief that all accidents could be prevented. This CCCF plan has been implemented among almost all Toyota's affiliates and associates, including its suppliers and construction contractors.

As one of Toyota's first tier suppliers, SBG was required to adopt the CCCF plan as part of CSR in its own manufacturing operations. The CCCF aimed to increase security within the factory through examination and assessment of potential safety issues and to obtain preventive solutions. This was done with the cooperation of employees who helped identify potential problems and their resolutions.

SBG had to follow the stringent regulations without any financial support from the clients, thus it had no choice but to put its own money into the implementation of activities to meet Toyota's requirements. Simply put, if SBG had decided not to follow such requirements, it would have failed the client's performance assessment, which would have resulted in an interruption of business transactions with Toyota. It would also have been more difficult for SBG to acquire more clients. SBG's clients have recently added an extra annual cost savings constraint, which has further intensified the challenge for SBG.

⁴ "Sustainability Report 2006," Toyota Motor Thailand Co., Ltd page 6.

⁵ Op.cit., page 37.

SBG has grouped potential hazards into six categories according to potential safety issues that may arise from them⁶

1. Machinery hazard
2. Hazard from falling objects
3. Vehicle hazard
4. Fall-from-height hazard
5. Electricity hazard
6. Other hazards

To comply with Toyota's CCCF system, SBG was initially audited twice a year to ascertain if the company had met the minimum requirements. After a short while, however, SBG's performance was deemed to be satisfactory enough such that it was exempted from on-site auditing and was instead required to submit only regular progress reports to Toyota.

SBG's willingness to make the substantial investments required to ensure that it met the specifications of its customers and its success in achieving them emanated from the company's firm belief that from a long-term perspective, such activities actually help increase SBG's business potential, decrease company expenses, and reduce potential loss of property, health, and lives of employees due to accidents. In fact, much of SBG's CCCF achievement was rooted in its own long-standing commitment to CSR activities; hence, the employees did not regard the additional requirements as big changes that would require additional effort from them.

Some of SBG's long established CSR activities include:

- Refraining from drinking during the Buddhist lent period of three consecutive months, which is a campaign to have employees refrain from alcohol consumption for at least the entire duration of this period every year. The first-year campaign only had 27 participants, but subsequent campaigns saw an increasing number of participants reaching 900 in 2007. Many have quit drinking as a result of this program, which has resulted in improvement in their families' financial conditions, better relationships among family members, and healthier physical and mental conditions. The employee can come to work with full energy, which in turn results in reduction of accidents at work.
- Employees are encouraged to participate in various contests and activities that help identify and suggest potential safety issues, prevention, and solution. A special award is given to the department that has zero accident rate within a specific time frame. SBG has campaigned to make 2007 the year of accident reduction at work.⁷
- SBG is trying its best to promote awareness of occupational safety and to help all employees to realize the consequence of accidents, not only to the employees themselves, but also to their family members, as well as to SBG and its business partners. Damage to the business would hurt the employees themselves.
- Other than enforcing strict regulations for their own employees, SBG also asks for supplier's cooperation to follow both safety and environmental policies while being on SBG premises. This has turned out to be a big challenge when dealing with suppliers (**Appendix 1**).

⁶ Mr Kasidit Charoenpun, Safety Manager, Somboon Group.

⁷ SBG Network Quarterly, Vol.14 (1), 2007, page 14.

Challenges from the Upstream Chain - Small Suppliers

To successfully achieve Toyota's CCCF requirements, SBG had to readjust its own procedures and at the same time make sure that all its suppliers supported SBG's new safety measures. SBG therefore added an extra step in its safety and environment control regulations by closely monitoring and strictly enforcing upstream safety and environmental practices by its suppliers, including delivery, packing and pallet stacking. More specifically, the delivery truck must be in good condition, and driven within SBG's premises at a safe speed, not exceeding 20 km/hr. The truck driver must also be properly dressed.⁸

Every so often, drivers and delivery persons from suppliers come to SBG premises wearing only slippers. SBG therefore prepares proper shoes for them to wear within the premises to prevent accidents. All flammable fluid containers in the delivery truck are also inspected and must be securely fastened prior to entering the SBG premises to avoid unwanted movement and grazing or pose as possible fire hazard.

Some enforcement efforts did not receive very positive response at the beginning. For example, at times, delivery trucks came in with muddy wheels. As dried mud tended to create dust, the security guard began to deny these delivery trucks entry to SBG property until the mud was removed. The truck drivers were certainly irritated and resisted the clean wheel requirement, but SBG still stood firm in its enforcement policy. The current practice is that if any problem is present in a delivery, the top management is notified and the performance assessment scores of such a supplier are adjusted downward at year-end. During the past year, SBG has received good cooperation from all its suppliers since there has been a general understanding that the company would stop dealing with any uncooperative supplier.

In general practice, suppliers who do not meet the quality requirements or those with low performance scores are subjected to stringent auditing to discuss problems and solutions. In addition, the supplier has also to do its own internal assessment, especially of safety and environmental issues, based on a given template.

Although SBG does have clear policies for the management of environmental and safety issues, communication with all working levels in each supplier is sometimes not effective enough to ensure that the rules are consistently and strictly followed. At times, some suppliers do break the rules, either intentionally or unintentionally. Part of the solution is to apply the same strict enforcement internally, that is, to have SBG officials continually examined for any violations, starting from the security guard booth at the entrance all the way to the receiving dock.

As anybody can imagine, since the suppliers must incur their own expenses to comply with SBG's regulations, the company is under considerable pressure to help its suppliers figure out what needs to be done so that the suppliers could adjust their systems to meet the required standard. SBG realized that a problematic supplier would affect SBG's own operations and ultimately affect SBG's customers. Therefore, SBG has arranged supplier meetings twice a year in order to reinforce the company's policy and request strict cooperation. During the supplier meeting on 14 February 2007, the company provided a guideline on CSR policies that each supplier must follow, (e.g., environment and safety control of their businesses) and encouraged them to participate in CSR activities to be conducted by SBG. These proposals were positively accepted.

⁸ Mr Kasidit Charoenpun, Safety Manager, Somboon Group.

The main challenge to SBG is to get all its domestic and international suppliers to understand and abide by its proposed CSR regulations at a low cost. It is not difficult to invest a lot of money to improve standards if the costs can be passed on to customers. But in the automotive industry, competitive pressures require both excellent quality and cost competitiveness. Many of SBG's suppliers requested a price increase on the grounds that they had to change many of their practices, such as disallowing illegal workers, improving workers' benefit, providing trainings to achieve ISO certification, and so on.

SBG took exception to the idea of passing on the costs, since it is the individual company's corporate responsibility to improve its quality and management practice. SBG itself does not think of CSR as a current expenditure, but as a valuable investment that is essential for its long-term business operation.

Seeking Assistance from Thailand Automotive Institute

For most small suppliers, neither a request nor the threat of enforcement alone was generally sufficient to guarantee that the supplier would be able to comply with the standard, due to the additional expenses involved. Many suppliers operating on thin margins would try to get around requirements whenever there was a chance to do so. At the same time, it would have been impossible for SBG to closely monitor every single supplier. The best way to address this dilemma was to have the suppliers themselves develop their awareness. SBG reasoned that once new policies were put into practice, suppliers would themselves clearly see their long-term benefits, compared to the *ad hoc* way of doing business. But this would require management capacity building. To make this happen, SBG sought the cooperation and assistance of an outside organization, the Thailand Automotive Institute (TAI). TAI has agreed to assist in providing public education and training to achieve an ISO-9000 conformed work system.

TAI has been assigned by the Thai Ministry of Industry to function as an Intelligence Unit through management information, analysis study and proposal to the management for the benefit of decision-making on policy. The institute also provides advice to support the sustainable development of the Thai automotive industry and strengthen its competitiveness.⁹

Another important mission of TAI is to serve entrepreneurs within the automotive industry, especially parts manufacturers. TAI has worked in various projects to increase efficiency in management, production, costing and the development of automotive standards. These interventions aim to increase the capacity of domestic manufacturers to compete within a regional free-trade area, and to increase capabilities in research and technology development, parts manufacturing and human resource development (See **Box 2**).

⁹ Annual Report 2005, Thailand Automotive Institute.

Box 2:**TAI's Scope of Work:**

1. Conducting research necessary for the formulation of suitable policies, and taking a coordinating role in facilitating the country's continuous automobile industrial development.
2. Preparing master plans for the development of Thailand's automobile and plastic industries, as well as comparative facts on the automobile industry. This is to create business competitiveness in domestic and international trade.
3. Assisting the country's spare parts manufacturers in developing their production technology towards international standards.
4. International capacity building: facilitating the development of human resources in the automobile industry.
5. Establishing national spare parts standards and providing inspection and testing services for spare parts certification.
6. Developing Thailand's automobile and spare parts testing center.
7. Applying latest techniques to enable Thailand's automobile industry to develop in terms of technology and quality.

TAI's Scope of Public Services:

1. Providing training, seminars and information services.
2. Providing advice related to the automobile industry.
3. Testing automobile products and spare parts

Through its cooperation with TAI, SBG has been able to organize very low-cost trainings for its suppliers to learn more and understand ISO-9000 system, as well as how to retool their business practices for higher-quality standards. In the recent round of training, seven out of 10 suppliers passed the requirements and were certified under SBG's requirements. These suppliers eventually realized that good working systems could maintain the high-quality standard of their companies and reduce unforeseen accidents. In turn, all business partners have gained more confidence which would ultimately bring lasting success to their companies. SBG's upcoming mission is to collaborate with TAI to give trainings for ISO-14000 compliance.

Conclusion

CSR is not widely recognized as the way of doing business in many companies in Thailand. However, some companies have implemented CSR progressively and the Thai government has also been promoting and encouraging good CSR practices. SBG is one company that has long seen itself as being responsible for its social and environmental performance. The manner in which SBG has adopted CSR has received considerable support from employees and business partners, and widespread recognition from both the Thai government and communities in which the company operates.

SBG adopted CSR principles based on its founder's philosophy. It has strictly practiced CSR for the past 46 years and its reputation for good CSR practice is widespread. Since SBG is registered in the Stock Exchange of Thailand (SET), its business can be audited by the SET and the public. In line with the SET's guidelines on good Corporate Governance (The Rule of Law, Morality, Accountability, Participation, Responsibility, and Cost-Effectiveness or Economy),¹⁰ all subsidiaries of the Somboon Group have strictly followed and put a high priority on environmentally friendly working conditions, providing to their employees mental and physical

¹⁰ "The Principle of Good Corporate Governance for Listed Companies," Corporate Government Center, The Stock Exchange of Thailand, 2006.

health care, human resource and skills development opportunities and social services. The company believes that the cost of training new employees would be much higher than investing in the implementation of CSR within the organization. That explains why SBG's employee turnover rate is very low.

Fortunately, SBG has rarely encountered problems with business partners in the supply chain, as its founder has long been practicing CSR even before it became an accepted concept in the business world. SBG has started with its partners first, resulting in effortless cooperation from other subsequent partners.

In conclusion, SBG's example emphasizes that the implementation of good CSR policies and practices will provide a long-term business payback despite the high initial investment required for its development. SBG clearly views CSR as a commitment that affects not only the company's business operations but also its employees' mindsets, satisfaction and dedication in their workplace. Several activities have reflected SBG's determination to be a good corporate citizen in order to be a role model for other organizations and build a social responsibility network under Thailand's sufficiency economy policy so that the Thai people can live happily together.

Appendix 1 SBG's CSR Activities¹¹

Somboon Group (SBG) has a long and good record in its several decades in business. SBG is committed to operate a business that is environment friendly and contributes to society. SBG also provides fair benefits and remuneration packages to their employees such as food allowance, plant transportation, health and life insurance, sport facilities and scholarship.

SBG also considers social and environmental benefits as part of the company's successful operation. SBG encourages their employees to be involved in charitable activities as ways of giving back to society, by sponsoring various independent social programs through a volunteer group that performs charitable works for the public and those in need.

Employees are encouraged to join CSR activities during the holidays to help improve the environment in communities nearby, construct public places, renovate school buildings, donate money or necessary items, and conduct activities for children and HIV foundations.¹²

A. Why CSR?

SBG has strictly followed its founder's philosophy that "Alcohol and cigarettes should be avoided as they are no good for no one. We shall instead focus on our work; do all the best we can...if someone could do it, you as well could. Most importantly, we must be supportive to ones in need. And finally, morality is the key to successful management, while treating all as if they are your family members."

This is why SBG has performed business transactions according to CSR from the very beginning and at every step of its way.

B. Giving Back to the Thai Society

In 1942, Mr Somboon Kitaphanich founded Yongki Limited Partnership as a sales agent of automotive parts which grew to a leading automotive parts manufacturer in Thailand. One of his philosophies is to closely pay attention to his subordinates and treat them as his own family members whom he "raises." He provides "warmth" to his employees in the workplace as their second home. He always provides for his employees and assists them when in need. He provides them a career path through scholarships for them and their children.

When the company has grown to over 1,700 employees, the new generation executive who is Mr Somboon's successor has to reorganize its management according to international standards but the big boss' philosophy still remains. Employee welfare remains a concern with the provision of lunch, per diem compensation, transportation, uniform, health and life insurance, scholarships for employees and their children, as well as performance-based extra pay. Annual Life-quality development activities for employees are continuously arranged, (e.g., anti-drug/anti-alcohol programs, SBG Smart Club, HIV awareness program, etc).

Another reason why this is the place to work is the secure and suitable working environment. SBG has given priority to the maintenance of the working environment according to proper standards without affecting the surrounding community. Working areas are clean and suitable for work and provided with necessary emergency tools around risky area as well as water treatment and smoke control system to avoid unwanted impact on the community. Green area and sporting area are also established as relaxation facility.

¹¹ Ms Kanjana Sookprom, CSR Manager, Somboon Group

¹² SBG Network Quarterly, Vol.13 (1-3), 2006.

When the family is fulfilled, sharing with neighbor is generally practiced in the Thai culture. SBG's social assistance started by giving help to people in need but eventually became a full range of social services and other social concerns of employees. Most of SBG Volunteer Club's activities with full support of employees were initially intended to develop communication skills within the organization. Subsequently, its members expanded the club activities to the communities outside during weekends starting from communities around the workplace, (e.g., cleaning public property, school building maintenance, toilet construction, playgrounds, home construction, and activities for HIV patients, people with disability and the elderly). SBG has sought the participation of executives, employees, business partners, government officials and the general public in these activities.

As today's business trend has put priority on Corporate Social Responsibility, it is often found that most companies focus on financial donations. However, financial considerations play only a small part in SBG's social activities since financial assistance alone cannot solve all social problems; it is developing voluntary mindset among executives, employees, stockholders, and business partners to help the less fortunate and disaster victims that can. Consequently, these stakeholders would also learn to utilize national resources effectively, persuade other specialized organizations to participate in these activities and convince the locals to be involved in their own community activities for sustainable growth. Therefore, SBG's social responsibility activities cover all aspects that would contribute to the economy's sustainable happiness.

BITIS in Viet Nam

Creating Values Through Good CSR Initiatives in Supply Chain

Viet Nam

Case Study:
Viet Nam

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The case was developed with the cooperation of Center for Development and Integration solely for educational purposes as a contribution to the Project entitled “New Corporate Procurement Strategy on Trade in Goods and Services in APEC Region - Supply-chain options with CSR perspective-” conducted under the auspices of the Asia Pacific Economic Cooperation (APEC). The case is neither designed nor intended to illustrate the correct or incorrect management of the situation or issues contained in the case. No part of this case can be reproduced, stored or used without the written permission of the author(s) and the Asia Pacific Economic Cooperation.

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Executive Summary

This case focuses on the experiences and practices of a Vietnamese shoe-making enterprise, BINH TIEN Consumption Goods Production Company Limited, popularly known as BITIS. It is an example of the development and implementation of an effective CSR strategy in the context of Viet Nam's rapid integration into the global economy and the concurrent transformation of BITIS from a modest local enterprise into an organization linked to a global supply chain. Given Viet Nam's fast-paced economic reform and recent accession to the World Trade Organization (WTO), Vietnamese enterprises are finding new ways of doing business in a more sustainable and competitive manner.

Becoming part of a global supply chain requires compliance with international standards, as well as considerable innovation in management practices. BITIS, supported by good CSR practices, has successfully developed its brand reputation and market presence. BITIS has a strong focus on improving its environmental and human resources practices, while working with overseas partners.

The growth of BITIS has followed closely the "Doi Moi" [renovation and opening up] of Viet Nam over the last 20 years. Its success shows that the private sector has played a key role in the economy's development and growth by "doing good and doing well".

Background

Viet Nam is entering into a period of more rapid economic integration with the facilitation of foreign investment and the increase in trade, all supported by internal economic reforms. These changes bring with them stronger economic growth as well as challenges for Vietnamese companies which are under increased pressure to improve their productivity, strengthen their competitiveness and develop their human resources.

Viet Nam's economy has experienced a spurt of growth following the "Doi Moi" reforms that began in 1986. Viet Nam is being touted as the next Asian miracle economy. The economy is attracting more Foreign Direct Investment (FDI). It has high literacy rate of above 90%. With its sustained growth rate of 7.5% per annum (2001-2005) Viet Nam has seen an impressive record of poverty reduction. At the same time the young population is demanding a better standard of living.

Viet Nam continues to make a successful transition from a centrally planned to a market-oriented economy. During the 1990s, Viet Nam's economy doubled in size, and the rate of poverty was halved. Export earnings grew from US\$2.4 billion in 1990 to US\$32.2 billion in 2005. Exports have grown at an average of 18% per year since 2000. This trend is expected to continue, guided by the government's commitment to export-led growth.

Viet Nam: Key Socio-economic Indicators (2005)

Population	82 million
GDP growth rate	8.1%
GDP per capita	US\$640
FDI	US\$3,3 billion (by end 2005)
Export volume	US\$32.2 billion (by end 2005)
Growth and Competitive Index	81/117 rank
Private enterprise	200,000 (by 2005)

Source: GSO and MPI, 2006

Viet Nam's international economic integration took important steps forward with the implementation of the bilateral trade agreement with the United States and the ASEAN Free Trade Agreement (AFTA), which required the reduction of tariffs and import barriers among all ASEAN members by 2006. Viet Nam achieved full membership of the WTO with its accession in late 2006. This will further advance Viet Nam's integration into the global economy.

Nonetheless the government recognizes that the pace of economic reform has been slower than it might have been, and that Viet Nam's economic growth path is not yet on a sustainable footing. Economic efficiency is not high, labour productivity is generally low, and many sectors and products are not competitive in global markets.

The implementation of socially responsible management practices by Viet Nam's business enterprises is recognized as an effective way to strengthen their competitiveness in the global marketplace on a sustained basis. But according to Transparency International's *Growth and Competitive Index*, Viet Nam ranks 81st among 117 economies. The World Bank's *Doing Business 2008* reports that Viet Nam ranked as number 91 out of 178 economies. Clearly there is room to do better.

Similarly, WTO membership has created both opportunities and challenges for Viet Nam. It is clear that Viet Nam is striving to facilitate its trade and is committed to the removal of trade barriers in order to stimulate growth in exports and imports. Not surprisingly, the impact of trade liberalization level differs from sector to sector. Research done by the Viet Nam Academy for Social Science has indicated that the commitments made in the WTO accession process would have negative impact on the fishery sector but would have positive impact on shoe production and textile making. At the firm level, the challenge will be for Vietnamese-controlled companies to compete effectively with foreign investment for their share of the Viet Nam market, not only in terms of their available resources, but also in terms of their business management capability. Adopting global standards in management practices and integrating into the global supply chains have become crucial requirements in this new and more competitive business environment.

CSR in Viet Nam's Private Sector

The World Bank Group's *CSR Practice* defines corporate social responsibility (CSR) as "the commitment of business to contribute to sustainable economic development working with employees, their families, the local community, and society at large to improve their quality of life, in ways that are both good for business and good for development."¹

The concept operates at four quite distinct levels. First, CSR is perceived as the participation of business enterprises in humanitarian and charitable activities. Second, CSR is based on good management practices, satisfying customer demands in terms of quantity and quality of product as well as timeframes for delivery of goods. Third, CSR often involves a certification process, such as SA 8000. Fourth, CSR can be viewed from a "brand protection" perspective. In this context safeguarding the quality of life of workers, stabilizing and developing the production of safe and reliable products, and operating in an environmentally-responsible manner all contribute to building a company's credibility and reputation in the marketplace.

The CSR agenda is relatively new in Viet Nam, although safeguards for worker's rights and working conditions are well-articulated in national legislation.² Just like in other APEC

¹ "Strengthening Implementation of CSR in Global Supply Chains," Oct 2003, World Bank Group.

² "Corporate Social Responsibility (CSR) in Viet Nam" - World Bank- Institute of Labor Science and Social Affairs Ministry of Labor - Invalids and Social Affairs, Viet Nam ,December 2003.

economies, CSR is a particular challenge for smaller enterprises, which predominate in Viet Nam. Indeed, there is a growing fear that many SMEs may have to shut down their operations if they fail to meet the new and tougher global standards. Hence, the strengthening of socially responsible behaviour concurrent with the further growth of SMEs is critical to the overall success of Viet Nam's development.

SMEs are defined as businesses and production establishments that have a registered capital of less than VND10 billion (about US\$670,000) and/or fewer than 300 annual permanent employees. SMEs contribute significantly to the Vietnamese economy as they account for 65% of the GDP (based on value-added), employ 85% of the industrial labour force and comprise 20% of the exports.³ A profile of Viet Nam's SMEs is shown in the following table.

Table 1:
Profile of the Small and Medium-Sized Enterprise Sector

Item	2000		2002		2004	
		%		%		%
Total number of Large Firms (>D10 billion)	5,983	—	8,692	—	12,335	—
Total number of SMEs	36,305	100.0	54,216	100.0	79,420	100.0
SMEs with less than D1 billion in capital	22,801	62.8	29,585	54.6	39,378	49.6
SMEs with D1 billion–5 billion in capital	10,759	29.6	20,141	37.1	32,739	41.2
SMEs with D5 billion–10 billion in capital	2,745	7.5	4,490	8.3	7,303	9.1
Total number of Large Firms (>300 employees)	2,391	—	3,077	—	3,533	—
Total number of SMEs (<300 employees)	39,897	100.0	59,831	100.0	88,222	100.0
SMEs with less than 5 employees	10,169	25.5	12,079	20.2	17,977	20.4
SMEs with 5–9 employees	10,900	27.3	18,139	30.3	26,459	30.0
SMEs with 10–49 employees	12,071	30.3	20,718	34.6	32,443	36.8
SMEs with 50–299 employees	6,757	16.9	8,895	14.9	11,343	12.9
SMEs by Sector (based on employees)	39,897	100.0	59,831	100.0	88,222	100.0
Agriculture, forestry, and fishery	3,230	8.1	3,223	5.4	2,221	2.5
Industry and construction	13,142	32.9	21,300	35.6	32,679	37.0
Services and commerce	23,525	59.0	35,308	59.0	53,322	60.5

— = not available, SME = small- and medium-sized enterprise.

Source: General Statistics Office and Asian Development Bank estimates.

Following implementation of the new enterprise law in January 2000, the private sector has flourished in Viet Nam. Some 38,100 private enterprises were newly registered in 2005, up from 14,400 in 2000. Viet Nam has about 200,000 private enterprises, with a total registered capital of about US\$26 billion. The improved investment climate has continued to support foreign investment growth, with US\$2.4 billion in new investments in the first five months of 2006, up by 19.7% from the 2004 level. The domestic private and foreign invested sectors currently produce almost 60% of industrial output and 33% of production value in manufacturing.

As noted, the SMEs in Viet Nam are contributing significantly to value-added, but most of these enterprises are still highly focused on the domestic market. The typical export-oriented enterprise in Viet Nam is larger and more productive.

A stronger involvement of the private sector in the supply chains could help SMEs identify overseas partners and improve quality standards. Strengthening CSR backwards through the supply chain is one strategy for promoting these linkages. Many Transnational Corporations (TNCs) have helped introduce CSR to the local enterprises in their supply chain by requiring compliance with a code of conduct or with local laws and regulations

³ Website: <http://www.wasmeinfo.org/statearungse3.htm>.

Under the SME development plan 2006-2010, the Vietnamese government has supported the development of new enterprises by simplifying procedures for company registration, taxation, import and export clearances, land renting policies, and establishing industrial zones. This policy has also facilitated the availability of credit loans to SMEs, capacity building, and information and technology.

Opportunities and Challenges in Viet Nam's Leather and Footwear Sector

As one of Viet Nam's leading export industries, the leather and footwear sector has attracted significant foreign investment and has been a stable supplier to customers around the world, particularly in developed economies. With Viet Nam's integration into the global economy, leather and footwear enterprises have had more opportunities to access advanced technologies and to penetrate the global market at a larger scale.

However, leather and footwear enterprises have also faced increased competition, not only internally but also from other regional manufacturers, mainly from China, who are supplying 75% of the total requirements for footwear of major global brand names like Nike, Adidas, and Reebok. To compete with these overseas companies, Viet Nam's enterprises have been forced to enhance their positions by increasing their capital, investing in modern technology, improving management practices and applying quality assurance. In particular, they have had to increase their direct interactions with potential overseas clients.

The Viet Nam government's policy is to support both domestic production and exports of leather products and footwear. The shoe industry is Viet Nam's second largest industrial employer, employing approximately 500,000 people. Demand for footwear products throughout the world and Viet Nam's footwear exports to the US market have also increased, especially after Viet Nam became a full member of WTO in 2006.

Despite these successes, however, Viet Nam's leather and footwear sector faces stiff competition from other regional suppliers, especially China. In addition, despite the reduction in tariffs Viet Nam producers still face (or potentially face) a variety of non-tariff barriers to trade including technical barriers, US monitoring mechanisms for garments, and anti-dumping provisions in the European Union. Finally the sector is facing increased pressure to strengthen its governance practices and transparency and improve its record on CSR.

At the enterprise level, the main difficulties are perceived as follows:

- limited expertise, management skills and technical competencies in majority of the enterprises;
- out-of-date production methods with a focus on sub-contractor performance,
- obsolete technology and equipment;
- insufficient availability of specialized skills on the production line, and a general shortage of skilled labour;
- poorly designed or styled products;
- poor quality domestic materials supply source, which fail to compete with imported materials; and
- low labour productivity levels, with high labour turnover.

Migrant labour, predominantly female, constitutes a large proportion of the workforce in the footwear industry. Workers lack job security and often quit when they are faced with difficulties related to their living conditions. Work is seasonal in nature, leading to the *ad hoc* labour arrangements. The work day may extend up to 10-12 hours during peak times, but workers may be idle during other times of the year or they may be forced to move to obtain seasonal employment.

Vietnamese enterprises are very much aware of the need to employ advanced technologies and modern production management methods, improve business ethics, enhance employees' benefit and maintain good client relationship with key clients as fundamental requirements for conducting business globally. Enterprises are upgrading infrastructure to meet requirements for environmental protection.

The presence of many TNCs in the footwear sector in Viet Nam has facilitated the development of strong linkages between local production companies and overseas customers, which has positively influenced the production processes, design, and quality standards, trade volumes as well as labour-management practices and working conditions throughout the supply chain. Eighty percent of Vietnamese footwear companies export their products, mainly to EU markets. They receive materials from overseas companies and add value through labour-intensive manufacturing and assembly operations. The resulting products are sold under global brands such as Nike and Adidas.

This outsourced production has resulted in stiff competition for traditional EU-based shoe producers while giving very limited bargaining power to local SME suppliers.⁴ In this environment, the initial efforts at strengthening CSR in the supply chain by the TNCs were generally in response to the demands of end consumers in overseas markets, and generally took the form of a code of conduct that was implemented. This required buyers to assess and certify local companies as having met global standards. As a result, enterprises had made "great efforts" to fulfill the buyer's requirement specified in the code of conduct.

BITIS, the subject of this case, stands out as an example of a Vietnamese enterprise that has adopted good CSR practices and has successfully carried out its operations in the global marketplace.

BITIS: "Tender Care of Viet's Feet"

The BINH TIEN Consumption Goods Production Company Limited is commonly known as BITIS, and also by its tag line "*Best solution of your sourcing in Viet Nam.*" Over its 25 years of operation, BITIS has become the most renowned company in Viet Nam's footwear sector for the quality of its human resources. Building customers' trust is the core of the company's business strategy.

The first production units of BITIS were set up in 1982, called *Bình Tiên & Vạn Thành*, with 20 workers and producing only rubber sandals. After the Doi Moi in 1986, these two production units were merged into a Binh Tien Production Collective to produce high quality sandals. The challenge was to upgrade the production capacity from the initial level of the collective, which was based on only 20 low-skilled workers. This led to Binh Tien Production Collective's decision to have one of its production units enter into a joint venture with a Chinese Taipei-based company.

⁴ LEFASO, 2006.

The joint venture, named Son Quan Joint Venture, was the first registered joint venture in the Viet Nam footwear sector in 1991. However, the whole company was still a Vietnamese controlled private company, under the leadership of Mr. Vuu Khai Thanh, registered as a limited company, BINH TIEN Consumption Goods Production Company Limited, when the first Vietnamese Enterprise law was issued in 1992. The business venture opened up opportunities in new markets and also helped the company to employ more workers, and to manage its work force in a modern way.

By 1989 or very early in Viet Nam's opening process, BITIS had become the first registered Vietnamese private company to produce goods for export. The company's trading activities started, strongly supported by its relationship with global partners. In 1990, the management decided to renovate its production technology and adopt global standards - a move which helped BITIS to integrate faster and make the BITIS trademark well-known outside Viet Nam.

BITIS attributed its success to the company's commitment to grow through market opportunities and the increasing role of the private sector.

The BITIS group encompasses three companies under a single brand, with a total labour force of over 7500. BITIS operates both in Viet Nam and as part of global supply chains. Within Viet Nam, the company has 11 branches (see Figure 1), two business centers and over 4,500 agents.

Figure 1:
BITIS Supply Map in Viet Nam



The company exports to more than 40 economies, including Japan and the United States. It has three representative offices in China, and two business centers in Central Highlands and in Lao Cai Border with total investment of US\$10 million. As of 2005, BITIS reported total turnover amounting to nearly 1,000 billion Dong (equivalent to US\$66 million), of which 30% was from exports (See **Table 2**).

Table 2:
BITIS Performance: 2001-2006

Particulars		2001	2002	2003	2004	2005	2006
1. Turnover (Dongs mil.)		465,742	559,060	695,616	726,082	836,354	828,057
2. Number of products (pairs)		10.588.961	13.068.306	14.788.186	15.179.308	16.031.713	17.843.160
3. Number of suppliers/retailers	Domestic	3007	3591	4179	4567	3448	3561
	Foreign	21	21	20	34	32	31
Average Income per employee(dongs/month)			856,371	853,829	846,892	867,465	

CSR at BITIS

BITIS actively contributes to community development and environmental protection. For example, BITIS has been honored for its work in supporting poor people and children with health examinations and social assistance. BITIS is not only committed to the production of high quality products but also to innovation in its human resources management. The company understands that improving working conditions and safety will redound to productivity improvements. The company also pays close attention to environmental sustainability and to the development and enhancement of its sustainable strategy and customers' trust.

In 2001 BITIS received the BVQI and QUACERT certificates for ISO 9001:2000. BITIS was honored for its products which have consistently been among the “Top Ten of Viet Nam” based on consumer votes, for the last eight years. BITIS is committed to integrate CSR into its overall management approach, particularly with regard to labour conditions and environment protection. BITIS intends to make CSR integration an important core competence of the company.

Employing about 7,500 workers in its various operations, BITIS views its people as key assets. The company has invested heavily in education and skills development through the setting up of a training institute. The company has also invested in improved working conditions for its employees believing that this will pay off in terms of employee enthusiasm and long term commitment. It has given priority to employee health and safety and has made significant investments to make the factory environment clean and comfortable as well as safe places of work, giving much attention to cleanliness, ventilation, noise levels and lighting. These investments have simultaneously supported improved productivity. For example, working places are well-maintained and kept clean, hygienic, and non-toxic. Workers are properly trained for health and safety protection, have scheduled rest time, and provided with nutritious meals.

Specific Strategies in Using CSR in Supply Chain to Achieve Competitive Advantage

BITIS supplies raw materials, packaging through sub-contractors and provides finished goods through distribution services and its wide spread retail sale chain. A key strategy for integrating CSR throughout the supply chain is continual innovation in production technology and retail distribution. The company sets quality, safety, and environmental standards for its partners and provides the technological inputs necessary that would enable its partners to meet those standards. The wage rates for suppliers' employees are also determined in labour contracts and are above the legal minimum rates.

Technology and Modern Management have Improved Working Conditions and Boosted Productivity

BITIS has focused on transforming itself from a product-oriented to a market-oriented company. It regularly provides training supportive of continual improvement, with an emphasis on the application of international standards to its production sites and those of its suppliers. Growing demand for its products in China has made the company highly responsive to technology changes such that 80% of its production is now automated. Through such automated technologies, BITIS has been able to meet consumer demands even from rural areas in China, supplying durable and high quality goods at low cost to these areas. To encourage innovation, the company introduced a campaign for employees entitled “promotion of talents and knowledge” and created financial incentives (both bonuses and base salary increases) to encourage technical staff to propose innovations in production technology and business promotion. BITIS investment in technology improvement has increased to 2,613 million Dongs in 2005 (equivalent to US\$175,000) from 326 million Dongs in 2002.

Consistent with its market orientation, BITIS has linked its production facilities closely to its retail marketing. BITIS imparts its knowledge of best practices to its key contract manufacturers in such areas as equipment formulation and processing, as well as repairs and maintenance. Retail distribution receives special emphasis particularly in regions adjacent to the Viet Nam-China border. In China, where BITIS has over 20 wholesale units and 350 retailers, the sales system has been tailored to fit the local context and consumer demand. A one-price policy is in effect in all markets. Market expansion focuses on rural and remote areas, but this encompasses a large and growing population

Human Resources Management and Development

The owner of BITIS, Mr. Vuu Khai Thanh, sees his employees as collaborators and shareholders in the company. Provision of good working conditions in a safe and healthy work place environment is a value that not only benefits the work force, but also generates a positive impact on productivity and on the quality of the products. Investing in human resources development is also a basic policy. Employees benefit from improved knowledge and skills and remain with the company longer.

A number of programs are in place to support workers’ long-term commitment to BITIS and to encourage continuing education and skills upgrading, including leadership, management and professional development, as well as quality, occupational health and safety and environmental standards. As mentioned earlier, the company has established a system of collective bargaining and a code of conduct. These complement a comprehensive compensation system, that includes base salary, incentive pay and allowances, for example, for housing and health care. Labour standards are set out in contracts with suppliers, including the legal minimum working age of 18 years in conformance to Vietnamese law.

CSR - Before and After the CSR Initiatives in the Supply Chain

BITIS has seen a number of tangible results from its investment in CSR through its supply chain, as follows:

- Improved image and enhanced consumer trust in the BITIS brand, resulting in growth in sales in both Vietnamese and overseas markets.
- Enhanced ability to design its own products to meet local market conditions, while assuring high quality standards.
- Better brand positioning in global markets, in particular the successful penetration of the China market in direct competition with local products.
- Gaining employee's loyalty in order to retain talent and assure labor stability.
- An increase in production capacity by 65% over five years, through the systematic application of new technology and improvements in management systems.

In summary, BITIS's good CSR practices include:

1. the respect of the enterprise for the basic rights of employees, supported by extensive training on product quality, a code of conduct based on respect for human rights, and providing decent working conditions,
2. the respect of the enterprise for the perspectives of consumers and buyers towards the products offered,
3. the commitment to investment in clean technology and waste treatment in order to protect the environment, and
4. the commitment to comply with the law, especially labour code obligations, and fair competition.

Conclusion

Globalization has created both opportunities and challenges to Viet Nam's social and economic development. Though faced with fierce and increasing competition, BITIS has been able to flourish in this dynamic environment through a commitment to product quality, customer focus, support for its employees, and respect for the environment. The BITIS brand is now well known and trusted, both in Viet Nam and overseas.

CSR is a core value of the business that has created a source of competitive advantage for the company. BITIS shows its commitment through continual improvement, management innovation and human resource development. BITIS strives for the adoption of good CSR practices throughout its supply chain, from its suppliers to its retail distributors. The key to sustaining the company's growth is maintaining the trust and commitment of employees and other stakeholders, understanding its markets, and supporting the communities in which it operates.

