Socially Inclusive Economic Growth Through Innovative Governance

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Introduction

The OECD defines socially inclusive growth as "economic growth that creates opportunity for all segments of the population and distributes the dividends of increased prosperity, both in monetary and non-monetary terms, fairly across society" ("OECD Policy Shaping and Policy Making: The Governance of Inclusive Growth", accessed July 8, 2016. https://www.oecd.org/governance/ministerial/the-governance-of-inclusive-growth.pdf). For the purposes of this paper, socially inclusive growth is being defined as the *creation* of opportunities for economic advancement that are accessible to all components of society regardless of their economic status, social class, race, ethnicity or gender. While this term can be applied to developed countries, the focus here will be on developing countries. It should be noted as well that 'creation of opportunities' does not mean that economic advancement is guaranteed, as what an individual or group does with those opportunities will in large part determine the extent to which economic advancement occurs. But, at the same time, 'accessible to all components of society' implies that those who want to create opportunities for economic advancement should not have to face any barriers. Barriers, however, do exist, and can take the form of low socio-economic status, limited education, unequal access to education, limited access to capital or financing, inadequate or unsupportive institutions and government policies. Socially inclusive economic growth, therefore, cannot happen unless these barriers are eliminated or, at minimum, greatly reduced.

The removal of barriers to economic growth largely is a public governance issue, and the policies oriented toward economic development that arise from public governance is influenced by the philosophic approach to economic government chosen by public governance. In the late 20th century, with the collapse of the Soviet Union and the beginning of the Chinese 'experiment' with capitalism, a broadly defined 'consensus' has emerged in favor of at least some form of a market economy as the key to economic development. This, then, means that the governance philosophy needs to change to one that supports a market economy. A market economy works best when it is open to all, transparent, fair, accountable and operates under a set of well-defined and shared rules. Therefore, governance should be participatory, accountable, fair and open. That this looks a bit like democracy is no accident, for much of what makes a democracy 'work' also is what makes a market economy 'work'.

Economic growth and socially inclusive economic growth, though, are not the same. The former focuses on *national* economic growth, while the latter is concerned with how widely dispersed economic development has been within a country. Still, though, the achievement of socially inclusive economic growth, an important part of the sustainable development goals, also will depend on a supportive governance structure.

So, is just finding the right governance structure conducive to socially inclusive economic growth enough to ensure that it will occur? No, for governance is executed through institutions, and if those institutions are weak or non-existent, all forms of economic development are in jeopardy. Not present and/or weak institutions creates what is called an institutional void (see Douglas North, "The new institutional economics and third world development," in J. Harris, J. Huner and C. Lewis (Eds), *The New Institutional Economics and Third World Development,* ed. J. Harris, J. Huner and C. Lewis (London, UK: Routledge, 1995), 17.)How those institutional voids are filled will go a long way in determining how successful any effort to create inclusive economic growth will be. And this is where the MNE can come in. There is an increasing body of literature describing how MNEs operate in institutional voids (see, for example, the 2009 *Journal of World Business* issue devoted to multinational enterprises and economic development). While some of the actions by MNEs are taking advantage of institutional voids for their own benefit, thanks to the influence of corporate social responsibility (CSR) practices, many MNEs are in the position to assist in economic development in the way a country's institutions are not. In other words, they have the ability to support socially inclusive economic growth. How much they do that, though, is affected by the MNEs' own governance mechanisms. As will be discussed further below, MNE governance looks inward (in concert with its own self-interest) rather than outward (to promote socially inclusive economic growth, so the innovation in governance referred to in the title of this paper begins at the level of the MNE.

The rest of the paper will proceed as follows. The next section will discuss in more detail the link between governance and growth and describe the governance structures that are believed to support socially inclusive economic growth. That will be followed by a review of what some select MNEs are saying they are doing to promote socially inclusive economic growth, based on their CSR or sustainability reports. After that will be a discussion of what common themes emerge from these reports. And, finally, a new approach to governance will be suggested.

Growth and Governance

First, let us start with the assumption that some form of market economy provides the best environment for economic growth, and that a good working definition of a market economy is one in which decisions about investment, production and distribution are influenced by competition, the laws of supply and demand and a free price system. The private sector, of course, is a key part of a market economy.

A market economy in which the private sector plays a key role thus needs to: encourage participation in it (have many players); welcome competition; be responsive to factors of supply and demand as determined by an informed set of customers and suppliers; be accountable to its customers and suppliers; and be transparent in its actions. It also needs to be governed to prevent what economists would call market failure, or the inability of a market to function in a competitive, participatory, accountable and transparent way. In other words, the market needs rules to which all actors adhere and which prescribe the environment in which competition, open participation, accountability and transparency are assured.

The rules under which a market economy functions are set by government. Because competition, participation, accountability and transparency also are traits of a democracy, organizations such as the Center for International Private Enterprise, a strong supporter of the link between the private sector, democratic ideas and market economies, stress the need for a symbiotic relationship between a market economies and democracies. Underpinning this symbiotic relationship is good governance, which "sustains both responsible, productive market behavior and effective, legitimate democracies." ("The CIPE Guide to Governance Reform: Strategic Planning for Emerging Markets", Kim Bettcher, ed., CIPE 2009, 8) Note that what the link between market economies and democracies is 'good governance', particularly good *public* governance. But what constitutes 'good public governance'?

CIPE (The CIPE Guide, 7) characterizes good governance as being "responsive, effective, and accountable to the people [and centering] on high-quality decision-making in a participatory policy process". The key word here is 'participatory', as those who are affected by governance should be the ones to participate in it. To link this back to socially inclusive economic growth, then, if the goal is to have socially inclusive economic growth, governance should be inclusive as well.

The OECD, in its 2016 document 'Policy Shaping and Policy Making: The Governance of Inclusive Growth' described the importance of governance for inclusiveness as follows:

"Governance also matters for inclusiveness. Inclusive institutions ….. allow for broad citizen participation, pluralism and an effective system of checks and balances, leading to better access to services and opportunity." [1]("Policy Shaping and Policy Making: The Governance of Inclusive Growth 2016, OECD, accessed July 8, 2016, https://www.oecd.org/governance/ministerial/the-governance-of-inclusive-growth.pdf) Building inclusive institutions involves stakeholder engagement, as it is through engagement that the stakeholders develop a sense of ownership over policy choices and helps enable control over the decision making process, strengthens accountability due to the wider array of entities involved, and gives a voice to all. (Policy Shaping and Policy Making)

To ensure that stakeholder engagement is achieved, several actions are recommended. These actions involve using existing legal frameworks, clearly identifying the objectives, goals and scope of stakeholder engagement, reaching out to any and all groups that could be considered stakeholders, using a wide array of tools to reach out to those stakeholders, keeping information flowing through feedback loops, evaluating the process in a systematic way, avoiding a 'one size fits all mentality', and embedding the values of open engagement in all levels of public administration. (Policy Shaping and Policy Making)

The focus of the above discussion of good governance has been on public governance. The public sector, as has been stated above, is not the only sector involved with either economic development or socially inclusive economic growth. The private sector (for this paper, the MNE) also is involved, so a discussion about corporate governance needs is in order.

The OECD's 2015 G20/OECD Principles of Corporate Governance noted that "Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders [and] provides the structure through which the objectives of the company are set and the means of attaining those objectives and monitoring performance are determined." ("G20/OECD Principles of Corporate Governance OECD Report to G20 Finance Ministers and Central Bank Governors", Organization for Economic Cooperation and Development OECD, September 2015). Of the six principles, most refer to company governance or governance matters related to shareholders, but one, the fourth, says that the

[1] Note the similarities to CIPE in the use of the terms competition and participation.

corporate governance framework should “recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.” (G20/OECD Principles 37)

Those stakeholders, however, consist mostly of labor and those parties with whom the company has a legal arrangement, such as suppliers, customers and unspecified ‘others’. When no such legal arrangement exists (stakeholder interests are not legislated), but the company does have commitments with stakeholders, all that is said is “concern over corporate reputation and corporate performance often requires the recognition of broader interests” (OECD 2015, p 37). These kinds of commitments most often are found in developing countries in which governance structures and the institutions that support them (and through which governance is executed) are weak. Thus, in the presence of governance and institutional voids, what a company decides to do in terms of honoring its commitments in a developing country falls to its approach to or philosophy of corporate social responsibility.

Remember that it is being more widely accepted that the private sector must be play a larger role in both economic development (see, for example, Andris Piebalgs, “*Working with the Private Sector for a Stronger Link between Growth and Poverty Alleviation”*, *Great Insights 3*, no. 6, 2014, as well as Rilana Riikinen and Asta Salmi, “What Makes MNCs Sustainable? - Institutional Pressures as Drivers of Operational Sustainability”, (paper presented at the annual meeting of the Academy of International Business, New Orleans, Louisiana, June 27 – 30, 2016). James Michel, in *Beyond Aid: The Integration of Sustainable Development in a Coherent International Agenda*, noted that:

> “More than all other non-state actors, the private sector will drive the pursuit of inclusive and sustainable economic growth and job creation and the transition to sustainable patterns of production and consumption. That rationale implies a central role for the private sector.” (James Michel, *Beyond Aid: The Integration of Sustainable Development in a Coherent International Agenda.* (Lanham: Rowan & Littlefield 2016), 31.

For the private sector (MNEs) to drive the pursuit of inclusive economic growth, it is reasonable to assume that it will need a governance structure that supports that objective. In the context of the OECD governance principles, that would mean that principle 4 would need to more explicitly state just who the stakeholders are, where they are, what kind of cooperation is needed between the private sector and stakeholders, and how that cooperation will generate economic opportunities for stakeholders.

Even though many MNEs have altered their approach to corporate governance to include CSR and the support of CSR activities, the jury is still out about just how much MNEs are purposely doing to support socially inclusive economic growth through its governance (or, for that matter, its CSR activities). It is in fact easy to criticize an MNE’s CSR activities as being just window dressing or ‘green washing’ to make itself look good in the eyes of the public or its shareholders. The proof, as the saying goes, is in the pudding, so we should now take a look at what some MNEs are saying they are doing about socially inclusive growth.

MNEs and Socially Inclusive Growth

Of all the ways in which an MNE can assist socially inclusive economic growth, perhaps the most direct one is through its supply chain. As MNEs have globalized, many have shifted the sourcing of their goods and services out of their home countries to places where the goods and services can be acquired more cheaply – developing countries. By looking at what MNEs are saying they are doing in their developing country-located supply chains, we can get a sense for their attitudes toward socially inclusive economic growth.

One place to look is a company's CSR and/or sustainability report. In this paper, the CSR and sustainability reports of large food MNEs are used because food MNEs frequently use developing countries as sources for goods in their supply chains. The food MNEs described below represent some of the largest, in terms of sales, food MNEs as identified by Food & Engineering Magazine. This list includes (in alphabetical order):

1. Archer Daniels Midland
2. Cargill
3. Danone
4. JBS
5. Mars
6. Mondelez International
7. Nestle

The CSR and sustainability reports for each company were searched using such keywords as 'local', 'local development', and 'supply chain'.

Review of Company Approaches to Local Development

A few common elements emerged from what these companies are saying about local development and/or their supply chains. First, they all seem serious about the concept of supporting local development. Second, they all are concerned about human rights issues, both within their companies and in the communities with which they have contact. Third, they pay close attention to what happens in their supply chains, not just in terms of reducing costs or maintaining quality for their own benefit, but also in terms of what occurs at the local level. Fourth, most have an explicit code of conduct with which employees and suppliers are expected to comply. Fifth, there is a general consensus in support of 'responsible sourcing', with the most detailed and comprehensive being applied to palm oil, coffee and cocoa.

Local Development

The following are excerpts of what a company said about local development.

Archer Daniels Midland strives to make "a positive difference in the communities where [it] lives and works." (Archer Daniel Midland 2015 Corporate Responsibility Report, 35)

Cargill "works ….. to reverse deforestation trends and promote crop diversification, helping to build a more sustainable rural economy." (Cargill 2015 Annual Report, 4)

Danone has been active in "creating jobs and enhancing the economic activity of over 32,000 people, and benefiting 3 million people in local communities." (Danone 2015 Economic and Social Responsibility Report, 71)

JBS is "committed to contributing to social, economic and environmental development". (JBS 2015 Annual and Sustainability Report, 82)

Mars is committed to “drive down the environmental impact of our priority raw materials, respect the human rights of everyone in our upstream supply chain and help to lift farmers out of poverty.” (Mars 2015 Global Sustainability Report, 1)

Mondelez International says that “… all our farmers should benefit from more sustainable practices”, and it has “been working with civil society, government and industry to tackle conditions at the farm level.” (Mondelez International 2015 Well-Being and Sustainable Resource Report, 1)

Nestle provides support that will allow “farmers to pursue their livelihoods by choice, and strengthens the communities in which they live.” (Nestle 2015 Corporate Social Responsibility Report, 91)

Human Rights

All companies have something to say about human rights and/or respecting human rights within the company itself, throughout its supply chain, and in connection with its stakeholders. The most frequently stated human rights refer to child labor and human trafficking, but issues such as gender equity, women’s rights, and educational rights are also frequently cited.

Supply Chains

The importance of supply chains in each company cannot be understated, as they are of vital importance to the companies’ abilities to provide quality goods and services. Supply chains are mentioned in both CSR and sustainability reports; the former because care for and/or concern about what happens in the supply chain is good for a company’s image, and the latter because sustaining long term access to what’s in the supply chain is crucial to the company’s own sustainability. As a result, concern for being able to sustain the supply chain at the local level also becomes crucial. Let us revisit what the companies said about the supply chain.

Archer Daniels Midland –“We …. work closely with customers and industry stakeholders to help develop a more sustainable supply chain for palm oil, palm kernel oil and their derivatives.” (Corporate Social Responsibility Report, Appendix I, ii)

Cargill - “For more than 10 years, Cargill has been working to reduce deforestation and improve the sustainability of the palm oil industry. Now we are working to ensure that all palm oil and palm products we produce, trade or process honor the sustainable palm oil policy we issued in July 2014: no deforestation of high carbon stock (HCS) or high conservation value (HCV) land; no planting on peat, regardless of depth; and respect for rights of local and indigenous people.” (Annual Report, 2)

Danone – “For a food company, securing adequate, long-term supplies of safe, high-quality raw materials is a critical problem, and we’re solving it through new ways of working with our suppliers and with local communities whose future depends on preserving these resources.” (Economic and Social Responsibility Report, 61 – 62)

JBS – “With ongoing participation in the discussions of the sectors in which it operates, the Company has maintained a strong local and global influence, contributing to the proposal of new agendas, focused on sustainable production and the improvement of social and environmental governance in the global food industry.” (Annual and Sustainability Report, 57)

Mars – “Many of our raw materials, including cocoa, coffee, and tea, are grown by smallholder farmers. Because of the small size of their holdings, they’re particularly vulnerable to climate change impacts, water stress, soil degradation and plant diseases. Poor training and lack of access to markets and technologies also result in lower yields and lower incomes. We work with experts and community groups to improve farmers’ resilience and livelihoods, and also to help secure a sustainable and high-quality supply of raw materials for the future.” (Global Sustainability Report, 2)

Mondelez International – “We work with thousands of suppliers, consultants and business partners around the world. Of course, we cannot — and do not presume to — control how they run their businesses. But we certainly take pragmatic steps to align what they do for us with our own standards of fair and honest dealings.” (Well-Being and Sustainable Resource Report, 1)

Nestle - “To produce our foods and beverages we rely on secure, long-term supplies of raw materials from millions of farmers worldwide. The farmers and their many workers are critical to our success. By understanding and managing where and how our ingredients are produced, we can promote better agricultural practices, support rural development in line with local priorities, and address supply chain issues from gender inequality to deforestation.” (Corporate Social Responsibility Report, 90)

Codes of Conduct

Not all 7 companies have an explicit ‘code of conduct’ that is applied internally and externally, although all are concerned about their own behavior and that of others. For example, Nestle ascribes to codes of conduct applicable to cocoa and coffee production, and palm oil. For those that have identified a specific code of conduct – Archer Daniels Midland, JBS, Mars and Mondelez International – the following represent what they have in common.

1. Obeying all applicable laws and regulations.
2. Engaging in ethical business practices.
3. Treating employees and the people with whom they do business with dignity and respect.
4. Engaging in fair labor practices (especially with respect to child and forced labor).
5. Being concerned with health and safety (in the workplace and in their products).
6. Respecting/protecting the environment.

The way the companies implement their codes of conduct differs, particularly with the components of their supply chains, but it is worth noting that Mars, Mondelez and Nestle are much more explicit in what they expect from their supply chains than the others.

Responsible Sourcing

Responsible sourcing essentially is related to managing the supply chain and acting within the company’s code of conduct. But it also is related to local development, as the onus to source responsible is at the local level, as are the consequences for not sourcing responsibly. Some selected views on responsible sourcing from the 7 companies are as follows.

Archer Daniels Midland – see above comment vis-à-vis supply chains.

Mars – “Sustainable sourcing is Mars’ commitment to drive down the environmental impact of our priority raw materials, respect the human rights of everyone in our upstream supply chain and help to lift farmers out of poverty. This will be defined through our five impacts: greenhouse gas, water, land, human rights and income and priority raw material sourcing commitments. Responsible sourcing is a fundamental part of this commitment where we work with our direct suppliers as they seek to respect rights in their workplaces, in alignment with our Supplier Code of Conduct.” (Corporate Responsibility Report, 1)

Mondelez International – see above comment vis-à-vis supply chains

Nestle – “There are many challenges (to responsible sourcing). For example, many of our supply chains are complex, both geographically and in terms of language, so initiatives and materials must be tailored to meet local needs. We’ve made steady progress, by encouraging the adoption of internationally recognized ethical practices.” (Corporate Social Responsibility Report,105)

Implications at the Local Level

Each of the common themes noted above has an implication at the local level, for the burden of implementing programs to support local development, respect human rights, supply goods and services, adhere to a code of conduct, and source responsibly falls to those at the local level. Make no mistake, the pronouncements of a willingness and/or desire to make local lives better through economic advancement notwithstanding, the actions these companies take with respect to CSR and sustainability are first and foremost in their own best interests. And, given that at heart the relationships these companies have with local groups take the form of business transactions, they are tenuous; if the business relationship falters, or if a better business relationship can be found elsewhere, there is nothing preventing the company from moving on. So, realistically speaking, local communities are at the mercy of the MNCs with which they engage and on which they depend for their livelihoods.

Many of the companies talk about ‘supplying resources’ to, ‘providing training’ for, ‘giving tools’ to, ‘consulting’ with, or ‘engaging’ with local communities to help them solve environmental problems, apply acceptable labor practices (e.g., no child labor), behave in accordance with codes of conduct or meet supply requirements in a responsible way, but these are done with a top-down approach and in line with their own best interests. This attitude is expressed best by what Mondelez International said about responsible sourcing – that it does not presume to control how the various entities with which it does business around the world ‘conduct their businesses’, but “we certainly take pragmatic steps to align what they do for us with our own standards of fair and honest dealings.” (Well-Being and Sustainable Resource Report, 2) Interestingly, Mondelez International is the only company that includes in its code of conduct a provision for its suppliers to give the company their complete business loyalty.

A Word About Governance

The search through the CSR and sustainability reports of the 7 food companies noted in this paper did not include the word ‘governance’, but one can be rest assured that governance structures in each of the companies are in place to assure that it adheres to its code of conduct (and makes sure its pertinent stakeholders to so, too), manages its supply chain well and sources responsibly. This governance structure, though, is inward looking, and while many of the companies belong to supranational organizations such as the Sustainable Agriculture Initiative, the Roundtable on Sustainable Palm Oil, or those associated with cocoa and coffee production, those groups only have an indirect and non-binding impact on how the companies govern themselves.

Let us take another look at Mondelez International's that it does not presume to control how its suppliers conduct their business. While this may be consistent with an arm's length business transaction – and 'proper' in the sense that one company is not telling another company what to do – it ignores the imbalance of power and influence that exists between a large international food company and a local supplier in a developing country.

It might be a different story if the business, political and regulatory institutions that support the environment in which the local companies in developing countries operate are well-developed, efficient, effective and on the same page with respect to environmental concerns and business behavior as are the MNEs. In that case, the local suppliers could be presumed to already be operating in a way consistent with the way the MNEs would like them to behave (e.g., consistent with what is in their CSR and sustainability reports). But those institutions often are not well developed, efficient or effective. Institutional voids, as was noted above, are prevalent in developing countries. And, as also noted above, MNEs often fill those institutional voids. So, if the MNE is filling an institutional void and providing an institutional structure in which a local company operates, it by default also is providing a governance structure to which the local company has to adhere. It is, however, a governance structure in which the local company (and, by extension, the local community) has no voice.

The Need for Something Different

This paper is about what is needed to secure socially inclusive economic growth in developing countries. It has pointed out how a lack of supportive institutions in developing countries has made it difficult for them to support the kind of local efforts needed to ensure socially inclusive economic growth. It also has pointed out how the private sector – and in particular MNEs – are the critical engines of growth at the local level due in large part to a combination of their own economic power and resources and the institutional voids found in developing countries. Focusing on large food MNEs, the paper has shown that these MNEs mention local development and what they can do to support it, but that their efforts with respect to local development are guided by what it can do for them, not by what it can do for the local community.

Socially inclusive economic growth requires inclusive governance, and inclusive governance requires giving local communities a voice in the governance of the MNEs on which they rely on economic development. Governance has to become truly collaborative; all stakeholders, no matter how small, have to be represented and have to become part of the decision making process. It is this innovation in governance that will help secure socially inclusive economic growth.

How will this collaborative governance work? First, of course, is that the MNE has to officially allow representatives from local communities a place in its governance structure. Second, each local community will need to determine who those representatives are, and if they are the same for all the different MNEs that are present at the local level or are different. While this representation perhaps should come from the parties most affected by MNE decisions (e.g. a local supplier), keep in mind that it is not just the local supplier who will be affected; it is the *communities* interests that are to be served. Third, decisions have to be made about how much weight each member in this new governance structure has. Fourth, *everyone* in the governance structure has to commit and agree to a totally transparent process in which *all* parties are kept informed about how governance decisions are made. And fifth, *everyone* in the governance structure must be willing to compromise and accept that the ultimate decision came was collaborative. This implies that all parties will not get everything they wanted, but, also, that they will get something of what they wanted.

This kind of inclusive governance also, in a sense, is interconnected governance. The local representative will be cognizant of how the relationship with the MNE filters throughout the community. The MNE will discover how its relationship with a local supplier extends beyond just the supplier into the broader community. By having local representatives from *all* the communities involved, the MNE can better see how its decisions connect across those communities. And at the same time, all those communities can see how their individual interests are connected.

Implementing this innovation will not be easy, but it is not impossible. Possible models for it could be found in the Extractive Industries Transparency Initiative and how that is influencing governance at MNE and local levels (see Rich and Mossberg, 2015). And lessons could be learned from other MNEs. For example, Tetra Pak, the Swedish food packaging and processing MNE, seems to be practicing its own kind of inclusive governance by including local management and networks in its governance framework (see TetraPak's 2015 Sustainability Report, 15). Novo Nordisk, the Danish pharmaceutical MNE, stresses the role of partnerships in it governance and decision making processes (see Novo Nordisk's 2015 Sustainability Report). Researching more into what actually goes on inside the governance of MNEs such as those used in this study may also reveal that some form of inclusive governance is being practiced and can be leveraged to make it more widespread. The opportunity to create socially inclusive economic growth through this innovative, inclusive and interconnected form of governance, though, is well worth the effort needed to achieve it.

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