2 Sourcing. How to Supply Right

In most general terms, "sourcing" is about supplying resources efficiently, from some source. Its focus is the rational management of the upstream value chain – the "supply chain". In this unit, we will view this field of management from an ethical perspective, in the context of a globalized economy. Sourcing in this context concerns the global supply of raw materials and commodities, upstream products, but also of ready-made products and services *typically* by order of some entity situated in the "global centre", while the supply chain spans to countries of the "global periphery".

"Sourcing" is about supplying resources efficiently, by way of a rational management of the value chain.

The *economic reasons* for global sourcing – taking advantage from lower standards, meaning lower costs of production – are *the very reason for ethical reflection*: "Ethical sourcing", seen this way, is about managing the *tension that arises between claims for efficiency and legitimacy*, if *cost-cutting for profits goes at the cost of people and planet*. Starting from this general proposition, we will discuss

"Ethical sourcing" addresses the issue when cost-cutting for profits goes at the cost of people and planet.

- *promises and problems of a globalized economy*: Does "free trade" deliver on freedom and utility, and what about human rights? This part sketches the macro-economic context, the history and impact of globalization.
- *the ethical challenges hidden in the supply chain*: How far does a firm's "social responsibility" extend along the value chain, and how can it be managed? This part deals with reasons and instruments to care for social and ecological conditions throughout the supply chain.

What this unit does not focus on is the general issue of "fair treatment" of one's suppliers. That's an issue that's equally relevant in a local context – even though it is likely related to the fact that companies increasingly *do think global/ly*, increasing thus the pressure on local suppliers as well. Consumers, at the same time, are increasingly opting to *act local/ly*, longing for "regional products" – we will, however, also *not* focus on challenges to re-localize one's supply chain in this unit.

We will focus on global issues and challenges. Indeed, the economic and ethical issues of globalization are so far-reaching in terms of history and geography that most such local issues can only be understood in this context. What's more, the very process of globalization that's been updated and rebooted, as it were, more than three decades ago, and specifically the *critique* of globalization and corporate *irresponsibility* in its wake, actually sparked and continue to dominate today's debates on corporate social responsibility and sustainable development.

Problems and promises of globalization

The focus of ethical sourcing is usually on that unit that organizes production and sells the product in its name – and on what happens upstream.

As the term "supply chain management" suggests, global supply is usually envisioned in the form of a "chain". This model image of a chain indicates some sort of process, reaching from the digging and growing of resources and raw materials at the very beginning, through primary and intermediate products up to the final product. What's commonly called the "producer" is then usually that entity which designed, ordered and/or organized the production and sells the product in its own name. In consumer goods, it's usually the "brand" that becomes visible on the market – and the rest of the chain is usually hidden from sight of consumers.

Exactly this is the issue that's at stake when we talk about "ethical sourcing" or "ethical supply chain management": What responsibility does this entity (firm) have for the production? How far back does this responsibility reach? Why should the company care? And what can it do about it? Before we turn to these questions, let's first sketch the problem in its macro-economic and historical context: the globalized world in which we find ourselves today.

The notions "global centre" and "global periphery" used throughout this chapter do not *per se* carry any ethnocentric meaning. They are supposed to convey an understanding of globalization as an intended, interest-driven process that's characterized by relationships of dominance and dependency. The notions are roughly synonymous with such labels as the global "North" and "South", "developed" and "developing" countries, or – according to a popular scheme introduced by French demographer and historian Alfred Sauvy in 1952 – the "First" and "Third World": The erstwhile "Second World" that more or less submerged with the fall of the former "Eastern bloc" today usually shares the status of “threshold countries” with so-called "newly industrialized countries" (NIC), "emerging markets" such as Brazil, India, China and South Africa – together with Russia, these countries make up the so-called “BRICs states”. These countries have become new, rising centres of global trade and economic power, setting the stage for a completely new, multi-polar world order that will likely mark much of the 21st century. At the same time, there still remain dramatic differences in economic development between centre and periphery *within* these countries and regions. Within the European Union or the US, at the same time, we can observe such differences to re-emerge in the post-2008 crisis. Even though the situation is obviously somewhat fuzzy and in constant development, however, the conventional labels still have some heuristic value.

Today's economic globalization was facilitated by technological inventions, turning the world into a “global village” – yet at the same time it was necessitated by a deep economic crisis of the post-War, Fordist model of democratic capitalism.

When we talk about globalization in this context, we refer to *economic* globalization – even if it is indeed embedded in a broader process of the *globalization of the world*. The current economic globalization is defined by one central aspect: *the transformation and relocation of production processes around the globe*. This enormously complex and far-reaching process was made possible by new technologies – such as the internet, but also by cheap transportation and improved logistics. But it was actually caused (if not necessitated) by a change of the dominant model of accumulation, ending the long post-War era of constant growth, low unemployment and inflation, production for national markets and relatively balanced trade. This *crisis of accumulation*, which made itself felt throughout the 1970s, meant a radical shift in economic policy, starting in the US and the UK, based on watchwords such as *free trade, unfettered investment, deregulation, balanced budgets, low inflation and privatization* – this is what's been called the "six-step plan to national prosperity" by some, the "neo-liberal shock doctrine" by others.

Indeed, before we get back to look at the causes a little more closely, it should suffice to sum up that the ultimate motive of globalization has been an economic one: *buy low and sell high on the global marketplace*. Economic globalization – even if not in such unvarnished terms – is quite certainly not a new thing. And it is certainly also not new that it always implied the enrichment of the centre at the cost of the periphery.

Globalization is not new – what's new is the scope, the speed, the system and the sheer scale of economic exploitation that goes with it.

The "long 16th century" – Colonialism and Mercantilism: Racism, God and Glory

Peaceful trade among different regions and peoples of the world – with the participation of Europe – had existed for a long time in the history of mankind: albeit often sporadically, on a small scale and limited to luxury goods with high value per unit. Warfare, forced occupation and the exploitation of land and people had been around for an equally long time.

However, measured by its geographical scope and long-reaching effects, globalization and the model of accumulation linked with it actually started no more than 500 years ago – with the European "discovery" of the world. Various European empires – the Spanish and Portuguese, the Dutch, French, also Italians and Germans, and above all the English – started to occupy and divide up among them great parts of the non-European world, well up until the 20th century.

The first wave of globalization was based on a crude exploitation of European colonies, its value chain paradigm being the so-called “triangular trade”.

"Colonies" were actually conceived as extra-territorial extensions of the homeland. They were supposed first and foremost to increase the wealth and glory of the "empire", meaning first of all the imperial family. To this end, so-called "companies" had been founded end endowed with monopolies of force and trade, notably the Dutch and English *East-India Companies*, or the English *Royal African Company* that – similar to Portuguese, French, Dutch, German, Belgian and German companies – had been heavily involved in the slave trade up until the 18th century. The paradigm for this proto-capitalist, imperialist form of globalization – its typical "value chain" – was the so-called "trade triangle" or "triangular trade" (more specifically "Atlantic triangular Slave trade").

The Atlantic Triangular Slave Trade How it worked in its peculiar, efficient ways may be illustrated by an ideal example: A ship left its European harbour in late fall, loaded with weapons, it stocked up on slaves on a West-African slave market in early winter, followed the so-called "trade winds" to the American colonies, traded the slaves for cotton, sugar cane, tobacco etc. in spring (harvest time in the Southern hemisphere) and returned home with this load, following the Gulf Stream, in early summer. At every stage of this trade, the company could not only follow good winds and currents, but also make a lot of money.

European glory and economic growth was, for one, dearly paid for by African slaves, who lost their homes, their freedom and their lives: At least 12 mio. people from sub-Saharan Africa were enslaved between the 15th and 19th centuries, of which 10-20% died during the Middle Passage – more soon upon their arrival, many more in the slave raids in Africa, amounting to a death toll of roughly 10 million people (Ransom 2001).

The price of these ventures for the glory and enrichment of European empires was dearly paid by the people that were being enslaved, exploited and often worked to death in the colonies.

It was also paid by a heavy loss of life on the part of the south American native population – due to imported diseases, but also to slave labour: In the silver mines of Bolivian Potosí alone, by 1650, 8 mio. native Indios had died, labouring for the Spanish *conquistadores*. The death toll of European occupation was so heavy (about 90% by the late 1700s) that the number of indigenous people in Latin America today is likely no bigger than it was in 1492 (Braudel 1979 : 35f, *Wikipedia* >> *Population history of indigenous peoples of the Americas*).

As an ethical legitimation for slave labour and the deadly exploitation of heathens, Europeans could resort to racist theories that saw "negroids" as a subhuman race – a "theory" that was supposed to get late scientific backing by the 19th century "Hametic hypothesis" which reduced the sub-Saharan, black population of Africa to the status of animal-like barbarians without culture.

The economic theory that (later) justified colonial warfare and exploitation was mercantilism: It saw "trade" of this kind as being the source of a nation's wealth, usually measured by the amount of precious metals in the emperor's chest.

The "economic" legitimation of imperialist trade surplus, monopolies and high tariffs – in the often forceful confrontation with other colonial powers – was delivered by so-called "mercantilist" economics and its crude form of "bullionism", which defined the wealth of a nation by the amount of gold and silver it (viz. its emperor) owned. Indeed, it can be said that the plundering of the Americas (and Africa) from the 16th century onwards actually financed Europe's economic development and "industrial revolution" – for the great economist John Maynard Keynes, this was the start capital for capitalist accumulation based on compound interest: "From that time until to-day the power of accumulation by compound interest ... was re-born and renewed its strength." (Keynes 1972 : 324)

Maybe early libertines of that day had had a vague inkling of the origins of European wealth that inspired them to the proto-utilitarian "paradigm shift" of European bourgeois ethics: claiming that order, freedom, welfare and, not least, cultural bloom (such as the Dutch 17th century "Golden Age") were indeed not the fruit of sympathy, philanthropy or honest labour, but of greed and the consequent assertion of one's own material interests. The Dutch emigrant to England, Bernard Mandeville, very frankly and in his times – in 1716 – offensively put this discovery into a nutshell: "The worst of all the multitude / did something for the common good." (Mandeville 1957 : 24) In its crude form, the self-conscious (and likely also somewhat remorseful) commitment to the naturalness and utility of greed can already be found with the humanists of the early capitalist centres of northern Italy (Proulx Lang 1973) – if only it served the common good, the *multitude*.

The 19th century – Capitalism and Liberalism: Freedom, free markets and free trade

Economic liberalism is based on a broader, anti-imperialist concept of national welfare: the rational organization of free labour (and the protection of private property derived thereof) was supposed to be the actual source of the wealth of nations.

Such proto-utilitarian ideas – focusing less on the emperor's treasure than on welfare of the masses (at least in the homelands) – set the stage for the economic and political revolutions to come. Central to this – besides "utility" – was the claim for "freedom": According to liberal Enlightenment thinkers such as John Locke, men (and women) had a "natural right" to freedom and private property: to act and interact freely, according to "God-given" reason, and make use of one's labour and everything that comes of it (cf. chapter 1).

The right to enter voluntary economic transactions and to dispose of one's private property are thus derived from claims to human freedom and sovereignty. Yet, political liberalism – as opposed to libertarianism and hard-core economic liberalism – also rested on the confession that the "state of nature", in which absolute freedom, based on a reasoned intuition of the "laws of nature", was possible, was also highly perilous and unsafe. These liberals' view was certainly much more optimistic than Thomas Hobbes' erstwhile conviction that – in a state of nature – "man was man's wolf" (*homo homini lupus*). Yet, it also required some sort of *republican self-limitation* of personal liberty – in exchange for the duty of this enlightened *Leviathan* (that's how Hobbes had called the entity to which everybody trusts her liberties in exchange for protection) to protect, within such limits, the natural rights of the person: her freedom and private property.

Mercantilism, with its protectionist, imperialistic economy based on the exploitation of foreign lands and peoples, however, did not come under criticism for reasons of freedom, rights or the welfare of the colonies and slave labourers it needed. It was the *freedom, rights and welfare of the homelands* that was at stake. Mercantilism, therefore, was mainly criticized as a theory that justified the illegitimate and inefficient enrichment of a privileged class. What its critics tried to promote instead was the *Wealth of Nations* – as already spelled out quite prominently in the very title of Adam Smith's seminal economic work which laid the groundwork for classical liberal economics (Smith 2008).

Liberalism opposed the imperialist economics of mercantilism in the name of consumer sovereignty, self-regulating markets and free trade – for the benefit of everybody (except the colonies).

Against far-reaching protection, powers and privileges for producers, Smith argued the merits of consumer sovereignty. As bearers of the "general interest" it was the consumers, not the producers, whose free choice not only constituted a right, but it also promised a truly efficient allocation of resources, to the benefit of all (cf. chapter 3).

Against regulation of markets, Smith argued that competition – by checking and balancing individual interests – would eventually transform the egoistic impulses of economic men in such a way that they would promote the general welfare. That's what Smith referred to as the workings of an "invisible hand", bridging the gap between self-interest and general welfare: a metaphysical image that implicitly lives on in the fascination for "self-regulating" markets and the implicit ethics of competition, however incomplete and lopsided it may be (cf. the box on *The ethics of a perfectly competitive, free market*).

Finally, against protectionist trade surplus theories, Smith generalized his argument on the efficient merits of the division of labour to the relationships between nations (by which he primarily meant the colonial powers). According to what has been called Smith's theory of "absolute advantage", it would therefore make sense for two nations to specialize on the production of those goods which they could make more cheaply than others – and then trade them freely, for the benefit of all. This way, overall efficiency of the world economy could be optimized in a way that protectionist mercantilism was unable to deliver.

The ethics of a perfectly competitive, free market Freedom and welfare, thus, are the two main pillars of liberal economical theory. According to this theory, a perfectly competitive, free market – as an “ideal type” – has the following characteristics:

- no market power: numerous buyers and sellers, none having a substantial market share
- no entrance barriers, no lock-ins: everybody is able to freely and immediately enter and leave the market
- complete information: everyone's fully and perfectly informed about others' actions and the prices, quantities and qualities of all goods on the market

---

- homogeneity: goods offered on the market are sufficiently similar
- no externalities: costs and benefits of the goods are being borne entirely by those buying and selling them
- efficiency: all market participants are utility maximizers
- non-regulation: there's no external regulation of prices, quantities or qualities of the goods on the market

Such a complete market, according to its advocates, is morally desirable because it corresponds to certain notions of justice, utility and moral rights: On the equilibrium point, where supply and demand curves meet, *everybody gets their fair share, at a fair price*. Also, resources at this point are allocated efficiently, therefore *buyers maximize their utility*. Everybody finally *chooses freely one's business and exchanges*, and consumers are sovereign, because no single buyer is able to exert power.

Given these desirable implications, "most nations of the world have embraced and tried hard to maintain competitive markets", in the words of Manuel G. Vasquez, "precisely because competitive markets tend to maximize utility, because they are just, and because they respect people's moral rights." (Velasquez 2011 : 199) In this ideal fashion, a perfect market would be "perfectly moral" (ibid. : 207), albeit in a somewhat limited sense (ibid.):

First, there are other, non-capitalist notions of justice that are based on needs (of those who have nothing to exchange for) and equality (regarding the distribution of accumulated wealth).

Second, the utility maximized is not exactly society's, but that of usually those individuals who can spend more and whose marginal utility is smaller than that of those less well off.

Third, the market ignores any positive rights to attain certain goods.

Fourth, the demand to remain competitive may force to use one's resources efficiently, leaving no room for loyalty and care towards concrete others.

Fifth, the same pressures to compete may have pernicious effects on individuals' virtues, crowding out morality and encouraging vicious behaviour.

Sixth, and most fundamentally, the moral claims of complete markets only hold *iff* all prerequisites are met – which is no less than utopian.

Nevertheless, if the perfectly competitive free market serves as a normative ideal – at least for relationships and exchanges which we choose to trust to markets – then this helps to identify what's morally objectionable: any market behaviour or external regulation that – by departing from perfect competition – tends *to diminish utility, to be unjust and to violate people's rights*, such as price-fixing, anti-competitive activities, externalities or other misinformation to consumers.

David Ricardo's (or Jane Marcet's) theory of comparative advantage delivered the ideological backing for free trade, holding that if you focus on your core business as a nation this eventually pays off for everybody.

It was not until a generation after Smith, however, that the English millionaire stockbroker and entrepreneur David Ricardo (1772-1823) delivered a lasting ideological foundation of free trade, with his theory of "comparative advantage" – even though some attribute the ideas published in his 1817 *Principles of Political Economy and Taxation* to English philosopher and economist Jane Marcet, who had presented the main argument of the theory in her *Conversations on Political Economy* a year earlier (Ransom 2001).

Whatever the authorship of comparative advantage: The theory was meant to show – in a simple two-country two-goods model (cf. the box on *Ricardo's theory of comparative advantage* below) – that it would be in the interest of both sides to specialize and trade, even if one of the countries could have produced both goods more cheaply.

Ricardo's theory of comparative advantage In David Ricardo's original example, England and Portugal are advised to specialize and trade, because at the end both will be better off – even if England is more productive in absolute terms both in the production of wine and cloth.

State 1 – differences in productivity/costs in man-years

	100 barrels of wine	100 rolls of cloth
England	120	100
Portugal	80	90

State 1 – what's produced without trade (following the theory of absolute advantage)

	Wine	Cloth
England	100	100
Portugal	100	100
SUM	200	200

State 2 – what's produced following (following the theory of comparative advantage)

	Wine	Cloth
England	0	220
Portugal	212	0
SUM	212	220

State 2 – what both sides get, based on fair exchange rates (the middle of resp. costs of production)

	Wine	Cloth
England	102 (+2)	114 (+14)
Portugal	110 (+10)	106 (+6)
SUM	212 (+12)	220 (+20)

Thus, specialization and free trade based on comparative advantages (and opportunity costs) is supposed to increase the total output of goods – an added bounty all countries can share in through free trade.

Due to the simplicity and persuasive power of the argument, *comparative advantage* was hailed one of the most important findings of modern economics. At least, the theory may have served to justify why not assorted royalty and landed gentry, but bourgeois industrial capitalists were the legitimate heirs to the riches that could be harvested form international trade. At any rate, it has been widely acknowledged – by proponents and critics alike – to be the key argument for the free trade doctrine and globalization, up until the present day. Even if the real world never had much in common with Ricardo's oversimple two-country two-goods example (Ransom 2001):

Comparative advantage was hailed one of the most important findings of modern economics, even if it didn't stand the reality check – maybe just because it so well served the interests of those unduly profiting from “free trade”.

- Capital does move from one country to another, and it is quite often not invested in production, but in speculative ventures ("hot money").
- Costs of production are not constant but will likely fall with economies of scale.
- Labour cannot simply be moved from one industry to another.
- International relationships and institutions – such as the WTO – are characterized

by power and dependency, and rules tend to favor influential industrial countries.

- The "terms of trade" at which goods are exchanged are not fair, but they do mirror these power relationships and may be subject to international speculation.
- Trade is by no means balanced, and some countries may actually be forced – due to debt and dependency from international capital markets – to let in foreign capital, to import or export more than actually furthers their national welfare.

So, as in the case of trade – which in theory is always voluntary and therefore fair – the notion of "comparative advantage" paints an ideal picture of a world of free exchange, in which every nation profits based on what it can do best. If this model is mixed up with reality, however, the argument serves an ideological end: It justifies conditions and relations that may be much more "advantageous" for some, compared to others – especially when it is known that, at the same time that liberalization and deregulation are being enforced in other countries through the WTO, protectionist measures are being taken in favour of national economies, from a position of power. An important lesson can be learned however, from the stubborn belief in free trade – in the words of David Ransom: "It is quite impossible to detach economic orthodoxy from the prevailing disposition of wealth, power and self-interest." (Ransom 2001 : 13)

Whatever the promised advantages of free trade – they were not to be had for the colonies that were still meant to serve as sources of cheap raw materials and labour, and as “dumps” for surplus goods produced in the homelands.

So, even if "free trade" had already become all the rage at the end of the 19th century, colonialism was still characterized by the very same imperialistic attitude that's expressed in the frank words of British colonialist Cecile Rhodes: "We must find new lands from which we can easily obtain raw materials and at the same time exploit the cheap slave labor that is available from the natives of the colonies. The colonies [will] also provide a dumping ground for the surplus goods produced in our factories." (*Wikipedia >> Cecil Rhodes*)

At the *fin de siècle*, globalization had reached a level not to be tied until a hundred years after.

Rhodes wrote this at the heyday of globalization: The amount of world trade reached in the last third of the 19th century – due to liberalization of economies, the industrial revolution and other technological innovations in transportation and communications – would not be tied for decades to come: The capital transfers to colonies by 1890 were greater in real terms than in 1990. Until before World War I, exports accounted or a larger share of global production than they did at the end of the millennium (Ellwood 2010 :18)

Apart from sheer numbers (we will come back to these in a second), what was new about this 19th century globalization, including colonialism, was *its explicit use for the capitalist accumulation of national wealth*: Not only did the colonies serve as a source of cheap raw materials and commodities. They had become what we would today call "emerging markets", staffed by the surplus population that had immigrated from the imperial homelands and was now supposed to buy the "surplus goods produced in our factories", as Rhodes had put it.

Globalization in numbers The development of economic globalization can be plotted by several indicators, such as the amount of world trade ("trade volume"), the amount of direct foreign investments, the number of internationally active corporations, or the worldwide integration of commodity and financial markets.
If we choose trade volume (measured by exports at current prices) as a proxy for economic globalization, it shows that world trade

- had grown steadily between 1870 (shortly before the deep crisis in 1873) and 1913 at 3,5% p.a.,
- slowed down but still grew at a rate of 1,3% p.a. between 1913 and 1937 (despite World War One and the Great Depression)
- and would reach an overall volume of 22,7 billion $ shortly before the outbreak of World War II, in 1938.

After World War II, world trade quickly (in 1948) settled at the double pre-War level and developed at impressive yearly growth rates, starting from the 1950s. The following table shows the middle yearly growth rates in total world merchandise trade for every decade up until the 2000s:

1950s 7%
1960s 8%
1970s 19%
1980s 9%
1990s 7%
2000s 12%
2010s (2009-2011) 6%

What this table clearly shows is that the new wave of globalization that we are currently experiencing started in the 1970's.

The sectoral distribution of trade volumes mapped in the next table indicates that commodities ("cash crops") and raw materials – the things that used to come from the South – have constantly lost ground compared to the value of other worldwide sectoral exports. There's already more money involved in the export of commercial services (excluding tourism and transport).

	agriculture	mining	industry	services
1980	14%	27%	53%	6%
2009	9%	17%	62%	13%

While these numbers do not distinguish export and import countries, exports from "peripheral" regions between 2000 and 2009 (without services) show quite well
- how these regions differ economically and
- that what's considered to be new about this recent globalization – a *New International Division of Labour* – mainly concerns Asia and
- that this structural imbalance has rather been aggravated than levied in the new millennium.

(*Sources: World Trade Organization; Ransom 2001, Ellwood 2010 – own calculations*)

Globalization 3.0 – The New International Division of Labour

The (quantitative) observation of a general, albeit uneven growth of exports in different sectors and regions of the world indicates that the economic globalization we experienced throughout the last 30 years is marked by a *qualitative change* – something that makes it different from earlier globalizations, apart from its scale: *Global trade today implies a new organization of global production – a New International Division of Labour.*

The new thing about today's globalization is the rearrangement of global production in terms of a *New International Division of Labour.*

This also implies a dramatic change of the "firm" as an economic entity: Processes and transactions that used to be run inside the firm – and therefore outside the market – are now being organized through the market, by contract. Therefore, *outsourcing* – including

Globalization goes hand in hand with a new model of the firm as an open network of mostly outsourced, market-based transactions.

its variants called "offshoring" and "nearshoring" – is the corporate core of this new globalization. The new model of the firm is the network.

All this means a completely new "global organization of production". Processes are being split up into tiny bits and pieces and relocated to various sites all over the globe. Here again, it is comparative advantage, but mostly absolute advantage that's at stake when companies decide to relocate or outsource production: low wages that may not suffice for leading a decent life, poor working conditions or minimal environmental standards which mean that these "advantages" all too often have to be paid by others, by way of "externalizing costs". That's exactly where the ethical issues of globalization come in: What's economically *efficient* (or at least "advantageous") may actually be seen as morally *illegitimate*.

This new wave of globalization, its uneven economic benefits and the social and ecological upheaval in its wake sparked the debates on CSR, sustainability and global governance that still go on today.

Indeed, public critique of economic globalization – given all the economic, social, ecological, cultural and political upheavals in its wake – very much initiated the renewed and hitherto unprecedented debate on corporate responsibility, sustainability, global governance and corporate citizenship that still goes on today.

Reasons and by-products of the current globalization The new wave of economic globalization itself was initiated by a deep crisis of the Fordist model that had dominated the booming post-War period in western Europe and the US, based on domestic markets, relatively balanced trade, full employment, Keynesian growth policies and the welfare state. Due to falling profits and an ensuing crisis of accumulation, the model came to be replaced on from the late 1970s by a "neo-liberal" model that set out to promote the rule of private property, markets and free trade.

This was made possible by several technological and institutional changes:

- **Technological innovations** at the turn of the millennium spurred and enabled this development. The internet and other instant means of communication and logistics allowed for global "just-in-time" production, but also the outsourcing of commercial services (such as call centers) to distant places.
- **Cargo costs** fell considerably (ocean freight unit costs -70%, air freight unit costs -3-4% p. a. since the 1980's). Thanks to cheap oil mainly, air traffic cargo tripled from 1985 to 1997 and is predicted to triple again by 2015.
- **Global institutions and regulations** such as the "Washington Consensus" and the WTO, which replaced the GATT in 1995, were designed to promote global free trade – albeit in a somewhat lopsided way that concedes protectionist exceptions mainly to rich countries of the North, while calling for "structural adjustment" and liberalization in the South.
- **Transnational Corporations** – entities that may move freely between national borders, invest, produce sell and pay taxes (or not) wherever they want – have become the paradigmatic institutions of today's globalization.
- **Export processing zones** in countries like China, Mexico ("maquiladoras") or lately also North Korea have become the workbenches of the global economy – and they also have to be seen in the context of forced liberalization and abandonment of import-susbstituting domestic policies.
- **Debt crises** like those in Africa and South America, South East Asia, Argentina and most recently within the North itself have become almost constant by-products of globalization. Massive inflow of foreign capital in search of quick gains ("hot money") has repeatedly brought countries at the verge of collapse and – through forced measures of "structural adjustment" – into deeper dependency.

The ethical challenges hidden in the supply chain

The ethical problem of "sourcing" is exactly about this critique on the downsides of globalization: The exploitation of lower legal and moral standards elsewhere for profits – and thus the failure to live up to the actual promises of globalization and free trade, as an ideal that's still alive (at least as a promise) in the claims of an eventual "convergence" of economies that would translate into a “social upgrading” in terms of income and standard of life as well. Until now, the promises have not become a reality for millions of people for which globalization may have brought work, but not a living.

The “balance of globalization” is – at best – mixed: The world has become a little richer, smaller, smarter and more democratic, yet at the same time less equal, less ecologically sustainable, less economically self-reliant and less diverse.

That's why the UNIDO, in 2008, decided to define a new category of "least developed manufacturing countries" – the "working poor" among the world's peoples, as it were. What, then, is the balance of globalization? Let's try to pin it down very roughly, based on four core areas of development and related promises and problems.

ISSUE	The promises of globalization	The problems of globalization
Economic development	increased efficiency and welfare on all sides based on comparative advantage, a process of consistent “industrial upgrading”, which is shown by GDP trends worldwide	distribution of the generated wealth has not been just, the gap between haves and have-nots, (new) centres and peripheries has increased
Social development	industrial upgrading is followed by social upgrading and better quality of life in poor countries, which is shown by HDI trends worldwide	human rights have been violated for profits, many do not earn living wages, and quality of life of many has deteriorated with the loss of economic independence and the deterioration of natural environments
Rule of Law	global trade necessitates legal certainty and improves the rule of law	corporations profit from poor law enforcement due to lack of staff, but also corporate bribery, corruption and pressure
Global Integration	global economic integration is a source of cultural integration, stability and peace	Globalization increases global competition, it increases traffic, transport & energy use, producing huge ecological problems, growing global dependency, and at a loss of regionally located economies

Obviously, the balance is mixed. The world may have become a little richer, smaller, smarter and more democratic – on the other hand, it likely also has become less equal, less ecologically sustainable, less economically self-reliant and less diverse. So, globalization did not deliver – but outright criticism also misses the point. Look at hard data, we can see clearly that there's been real development in most world regions during the last three decades – not only in terms of pure monetary gains (as measured by the GDP), but also in terms of quality of life (as very roughly measured by the HDI, even though it does not include quality of the natural environment).

The costs and benefits of globalization have been unevenly spread across the planet.

Still, half of the world's population have to live from less than two dollars per day, there are over 2 million deathly work accidents or work-related diseases per year, and there's an estimated number of over 200 million children working. According to the E*thical Trading Initiative*, a British-based multi-stakeholder group, there's a clear “moral case” for ethical sourcing that exactly follows from that: "Although buying companies benefit from sourcing from poor countries where wages and costs are low, they do have a moral responsibility to ensure that they do not exploit such conditions, but rather help to improve them." (Ethical Trading Initiative 2006 : 11)

Given this state of the world, after three decades of neoliberal globalization, companies should care, because they are involved, they do profit from it, they can't conceal it, and they are under scrutiny.

When this is – in very rough terms – the ambiguous situation of today's globalized world, what is the ethical problem, then, on the part of the firm? Why would it have to concern itself with these problems and challenges? And what's in for it when it manages to rethink and reform its (global) sourcing processes? In a word: *Why should companies care?*

- **They are involved**: Due to the fast and heavy integration of the world economy in recent years, almost any firm today has become – more or less obviously and intentionally so – part of a global supply chain or network. This may not be an entirely new situation (just think of a café that needs huge amounts of coffee and tea every day, or of a shoemaker who needs rubber soles), but its ubiquity and scale today is striking.
- **They do profit from it**: More or less consciously so, sourcing globally usually means taking advantage of lower standards and costs.
- **They can't conceal it**: This is due to the innovative technologies in communications, logistics, traffic and transportation which not only facilitate the global sourcing process, but also make it transparent.
- **They are under scrutiny**: Civil society interest groups in the North – and more and more so also in the South – have become very wary and critical about what companies are doing. The more exposed to a global market it is, the more exposed a firm becomes to the global public.

Taking advantage of cost advantage – at the cost of people and planet – may turn out to be a disadvantage.

In short: Taking advantage of cost advantage – at the cost of people and planet – may turn out to become a disadvantage for corporations. This is a lesson that many a company had to learn in recent years. One of them was *Nike* – a truly paradigmatic case of global learning (cf. the box on *The Nike Lesson*).

The Nike Lesson In a 1992 *Harper's Magazine* article, Nike was denounced for the appalling working conditions in some of its suppliers' factories. Labour activists and NGOs did single out Nike not because it was any worse than its immediate competitors – their business model was more or less similarly based exclusively on global outsourcing. They picked Nike because of its high-profile brand and the potential effect it could have had to make it move forward – a strategy NGOs have since used over and over again to promote their cause.

Nike's first reaction was to resort to its "good values" in comparison to its competitors. When management realized, however, that this did not lead anywhere, they agreed to the implementation of labour codes and their external verification. Nike had these one-off audits done by paid personnel with little experience and no credibility in labour circles, so this approach backfired: It was seen as an attempt to mislead labour groups and the public. Critique of Nike's failed and seemingly hypocritical attempts threatened to cascade down to youth markets – a prime source of Nike's profits and brand value. So in 1996, Nike installed its first department specifically responsible for managing its supply chain partners' compliance. In 1998, it officially launched its Corporate Responsibility department, signalling that acting responsibly meant more than being compliant. By the turn of the millennium, Nike's labour compliance team was more than 80 strong and the company had hired many external professional auditors for its roughly 900 suppliers.

Still, there was constant critique that Nike did not do as much as it could to address labour standards. So, Nike CEO Phil Knight assigned senior management to leave no stone unturned in figuring out how to get beyond this frustrating situation: The systemic – not only behavioural – problems and upstream drivers were to be addressed. As a consequence, incentives for the procurement team had to be made compatible with labour standards: Buyers, e. g., had so far been encouraged to circumvent code compliance to hit targets and secure bonuses. It became clear that Nike had to manage corporate responsibility as a core part of the business – which was technically simple but culturally and commercially problematic. Changing procurement practices involved heavy risks – at least in the short run, in view of its mainstream investors. Nike had to change its business model without unduly compromising its present bottom line. Therefore, it had to forego any first-mover disadvantage by getting both its competitors and suppliers on board.

Nike took part in the launch of the multistakeholder *Fair Labour Association (FLA)* – established with the help of the Clinton administration. Nike CEO Phil Knight also attended the launch of the *UN Global Compact* in 2000 – being the only CEO of a US company in attendance – and committed himself to "support ... mandatory global standards for social auditing", which meant that suppliers and competitors had to share the burden with first-movers such as Nike. Also, in 2004, it joined a broad multistakeholder alliance to prepare for the challenges of a post-*MFA* world: The "Multi-Fibre Agreement" had regulated export quotas. Its imminent end posed a threat to hundreds of thousands of jobs in the garment industry, notably in Bangladesh.

So, as corporate sustainability pioneer and consultant Simon Zadek sums up Nike's "learning curve" from pariah to "civil leadership": "Nike is, of course, a business, and as such is accountable to its shareholders. But the company has taken significant steps in evolving a strategy and practice that shifts it from being an object of civil activism to a key participant in civil society initiatives and processes. In dealing with the challenges of corporate responsibility, Nike has come to view the issue as integral to the realities of globalization – and a major source of learning, relevant to its core business strategy and practices. That learning prompted the company to adopt codes of labour conduct, forge alliances with labour and civil society organizations, develop nonfinancial metrics for compliance that are linked to the company's management and its broader governance, and engage in the international debate about the role of business in society and in public policy." (Zadek 2004 : 132)

(*Source: Hiß 2005; Zadek 2004*)

Corporate sustainability pioneer and consultant Simon Zadek called this the *five stage process of "civil learning"* which any corporation that wants to live on in a stakeholder society would have to go through – sooner or later, slower or faster. He picked Nike as an early and model example for this process, because its business model was based exclusively on global outsourcing, and because it somehow managed to move form a strictly *defensive* approach – that was firmly rooted in the classical neo-liberal shareholder model of the global corporation – to a *proactive* approach that should make the company ready for the 21st century.

The process of "civil learning" paints an ideal picture of a company being reembedded into society and its moral fabric.

The Process of Civil Learning (Source: Zadek 2004)		
DEFENSIVE "It's not our job to fix that."	deny practices, outcomes or responsibilities	fight off negative short-term effects on brand value, sales, recruitment and productivity
COMPLIANCE "We'll do just as much as we have to."	adopt cost- & policy-based compliance approach	mitigate erosion of economic value in medium term due to reputation and litigation risks ...
MANAGERIAL "It's the business, stupid."	embed issues in the core management processes	... and accrue longer term gains due to integration
STRATEGIC "It gives us a competitive edge."	integrate societal issues in core business strategies	enhance economic value in the long term and gain first-mover advantage by aligning innovations & claims ...
CIVIL "We need to make sure everybody does it."	promote broad industry participation	... and overcome first-mover disadvantages and realize gains through collective action

The Nike example is instructive in that it shows in a nutshell a few things that have changed in the transition from a classical shareholder-focused understanding of corporate responsibility to a more timely understanding, realizing that a company is indeed part of society and will be held accountable for what it does to it – wherever this may be:

The lessons Nike had to learn hold true for all companies aiming to act in socially responsible ways, whether or not they are active on the global marketplace.

- **Legality does not mean legitimacy**. Companies can no longer resort to the apology that sourcing is nothing but an economic transaction, based on a contract that was signed between two separate legal entities on a voluntary basis.
- **The responsibility of firms does not end with their design and marketing studios.** It does not only extend to *what* they produce and how they sell it to their customers, but it does extend to how they produce or let produce it as well – throughout the whole supply chain (and the downstream value chain as well, as we will discuss in chapter 4).
- **Firms are advised to be proactive.** Firms are advised to not only react on public outcry and take *ad hoc* measures to minimize short-term risks. They have to realize that what they cannot sit out they better take into their own hands.
- **Firms are advised to be consequent and rational.** They need to develop strategies, processes and instruments/standards that are consistent with or still better integrated into their overall management systems.
- **Firms are advised to do this together** – with their suppliers, other companies in their industry, and third parties. There's a certain responsibility to do this, as a good corporate citizen, but it also helps to limit free-riding.

- **Firms are advised to rethink their model of value creation.** In a stakeholder society, companies need to realize that they are indeed part of society, its values and expectations.

All this has obviously changed rather quickly – and it is nothing which is "objectively" so: Actually, what is deemed moral or legitimate – in business, but similarly in politics or sports, you name it – is basically the product of a social *discourse*: a public, powerful confrontation of arguments between the corporate world and civil society (in the present example), in which the "moral economy" may eventually assert itself on the market. That's exactly why interest groups have targeted the high-profile brands that people like to identify with (sneakers and sports gear, textiles, IT gadgets, but also coffee, e. g.), because for these, reputation is really an asset – or their *Achilles' heel* (cf. chapters 3 and 4).

So far, however, the immediate sanctions companies have to face for not living by these simple rules are just (?) economic ones.

So, in the past, moral pressure initiated by civil society in many cases proved to be more effective than legal pressure: So far, efforts to bring corporations to justice in their homelands for human rights abuses abroad have not been very successful – and even in the case of a court sentence, the legal sanction itself (even though appropriate reparations to victims or their dependants would be much needed) would probably not have the same deterring effect as the reputational damage done to such a corporation – from immediate boycott measures to long-term loss of “brand equity”.

On the other hand, there's certainly also a business case of acting socially responsible – even if equally contingent on market demand.

Of course, this holds only as long there is sufficient pressure. Indeed, public attention and scrutiny is usually very short-lived. Still, changing societal expectations based on increasing wealth, education and information have been identified by some observers seen as a major source of an ongoing "moralization of markets", promising to change the way we do business in substantial ways (Stehr 2007 – we will get back to this in the next unit). Seen that way, doing good and internalizing costs along the value chain may prove to be a “business case” in the long run (cf. the box on *The Business Case of Ethical Sourcing*).

The Business Case of Ethical Sourcing

- It is good reputational management.
- It is good risk management.
- It is an indicator for good overall quality of management.
- It is good for access to capital (not only) from the SRI community.
- It is an asset in B2B transactions.
- It increases trust, reduces transaction costs.
- It wins the best brains.
- It is good for employee identification, motivation and retention.
- It is good marketing, as a trusted USP.

There's of course also a strong moral case for compliance with human rights and fundamental labour rights.

Of course, while the business case of ethical sourcing – however plausible it sounds – may be only anecdotical, rather small, hard-won or just non-existent, there's of course a *moral* case to it, too. And there's good reason to consider complying with human rights and fundamental labour rights a universal, unconditional moral norm in global business – at least as long as there's no binding (or sufficiently sanctioned) regulations on the global marketplace (cf. the box on *Human Rights and Basic Labour Rights*).

Human Rights and Basic Labour Rights In 1948, the UN General Assembly – in the aftermath of WW2 and the Holocaust – adopted the *Universal Declaration of Human Rights*. The concept of “human rights” is a truly modern ethical concept, based on the Enlightenment concept of “natural rights” that inspired the 18th century political revolutions. Its more immediate forerunners are 19th century movements for the abolition of slavery and child labour, for women's and workers' rights as well as national liberation movements and the civil rights movements of the 20th century.

The *UN Declaration* in the preamble recognizes that protecting "the inherent dignity and … the equal and inalienable rights of all members of the human family is the foundation of freedom, justice and peace in the world." This means that human rights are conceived to be valid regardless of any particular geographical location, state, race, culture or sex, and not bound to certain duties (such as are citizenship rights). The UN issued additional conventions relating to certain groups, such as "on the rights of the child" (1989) or on "migrant workers and their families" (1990, in force sine 2003)

With respect to corporations, there's yet no international treaty that specifically covers the behaviour of companies with regard to human rights – which has been harshly criticized. Since 2003, however, a draft on *Norms on the responsibilities of transnational corporations and other business enterprises with regard to human rights* was issued. These were considered by the *Human Rights Commission* in 2004, but have no binding status on corporations and are not monitored. Substantive rights include the right to life, to freedom from torture and from slavery, the right to a fair trial, freedom of speech, thought, conscience and religion.

Relativist criticisms of universal human rights usually argue for acceptance of different cultures & their practices. They fear that universalism could be a form of imperialism. Former Singapure prime minister Lee Kuan Yew, e. g., argued that authoritarian government, due to the sense of loyalty, social stability and prosperity, would be more appropriate in Asia than democracy. Similar reservations were made by Iranian UN representatives who see human rights as an offspring of Judeo-Christian tradition.

Universalists, on the other hand, argue for the general newness of human rights for all cultures, that they were drafted by people from many different cultures, and that there's a universal belief in universal norms.

ILO declarations on core workers' rights The *ILO (International Labour Organization)* is a UN agency with 183 member countries. It is the international body competent for raising international labour standards. It features a tripartite governing structure, representing government, employers & workers. The ILO issues both recommendations and conventions: ILO recommendations provide mere guidance to members states. ILO conventions have the status of a binding treaty on ratifying countries, they represent benchmarks of strong labour standards for national legislature.

In 1998, the *Declaration on Fundamental Principles and Rights at Work* was issued, committing member states to respect and promote supposedly universal "core" principles. They are grouped in four categories:

- freedom of association and the effective recognition of the right to collective bargaining,
- the elimination of forced or compulsory labour,
- the abolition of child labour,
- the elimination of discrimination in respect of employment and occupation.

Since these core principles are claimed to be universal, they apply to all people in all states, regardless of national certification. On the other hand, ILO structure and principles have been criticized to be either not "flexible" or not deterrent enough due to only light sanctions.

So, given that there's a promising business case and a clear moral case for it, integrity throughout the value chain is a topic of growing concern in most industries. Therefore, a good moral reputation based on assured quality and transparency in these realms – in a word: *legitimacy* – has become a central challenge in the process of value creation. So, how do conventional and ethical sourcing differ from each other?

A good moral reputation has been become a valuable asset – yet it has to be *earned* by applying a new model of ethical sourcing.

	old model	**new model**
concept of responsibility	downstream, for shareholders and consumers	supply or value chain responsibility for all stakeholders involved
concept of value	cost efficiency & profitability	legitimacy & social value
general management approach	power	dialogue
issues management approach	passive & reactive	proactive
means & objectives	price pressure	moral pressure

The Nike case already pointed at the importance of proactive change, cooperation and integrity – let's see what this involves for an ethical sourcing process in a bit more detail (adapted from Ethical Trading Initiative 2006):

- **Proactive strategy development**: This means to understand what society expects from a company, what the legitimate and powerful interests of different stakeholder groups are. Many leading companies in integrity management (such as the Swiss *Migros* or British *The Co-operative*) are actively involving their stakeholders in the process of strategy development.

Ethical sourcing in practice implies the development of an integrated strategy to be based on a true dialogue with stakeholders.

- **Cooperative implementation**: First, this involves a co-operative relationship with suppliers. What's important here is that it is made clear what is expected from them. This is not about imposing "codes of conduct" which suppliers themselves then delegate to their workers to sign. This is about actively working together with a clear understanding that such improvement is in the interest of common successful business relationships. What should be communicated to suppliers is the benefits of working towards compliance, how the supplier can work towards compliance, what will happen if the supplier doesn't comply and the importance of involving workers. Second, it involves a co-operative relationship within the industry, in the way of a shared responsibility for a business context that does reduce the risk of free-riding. Finally, this does imply cooperation with NGOs, certifying bodies and other stakeholder groups in that area.

It involves the definition and consequent implmentetation of goals to be based on a true cooperation with suppliers and other parties throughout the value chain.

- **Standards, Codes and Performance Indicators:** The sourcing process finally has to be based on definite standards, criteria and indicators on which management decisions, controlling and monitoring measures and public reporting can be based. There are already many different standards *on the market* that do considerably vary with respect to *subjects* (who or what is addressed, ranging from production sites to single products), *issues* (what area of management is addressed), *instruments* (ranging from binding

It involves, finally, the adoption of some performance measures to be based on reliable and comparable validation schemes.

minimum standards and their certification to voluntary commitments) and *validation* (whether and what kind of audit). Indeed, they also vary with respect to their quality. The following table lists some of the most important standards of different kinds.

	Global Compact	**SA 8000**	**ETI**	**Fair Trade**	**GRI**	**BSCI**
FOCUS	leadership	individual production sites, suppliers	supply chain	products ("cash crops")	value chain	supply chain
ISSUE	global governance	working conditions	working conditions and trade relations	working conditions and trade relations	Sustainability reporting	working conditions
INSTRUMENT	code of ethics, commitment & self-evaluation	substantial standard & indicators	standard & network for implementation & audit	product label	Sustainability KPIs & reporting guideline	industry self-commitment
EXTERNAL AUDIT & CERTIFICATION	no	yes	yes	yes	yes (voluntary)	no
SIMILAR	Sullivan Principles, Cauy Round Table Principles, OECD Guidelines for MNCs	ILO conventions and recommendations (targeted at countries)	FLA, CCC, FWF,	FairForLife, utz certified, Rainforest Alliance		RSPO, RTRS, 4CC,

Bibliography

Braudel, Fernand. 1979. *The Structures of Everyday Life. The Limits of the Possible*. Bd. 1. Civilization & Capitalism. 15th - 18th Century. New York & others.

Ellwood, Wayne. 2010. *The No-Nonsense Guide to Globalization*. Oxford.

Ethical Trading Initiative. 2006. *Ethical trade ... a comprehensive guide for companies*. ETI Workbook. Edition 2. London.

Hiß, Stefanie B. 2005. „Durch Reden zum Handeln?! Zur Rolle freiwilliger Unternehmensinitiativen bei der Verbreitung von Sozialstandards“. *Zeitschrift für Wirtschafts- und Unternehmensethik* 6 (2): 215–30.

Keynes, John Maynard. 1972. „Economic Possibilities for our Grandchildren“. In *Essays in Persuasion*, IX:321–32. The Collected Writings of John Maynard Keynes. London and Basingstoke.

Mandeville, Bernard. 1957. *The Fable of the Bees: Or, Private Vices, Publick Benefits*. Oxford.

Proulx Lang, Ann. 1973. „Poggio Bracciolini's De Avaritia. A Study in Fifteenth Century Florentine Attitudes Toward Avarice and Usury“. Montreal, Canada: Sir George Williams University.

Ransom, David. 2001. *The No-Nonsense Guide to Fair Trade*. Oxford.

Smith, Adam. 2008. *An Inquiry into the Nature and Causes of the Wealth of Nations [1776]*. o. O.: Forgotten Books (www.forgottenbooks.com).

Stehr, Nico. 2007. *Die Moralisierung der Märkte: eine Gesellschaftstheorie*. Frankfurt am Main.

Velasquez, Manuel G. 2011. *Business Ethics. Concepts and Cases*. London.

Zadek, Simon. 2004. „The Path to Corporate Responsibility“. *Harvard Business Review* December: 125–32.