

The contrarian

Milton Friedman – misunderstood or misguided?

The legendary economist was both right and wrong about corporate social responsibility, argues Jon Entine

The recent death of Milton Friedman, the Nobel-prize-winning economist, sent old-guard corporate social responsibility advocates into familiar anti-capitalist attack mode.

After all, Friedman penned the famous, or infamous, article in 1970, whose title supposedly constituted its only point: “The Social Responsibility of Business Is to Increase Its Profits.”

Joel Makower, a prominent “green business” consultant, toes the corporate social responsibility line, arguing that the “doctrinaire Friedmanesque” position encourages companies to “exploit and pollute ... in the name of economic growth and competitiveness”. Makower writes: “We know better now.”

Utter hogwash, as Friedman might have said.

Let’s be unequivocal: Friedman did not dismiss corporate social responsibility outright. He opposed the personalised, idiosyncratic form – executives who, in his words, have “affected to trade for the public good” but really just follow ideological vanity. Good intentions are not a high enough standard for corporations. Without checks and balances on executive behaviour, which is what the free market provides, intentions can, and often do, go awry. Then everyone – shareholders, employees, customers, and taxpayers – lose.

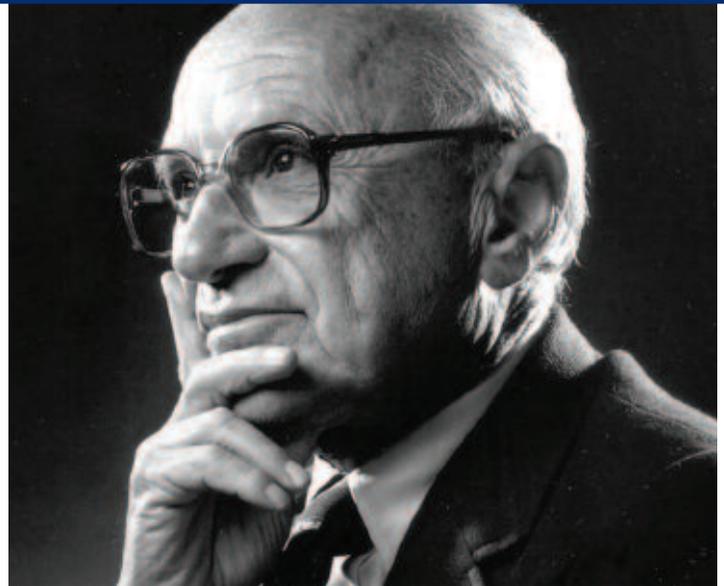
That is what happened at Levi Strauss in the 1990s. It was once a brand-behemoth attracting favourable press because of its “socially responsible” policies, including a pledge to manufacture jeans only in the US. While it promoted Aids prevention and board diversity, and funded a centre for corporate responsibility at Berkeley, it manufactured increasingly shoddy products, treated piece workers poorly, and saw its chief executive mismanage it into the ground.

Levi’s was ultimately forced to shut its US plants, canning 6,500 employees. It blamed the closure on cheap imports, which allowed it to pass the buck to taxpayers to compensate the workers. Then it got the government to subsidise a \$29 million insurance policy for a garment plant in Turkey in the process of moving all of its manufacturing to low-wage havens. The privately held company, which has to disclose its finances because of its public debts, still owes billions of dollars.

So in the end its high-minded stance resulted in a lot more harm than good. Why? Because Levi Strauss had its clock cleaned by competitors.

Belying the poison pen commentaries, Friedman wrote that, however he personally felt about it, doing good, using the popular parlance, not only should but must be pursued if it adds competitive value to products or services.

Whole Foods Market, the world’s largest natural foods retailer, provides a good contrast with Levi Strauss. In a debate last year in Reason magazine with Friedman, its chief executive, John Mackey,



Profit isn't always bad...

prattled that Whole Foods embraced “loving people” and “generating positive results for society”, attempting to paint the Chicago School economist as misguided.

But Mackey’s operating philosophy sounds positively Friedmanesque. “The most successful businesses put the customer first, instead of the investors,” he said, which Friedman said is what profitable businesses do because it drives up the stock price – and that is exactly what has happened at Whole Foods.

Goodwill as by-product

Mackey also said: “There can be little doubt that a certain amount of corporate philanthropy is simply good business and works for the long-term benefit of the investors.”

As Friedman replied, echoing what he wrote in 1970: “In the present climate of opinion, with its widespread aversion to ‘capitalism’, ‘profits’, the ‘soulless corporation’ and so on, [corporate social responsibility] is one way for a corporation to generate goodwill as a by-product of expenditures that are entirely justified in its own self-interest.”

Friedman wrote that if an energy company can demonstrate that the release of industrial effluents creates a controversy that results in adverse publicity, litigation, or regulation, or makes it difficult to retain employees, then voluntary reduction or clean-up makes business sense. They have a fiduciary responsibility to do so.

Let’s not be naïve. Executives that profess doing good know that corporate social responsibility has become a powerful reputation weapon in an increasingly commoditised marketplace.

But unless “good intentions” are mediated by market competition, frequent disasters are inevitable, and all stakeholders suffer. As Adam Smith contended, those who embrace the “invisible hand” often end up contributing more to the public weal than those who claim altruistic motives.

The fact is the growing prosperity throughout much of the world has been driven by the free market and anti-Keynesian economic policies that Friedman so eloquently advocated. As Bennett Freeman, the new vice-president of research at socially responsible investment specialist Calvert, has said, maybe it is time to depoliticise corporate social responsibility. ■

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