GDP and Business Social Responsibility

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Abstracts

Traditionally, GDP/PCY is used by UN to rank countries to indicate their level of economic growth/ development. This way of ranking countries suffers from a number of limitations which arise from inherent shortcomings in GDP/PCY. GDP/PCY does not capture inequalities of income, leisure, regrettable necessities, services rendered by house wives and other institutions out of love and affection, availability of clean and healthy environment etc,. To get a better measure of well-being Human Development Index, Measure of Economic Welfare, Index of Well-being, Gross National Happiness, Wealth Index, National Prosperity Index, Genuine Progress Indicator, Physical Quality of Life Index and Index of Sustainable Welfare are suggested. The problem with the alternatives to GDP/PCY is that all of them, except HDI, are not quantifiable to be expressed in one figure. For a country to achieve a certain level of well-being, businesses have to reorient themselves from pure business activities to Socially Responsible Business activities. How to make business socially responsible is a problem by itself. Should we leave it to businesses or government should play a Proactive role in this remains an issue.

Introduction

Business, undertaken in the private or public sector, makes its impact felt at the macro / aggregative level. At the aggregative level, it can influence GDP / GNP / NATIONAL INCOME / and PER CAPITA INCOME of an economy. In fact, if there is any one precise measurable figure which has been taken as indicative of the economic progress/ economic well-being of an economy, inspite of its innumerable shortcomings, it is per capita income (PCY) .Various other alternatives have been suggested to supplement PCY to measure the well-being of a nation.

One such measure published by United Nations Development programme (UNDP) is Human Development Index (HDI).This concept was visualized by Prof. Mahbub ul Hag and Prof. Amartya Sen and

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has been used by UNDP to rank countries. Besides HDI, other indices developed are Gender- related Development Index, the Gender Empowerment Measure and the Human Poverty index. Led by its Former King, King Jigme Singye Wangchuk, Bhutan measures its wellbeing by Gross National Happiness (GNH) instead of Gross Domestic Product (GDP).

Dr. A P J Abdul Kalam, Former President of India, has suggested an alternative to GDP which he calls it as National Prosperity Index (NPI).

Gross Well-being Index (GWI) is another alternative suggested by World Bank economist, Francois Bourguignon, World Health Organization (WHO) expert on violence indicators Alex Butchart and United Nations (UN) and International Labor Organization (ILO) Head of Statistics Francesca Perrncci and Sylvester Young.

Let us start with GDP. It is defined as the money value of the flow of final goods and services produced, over a year, within the Domestic territory of an economy, with the help of labor working with capital and natural resources of the economy. GDP of an economy can be at market prices as well as at factor costs. Further GDP can be worked out both at current prices as well as at constant prices. GDP at current prices is called Money GDP and GDP at constant prices is referred to as Real GDP.GDP at current prices is adjusted by an appropriate price index to arrive at GDP at constant prices which gives us in money terms the availability of final goods and services on which the Economic well-being of the people depends. Real per capita GDP is given by dividing Real GDP by the population of an economy i.e. it gives per capita availability of final goods and services used for final consumption and investment purposes. Economic well-being and real per capita GDP are expected to be positively related to each other.

Limitations of GDP

In reality, GDP or Per Capita GDP or Per Capita Income is not the best possible indicator of well-being of a nation. Some of the reasons for this are stated below. To begin with, GDP is a production concept which includes production of capital goods also, whereas Economic well-being depends more on income and consumption of individuals and households. Further, GDP is a 'gross' concept: it makes no allowance for the using-up of capital equipment in the production of goods and services and also because of normal obsolescence. To keep the production capacity in-tact we need to re-invest part of the output i.e. the economy needs to replace worn-out capital equipment. Thus Net Domestic Product (GDP minus Consumption of Fixed Capital) is a better Index of economic well-being.

GDP does not take account of income distribution of an economy. A society in which there were a few' colossally' wealthy families but the bulk of population lived in abject poverty, would presumably enjoy a lower level of "general" well-being than one with the same GDP but where there was no acute poverty.

The process of generation of GDP entails the co-production of "bads" (e.g. pollution, deterioration of the environment).These are rarely taken account of in the GDP accounts. GDP makes no allowance for the using-up of non-renewal resources, which will affect the economic well-being of future generations. Sustainability of GDP is as important as current level of GDP.

GDP includes only monetary transactions, it misses many other activities that people value like caring for children or elderly at home. GDP also ignores the value of leisure time spent relaxing or with family and friends. It does not include the value of clean air and water. It ignores every thing that happens outside the realm of monetized exchange, regardless of its importance to well-being. As non-market economy declines and its functions shift to the monetized service sector, the GDP portrays this process as economic advancement though economic well-being remains unchanged.

GDP includes many items that do not boost human well-being. If an earthquake destroys an entire region, the reconstruction effort is counted as a boost to GDP even if it only replaces something that was there not long before. Likewise expenditure on crime prevention and security adds significantly to GDP in many countries but only restores a safe environment. Medical expenditure as a result of air and noise pollution also adds to GDP as do diet classes, antidepressants and a sizeable list of other items.

It would be more appropriate to say that GDP is a fair measure of production (if real GDP is computed) but it is a misleading measure of well-being since non- market activities such as domestic and charity work equally contribute to well-being but are not included in GDP. Moreover complex realities such as crime, the environment and the efficiency of the health system as well as income inequalities do effect well-being. Taking the case of traffic jams, we can realize that more production does not necessarily correspond with greater well-being, It was way back in 1934 that Simon Kuznets, the economist who invented GDP said," Welfare of a nation can not be inferred from a measurement of national income". Output arising from wars and natural disasters may register as an increase in GDP but it does not necessarily increase well-being.

While GDP has proven useful in comparing data from different countries, one of the Main weaknesses is that it 'cannot distinguish between activities that have a negative and positive impact on the well-being' of society, as stated by Joauquin Almunia, the European Commissioner for economic affairs.

Well-being

Well-being, as is implied above, is multi-dimensional concept and the key dimensions which should be taken into account are:

- Material well-being (income, consumption and wealth)
- Health
- Education
- Personal activities including work
- Political voice and governance
- Social connections and relationships
- Environment (present and future conditions)
- Insecurity, economic as well as a physical

Besides the objective factors, subjective dimensions of well-being are equally important. The information relevant to valuing quality of life goes beyond people's self-reports and perceptions to include measures of their "functioning's" and freedoms. Subjective well-being covers different aspects (cognitive evaluation of one's life, happiness, satisfaction, positive emotions such joy and pride, and negative emotions such as pain and worry).

Human Development Index (HDI)

Human Development Index (HDI) is offered as an alternative to GDP. The first Human Development Report was published in 1990 under the leadership of Pakistan Economist and finance Minister (MahbubUl Hag) and the Indian Nobel Laureate for Economics Prof. Amartya Sen.

HDI is a summary measure of human development that is published by United Nations Development Programme (UNDP). The HDI provides an alternative to the common practice of evaluating a country's progress in development based per capita GDP, The concept is operationalised by UNDP and the countries are ranked based on HDI.

The HDI measures the average achievements in a country in three basic dimensions of human development.

1. A Long and healthy life, as measured by life expectancy at birth.
2. Knowledge, as measured by the adult literacy rate(with 2/3 weight) and the combined primary, secondary and tertiary gross enrollment ratio(with1/3 weight)
3. A decent standard of living, as measured by GDP per capita in purchasing power parity (ppp) terms in U.S dollars.

Before the HDI is calculated an index is created for each of these dimensions. To calculate these indices—the life expectancy, education and GDP indices-Minimum and Maximum value are chosen for each underlying indicator. For example, in 2004 the Maximum and Minimum values of life expectancy were 85 and 25 years respectively. Performance in each dimension is expressed as a value between 0 and 1. The HDI is then calculated as a simple average of the dimension indices.

Methodology to calculate HDI

In general, to transform a raw variable, say x, into a unit free index between 0 and 1 (which allows different indices to be added together), the following formula is used.

$$\text{x- Index} = \frac{x - \min(x)}{\max(x) - \min(x)}$$

Where min(x) and max(x) are the lowest and highest values the variable x can attain respectively. The Human Development Index (HDI) then represents the average of the three general indices.

$$\text{Life Expectancy Index} = \frac{LE - 25}{85 - 25}$$

Education Index = 2/3X ALI + 1/3 X GEI

$$\text{Adult Literacy Index} = \frac{ALR - 0}{100 - 0}$$

$$\text{Gross Enrollment Index (GE)} = \frac{CGER - 0}{100 - 0}$$

$$GDP = \frac{\log(GDP_{pc}) - \log(100)}{\log(40000) - \log(100)}$$

HDI = 1/3(Life Expectancy Index) + 1/3 (Educational Index) + 1/3(GDP Index)

To give an illustration, in the year 2007 World Bank gave GDP wise ranking as follows:

Country	Ranking
U.S.A	1
Japan	2
China	4
Canada	9
Australia	15
Pakistan	45
India	12

Based on HDI, UNDP ranked the above mentioned countries for the year 2007 as follows:

Country	**Ranking**	**HDI**
U.S.A	8	.948
Japan	7	.949
China	81	.768
Canada	6	.950
Australia	3	.957
Pakistan	134	.539
India	126	.611

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From GDP to Well-being

GDP – Depreciation - Net Income going abroad – Regrettable = Consumption + Net Investment.

Consumption + Net investment + Leisure + Wealth + Non-Market activities + Unemployment (insecurity) = Economic well-being.

Economic well-being + Environment + Health + Inequality + Educations = Living condition.

Living condition + Genetics + Family + activities + Friends + Work satisfaction +Community ties = Well-being or Happiness.

Measure of Economic Welfare (MEW)

Nobel Laureate James Tobin and William Nordhaus highlighted in the early 1970's that "GDP is not a measure of welfare" and proposed Measure of Economic Welfare (MEW) that adds to GNP the value of household services and leisure, subtract the cost of capital consumption and of "bads" such as pollution, and excludes for example police services to combat crimes. The weights of the different measures depend on the researchers' subjective assessment. Therefore this measure can not be put into use across different countries of the world.

Index of Well-being (IOW)

Another alternative is provided by the Index of Well-being, as given by Canadian centre for the study of living standards. It has four components. (1) Flow of private and government consumption (2) The stock of physical and human capital.(3)Inequality captured through the Gini co-efficient and the poverty intensity and (4) The security component aggregates diverse items such as divorce rates and employment rates(with a negative sign). The weights to above four components were originally set at .4,.1,.25 and .25,In the year 2004 Norway was ranked with highest Economic well-being.

Gross National Happiness (GNH)

Led by its Former King, Jigme Singye Wangchuk of Bhutan , the Kingdom of Bhutan is the only country in the world to measure its well-being by Gross National Happiness (GNH) instead of Gross National Product (GNP).This unorthodox approach is a serious attempt to question the values of unbridled economic progress, and foreground the importance of maintaining a balance between tradition and modernization. Bhutan has followed a cautious path of development since the 1960's with the intention of preserving its heritage and protecting its environment.

GNH is an official policy of the kingdom having been passed in Parliament and it is perhaps best illustrates by best some examples from Bhutan which prove that happiness really does take precedence over economic property there. The country limits the members of tourists that are able to visit it, because the Bhutanese had complained that the environment was being affected and sacred lands were being spoiled. Similarly, demonstrating that the concept of GNH is inextricably connected to accountability; anyone with a grievance can go to the king himself and get a hearing.

This policy of GNH, as well as focusing on cultural promotion and good governance, also aims to put an end to "Spiritual Hunger". Material and technological progress is not rejected or banned, but it must not be to the detriment of the value of human life, and humanity's soul. Mental and psychological wealth is genuine considerations in Bhutan. Happiness is more important than monetary wealth.

Essentially, the idea of GNH is to encourage a rethinking of what is important in people's life: Should the success of a nation be judged by its ability to produce and consume, or should it be based on the quality of life in that country, the happiness of its people, however difficult that might be to measure in practice?

"Economic calculation ignore the value of fresh water and green forests, clean air, traditional ways of life", merely because they cannot be easily quantified.

Money from logs is counted as part of a country's income but the depreciation of the forest as a result is nowhere calculated. The unpaid volunteering, caring and nurturing sectors, the informal 'Compassionate Economy' is also noticeably absent, despite some studies saying it represent 50% of all productive work in societies. And while the GNP measures an increase in production and consumption, and labels it as a symbol of success, there is no proportional increase in waste mentioned, nor the fact that environmental resources are finite ,not a free good.

Wealth Index (WI)

Amartya Sen. defines Economic development in terms of basic necessities such as education and health care. Thus an ethical dimension begins to be restored in economics. There has been an increasing trend for corporations and companies to demonstrate "Social responsibility" due to public pressure. All of these factors point to the need for and trend towards an altruistic economics taking account of all factors well concerning well- being, not just financial ones.

Steps in this direction include the World Bank's, "Wealth index"(which includes the concepts of human capital and environmental capital), the UN Human Development Index (which measures things like education provision, human rights records and life expectancy) and, most interestingly the "Calvert – Henderson quality of life indicators" which also incorporate cultural values and activities of self improvement and group discussion.

Altruistic Economics may be possible, and one with a spiritual dimension might also be, but as yet, GNH is a policy and an ideal, not a quantifiable economic system which is not to say that the example of Bhutan should not be followed, only that it should be improved upon.

National Prosperity Index (NPI)

The concept of National Prosperity Index (NPI) is propounded by the former President of India Dr.A.P.J.Abdual Kalam. NPI is a summation of annual growth of GDP, improvement in quality of life, particularly those living below the poverty line, and adoption of a value system derived from civilization heritage.

Quality of life, according to him is a function of availability of housing, good water, nutrition, proper sanitation, quality education, quality health care and employment potential. Value system is a function of promoting joint family system, creation of spirit-of working together, living in a righteous way of life ,removing social inequities ,and above all a conflict free, harmonious society .

Genuine Progress Indicator (GPI)

The Genuine Progress Indicator (GPI) is a concept in green economics and welfare economics that has been suggested to replace GDP as a metric of economic growth.

The GDP vs. the GPI is analogous to the difference between the gross profit of a company and the net profit. The net profit is the gross profit minus the costs incurred. Accordingly, the GPI will be 0 if the financial cost of crime and pollution equal financial gains in production of goods and services, all other factors being constant. The need for GPI to supplement biased indicators such as GDP was highlighted by analysis of uneconomic growth in the 1980's notably that of Marilyn Waring who studied biases in the UN system of national accounts. Some economists notably Herman Daly, John Cobb and Philip Lawn have asserted that a country's growth increased goods and services which have both "costs" and "benefits" that contribute to GDP. They asserted that, in some situations, expanded production facility damaged the health, culture and welfare of people. Growth that was excess of sustainable norms (e.g., of ecological yield) had to be considered to be uneconomic. According to the "threshold hypothesis", developed by Manfred Max and Neef, the notion that when macroeconomic system expands beyond a certain size, the additional benefits of growth are exceeded by the attendant costs.

According to Lawn's model, the "costs" of economic activity include the following potential harmful effects.

1. Cost of resource depletion.
2. Cost of ozone depletion.
3. Cost of crime.
4. Cost of family breakdown.
5. Cost of air, water and noise pollution.
6. Loss of farmland.
7. Loss of wetland.

Physical Quality of Life Index (PQLI)

This Index was developed by Overseas Development Council in the mid 70's by Morris David Morris. Steps to calculate PQLI are:

1. Find% of the population that illiterate (literacy rate).
2. Find the infant mortality rate. (Out of 1000 births) indexed infant mortality rate=(166-infant mortality)x0.625.
3. Find the Life Expectancy. Indexed Life Expectancy=(Life Expectancy-42) x 2.7.
4. Physical Quality of Life=(Literacy rate + Indexed Infant Mortality rate + Indexed life Expectancy

Index of Sustainable Welfare (ISW)

In feb,2008, the President of the French Republic, Nicholas Sarkozy, unsatisfied with the present state of statistical information about the economy and the society, asked Joseph Stiglitz (president of the commission), Amartya Sen (Advisor) and Jean Paul Fitoussi (coordinator)to create a commission, subsequently called" The commission on the measurement of economic performance and social progress(CMEPSP)." The commission's aim was to identify the limits of GDP as an indicator of economic performance and social progress, including the problems with its measurement; to consider what additional information might be required for the production of more relevant indicators of social progress; to assess the feasibility of alternative measurement tools, and to discuss how to present the statistical information in an appropriate way.

The report recommends looking at household income, consumption and wealth rather than National Production for a better reflection of material living standards. It brought back focus on the long held view that GDP can't measure economic welfare. The report, for instance, quotes a study by Professor Richard Easterlin to suggest that in spite of a 3 % increase in the American GDP per capita between 1972 and 1993, the share of individuals who were "very happy" did not increase. Economists call this lack of correlation the 'Easterlin Paradox'.

Instead of GDP, a better measure of welfare, observe Stiglitz and Sen, is household consumption. In 1989, Herman Daly and John B.Cobb fine -tuned this concept, proposing the Index of Sustainable welfare (ISEW). Unlike GDP, which simply adds together all expenditures, ISEW balances consumer expenditure by such factors as income distribution and cost associated with pollution and other unsustainable costs.

France, the leisure vacationer's paradise, has all the reasons to take the lead in shifting to such a measure for economic welfare. As does India with its vast force of home makers-cum-managers whose contribution to economic welfare GDP overlooks.

ISEW=CADT + P + G + W – D – E – N

CADJ Consumer spending adjusted for inequality.
P Public expenditures excluding defensive expenditure.
G Growth in capital and net change in interna tional position.
W Non-monetized contribution to welfare.
D Defensive private expenditures.
E Costs of environmental degradation.
N Depreciation of the environmental capital base.

Social INDICATORS (SI)

World Bank provides data up to 94 indicators including

1. Size, growth and structure of population
2. Determinants of population growth (including data on fertility and infant mortality
3. Labor force
4. Education and illiteracy
5. Natural resources
6. Income and poverty
7. Expenditure on food, housing, fuel and power
8. Transport and communication
9. Investment in medical care and education

Social Indicators are also complied by the statistics Division Department of Economic and social Affairs of the United Nations Secretariat. Indicators are provided on the following areas.

1. Child-bearing
2. Child and elderly population
3. Education
4. Housing
5. Health
6. Human settlements
7. Population
8. Unemployment
9. Water supply
10 Income and economic activity
11. Literacy
12. Contraception

Business Social Responsibility (BSR)

Business in the private sector is normally undertaken primarily to maximize private profits (=Total Revenue- Total private Costs). In the process of maximizing Private profits, businesses undertake those economic production activities for which there is maximum demand. In that sense businesses meet society's needs.

Social Responsibility is an ethical or ideological theory that an entity whether it is government, corporation, organization or individual has a responsibility to society. The responsibility can be "negative" meaning there is a responsibility to refrain from acting (resistance) or it can be "positive": meaning there is a responsibility to act (proactive stance)

Critics argue that corporate social responsibility(CSR) distracts from the fundamental economic role of business, others argue that it is nothing more than superficial window dressing; others argue that it is an attempt to pre-empt the role of governments as a watchdog over powerful multinational corporations.

Socially Responsible Business

Corporate Social Responsibility is a voluntary activity over and above the legal requirements of business. As such, it is a convergence of new ideas and practices (behaviors) that are impacting on management practice. Corporate Responsibility is a concept that applies to all the decision making processes and systems in a business. Corporate Responsibility must involve the decisions, actions, and behaviors of all people, at all levels throughout an organization, across all functions, and in all companies of all sectors.

CSR, also known as corporate responsibility, corporate citizenship, sustainable responsible business (SRB) or corporate social performance is a form of corporate self-regulation integrated into a business model. Ideally, CSR policy. Would function as a built-in self regulating mechanism whereby business would monitor and ensure their adherence to law, ethical standards, and international norms. Business would embrace responsibility for the impact of their activities on the environment, consumers, employees, communities, stakeholders and all other members of the public sphere.

For each business, different measures are taken into consideration to classify a business are taken to classify a business as "socially responsible". Each business attempts to reach different goals. There are four areas that should be measured regardless of the outcome needed: Economic function, Quality of Life, social investment and problem solving that is trying to be achieved should be measured to see if it meets with the cost guidelines that the business is willing to contribute.

Business of all sizes, in all sectors, and across many different countries is facing an increase in pressure, in order to make a positive contribution to the society beyond traditional economic benefits that are derived from corporate activities.

A general competency framework for corporate responsibility requires understanding of how the core business activities create opportunities for other actors in society, and how the company can contribute to the society. It also requires understanding of the social and environmental risks and opportunities of the organization.

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If an economy wants to achieve something beyond GDP it is important that businesses have to look beyond the objective of maximizing revenue, private profits, or market share

There lies the role of corporate social responsibility. The question arises should it be left to the businesses to be socially responsible or the state can play an active role in enforcing well set socially relevant goals.

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