From CSR Practices Towards Strategic Innovation: A Dynamic Capability Approach

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ABSTRACT

In an increasingly dynamic world, firms are being forced to become more innovative and adapt their activities, organizational structures, processes and products to reflect CSR policies. Firms can fulfill both social and business objectives by integrating CSR practices into their core business strategy as a strategic innovation investment. From the perspective of dynamic capabilities, CSR addresses the need for firms to be socially responsible and focus on innovative issues. When the model is properly specified, it becomes clear how to activate strategic CSR innovation to build competitive advantage.

Keywords: CSR Practices, Strategic Innovation, Dynamic Capability
INTRODUCTION

Drawing from both the resource-based view and the dynamic capabilities perspective, a firm must be capable of renewing, enhancing, and accommodating competencies over time (Teece et al., 1997). In a pioneering contribution to an emerging body of ‘dynamic capabilities’ literature, Teece et al. (1997) define ‘dynamic capabilities as the firm’s ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments’.

Companies need to innovate for many reasons, the most important of which is sustainable competitive advantage. The effort to link these two terms can be considered innovative in itself based on the Schumpeterian definition of an innovation as a new combination. Indeed, each successful company has developed a specific innovation solution based on its particular circumstances and constraints (Crosswhite & Rufat-Latre, 2009). To extract all of the business value implicit in an innovation, it must align with firm skills, processes, and other organizational building blocks.

What is the role of CSR in corporate strategic innovation? More businesses are operating transnationally, exceeding the boundaries of regulations intended to achieve compliance with CSR norms. This also makes it difficult for such firms to use their assets to create competitive advantage and to adjust organizational processes to transform their capabilities over time. This paper seeks to contribute to the development of strategic CSR innovation by combining CSR practices and strategic innovation. In addition, this paper makes a novel contribution in testing the link between innovation performance and inter-firm cooperation in association with CSR practices.

LITERATURE REVIEW

Corporate Social Responsibility

The most fundamental tenet of Corporate Social Responsibility (CSR) is that enterprises go beyond compliance and engage in ‘actions that appear to further some social good, beyond the interests of the enterprise and that which is required by law’ (McWilliams & Siegel, 2001). Based on the European Union definition of CSR, companies voluntarily integrate social and environmental concerns into their
business operations and their interaction with their stakeholders. The study of CSR has emerged as a prominent, serious discipline within the field of management, contributing to employee well being, to sustainability, and to competitive advantage. Ultimately, it also provides firms with many opportunities to work for the benefit of society. Numerous theories have developed around the CSR perspective. Here, some theoretical perspectives are developed in greater detail (McWilliams et al., 2006).

**Strategic Innovation**

Most companies agree that innovation is key to confronting frequent business changes. Two major concepts are central to strategic management – sustained competitive advantage and distinctive competencies. These qualities are necessary for organizations to develop firm-level strategies for how to sustain and safeguard existing dynamic capabilities. Innovation involves acting on creative ideas to make some specific and tangible difference in the domain in which the innovation occurs.

**Dynamic Capability Approach**

Dynamic capabilities are process-improvement techniques that create a way of modifying operating routines. The generation of capabilities requires sufficient experience for tacit organizational knowledge to become stored in new patterns of activity, known as routines (Teece et al., 1997). Teece, Pisano, and Shuen (1997) define dynamic capabilities as the competences necessary for firms to integrate, construct, and redesign their internal configurations and external capabilities to react to the rapid fluctuated environments. These processes delineated by firm assets are the essence of "dynamic capabilities" and competitive advantage (Teece, Pisano, & Shuen, 1997). In the taxonomy created by those authors, there are three categories of dynamic capabilities: positioning (sensing), process (seizing) and orientation (reconfiguring and transforming) (Teece, 2007).

Strategic CSR innovation is created within the frame of reference of management in personal and organizational values and sense-making processes. The dynamic capabilities framework analyzes CSR practices by private enterprise firms operating in environments characterized by rapid societal change. The competitive advantage of firms is seen as resting on distinctive innovation strategies shaped by
the firm's specific asset positions and the evolutionary path it has adopted or inherited. Identifying new CSR opportunities and organizing innovation management effectively and efficiently help to create private wealth, enhance business conduct, keep competitors off balance, raise rivals’ costs, and exclude new entrants.

Attempting to bridge the sensing, seizing and managing phases (Teece, 2007) by adopting a dynamic process approach and facilitating competitive advantage, and proper positioning in a variable system, this study reveals new strategic considerations and decision-making conventions. Thus, this framework helps to ensure that opportunities, once sensed, can be seized, and that businesses can be reconfigured when the market and or the technology is inevitably transformed once again. Then, the fundamental question in the field of strategic management is how firms achieve and sustain competitive advantage (Rumelt, Schendel, & Teece, 1994).

**Sensing and Shaping Opportunities - Corporate Social Responsibility**

For any organizations to fulfill CSR practices that just obeyed the law, regulations, legislation to achieve the social and economic goals are no longer satisfactory. In a fast-paced, globalized, and competitive environment, opportunities are everywhere and are open to both newcomers and incumbents. Hopefully, CSR can be combined with almost all of the existing elements within organizations for enterprises to identify and shape their own opportunities locally and distantly.

To uncover how CSR may help firms to identify and shape of opportunities, a brief review of the CSR literature is presented here. The study of CSR has risen to prominence within the field of management, contributing to employee well being, sustainability and competitive advantage. The core values underlying corporate social responsibility are the expectations that society holds regarding appropriate business behavior and outcomes. Wood (1991) describes three levels of CSR analysis: institutional, organizational, and individual. A fourth level, the global level, can be added in response to public concern about globalization.

**Proposition 1:** The firm must create particular CSR practices at different levels to maintain its social and business competences. (Figure 1.)
Institutional Level: Legitimacy

Firms consider CSR as a tool for acquiring organizational legitimacy. Adapting functional theory (Preston & Post, 1975), which specifies the various tasks carried out by specialized social institutions, firms further support their position and fulfill their obligations with regard to social responsibility due to their existence and operation in a shared environment. Using a different lens to investigate CSR, Freeman's (1984) stakeholder perspective indicates to whom businesses should be responsible. Firm self-interests also leads to the most efficient allocation of society's resources, and human beings make decisions and act on moral and rational economic (i.e., self-interested) grounds for the collective good. That is to say firms can use CSR to create a mutually beneficial relationship with their stakeholders and thereby ensure their legitimacy.

**Proposition 1a:** At the institutional level, the mutual impact of a firm’s relationship with its stakeholders can be reached by exercising CSR practices to ensure firm legitimacy and power to business.

Organizational Level: Public Responsibility

At the organizational level, businesses are responsible for performance related to social involvement with their primary and secondary areas (Wood, 1991). Primary involvement, behaviors and transactions are part of the firm's direct, specialized functional role, whereas secondary involvement entails effects that are not intrinsic to the character of the organization but are generated by its primary involvement activities (Preston & Post, 1975: 10-11). According to Freeman’s (1984) understanding of legitimacy and morals for firms, social considerations are no longer separate from organizations but instead now contribute to their sense of purpose. CSR has connected the question of public responsibility with issues of stakeholder identification, involvement, and communication, the legitimacy of corporate power, and the moral dimension of managerial decisions.

**Proposition 1b:** At the organizational level, a firm can take public responsibility to define particular CSR practices as part of corporate identification, stakeholder communication, and commercial opportunities.
Individual Level: Moral Choices of Managerial Discretion

Corporate social responsibility extends beyond firms’ economic, legal, and ethical responsibilities (Carroll, 1979). Under Ackerman’s (1975) vision of CSR accountability, managerial discretion in ensuring CSR has typically involved not only philanthropy or community involvement programs but also decisions that impact managerial actions and choices overall. At the individual level, a firm’s social responsibilities are fulfilled by certain individual moral actors, managers, who constantly make decisions and choices (Wood, 1990). Although managers are constrained by their work environment, they must weigh the moral consequences of the choices that they make.

**Proposition 1c:** At the individual level, moral considerations affect managerial decisions and thereby support the enterprise’s CSR practices in certain constrained work environments.

Global Level: CSR as the Sustainable Developmental Strategy

CSR as a sustainable development strategy makes sense for business as more and more enterprises begin to relate it to their organizational values in a globalized environment and international initiatives. Corporations are establishing a clear link between their business objectives and the global concerns of contemporary society, including poverty, climate change, obesity, sustainable energy, etc. More recently, CSR has emerged as a core strategic mode that is central to value creation. It is becoming part of the core strategy for firms, developing into a business megatrend with a global reach. The central insights of businesses also involve strategic CSR practices, extending the responsibility of firms globally and expanding the reach of social, environmental and economic concerns so that they are strategically included the core strategic model as a factor influencing sustainable development and competitive dynamic capabilities.

**Proposition 1d:** At the global level, a firm must utilize specific CSR practices to sustain its innovative competitive advantage in increasingly demanding environments.
Seizing Opportunities – Organizational Strategic Innovation

Innovation, like many business functions, is a management process that requires specific tools, rules, and discipline. Innovation management strategy involves not only new ideas that enable a firm to perform better in existing business areas but also ideas that help the firm to explore related new business areas. But how does this innovation strategy must forget much of what has helped the company thrive but at the same time must leverage its resources? How can firms maintain sustained competitive advantage and distinctive competencies? How can they enhance their fitness in dynamic environments? The answer may be to create appropriate organizational innovation strategies that will contribute to an enterprise’s competitive advantage.

Strategic innovation is the creation of growth strategies, new product categories, services or business models that change the game and generate significant new value for consumers, customers, and corporations (Palmer & Kaplan, 2007). Emphasizing strategic innovation as part of the unique capability approach, which is intensely relevant in a Schumpeterian world of innovation-based competition, Schumpeter argues that firm innovation and technological change come from the wild
spirits from creative individuals and from organizational capacity for change and adaptation.

**Proposition 2:** Organizational strategic innovation is deeply rooted in a firm’s ability to drive innovation, identifying, analyzing, and selecting possible innovations and then implementing them internally or through business ventures under different circumstances. (Figure 2.)

**Types of Innovation Management Strategy**

This study considers the impact of four types of innovation on firm capabilities: incremental, radical, sustaining, and disruptive innovation. Different innovations reinforce the capabilities of established organizations and force them to ask new questions, draw on new technical and commercial skills, and employ new problem-solving approaches. Therefore, based on different environmental fluctuations, industrial trends, and technological changes, different innovation management strategies are adopted to sustain firm competitive advantage and business competences.

Starting with organizational creativity and gradually working toward **incremental innovation**, firms improve and restructure existing products in minor ways, improve established designs, and help to maintain their market and technological leadership (Henderson & Clark, 1990). To be more specific, incremental innovation introduces relatively minor changes to existing product, exploits the potential of established designs, and often reinforces the dominance of established firms.

**Proposition 2a:** When the aim is to restructure processes and functions within an organization, incremental innovation strategy is often utilized. This type of innovation uses considerable skill and ingenuity and, over time, has very significant economic consequences.

In contrast, **radical innovation** often creates the basis for the successful entry of new firms or even the redefinition of an industry, opening up whole new markets and potential applications. Most often, new or small companies making radical innovations have the capacity to dominate the market and/or technology or even create new industries on their own. Established corporations must adjust or perish, and survival often means learning new technical skills as part of radical innovation and investing in research, development and engineering or retooling in the supply chain. Investments in manufacturing, marketing, and other aspects of the business are also necessary.
**Proposition 2b:** When firms seek to differentiate themselves from others in an industry to gain sustained competitive advantage, radical innovations are made to systems. This is visible in business models, processes, operations and project management models, and quality management systems for new, small or established companies, depending on the firm’s strategic management orientation.

When an organization begins to develop and institutionalize a cultural mindset and a set of processes that support repeatable innovation, the organization also starts to build a foundation for ongoing competitive advantage. Bower and Christensen (1995) point out that *sustaining innovation* means maintaining a certain rate of improvement, bringing a better product or service to market at a lower price that has the attributes that the firm’s best customers already value. In other words, sustained innovation can be incremental, radical or both. Some sustained innovations are simple, incremental, year-to-year improvements, whereas others are dramatic breakthrough.

**Proposition 2c:** When established firms discover that it is difficult to respond properly to new business trends, they develop sustained innovations in the existing market to seek new growth, providing higher-quality products at lower prices than were previously available.

A *disruptive innovation* (Christensen, 1997) provides a product that is initially not as high quality as existing products in the current market and that cannot be sold to mainstream customers as a result. However, because such a product is simple, is more affordable, and exceeds the requirements of certain market segments, it gains a foothold in the market. In this way, a disruptive innovation can create a new market by targeting non-consumers or competing at the low end of an established market. A disruptive innovation cannot be regarded as a breakthrough in a technological sense; however it disrupts and redefines a firm’s capabilities, allowing the firm to extend its specific market niche.

**Proposition 2d:** When firms seek to build new-growth businesses or see an opportunity to create new market space, they can try to beat their competitors by taking over the market share of incumbent firms with disruptive innovations that allow them to either create or nurture new markets, potentially winning an incumbent’s worst customers.
Managing Reconfiguration and Transformation - Strategic CSR Innovations

Reconfiguration and transformation refer to the ability of firms to change internally in tandem with changes in the environment, to sense the need to reconfigure their asset structures, and to achieve necessary internal and external transformations (Amit & Schoemaker, 1993; Teece et al., 1997). In core strategic CSR innovation, CSR becomes part of central value creation and core strategy. That is to say, firms must explore the challenges and opportunities associated with CSR practices and strategic innovation.

Corporations must also bear in mind that innovation is one of the key factors underlying the achievement of CSR objectives and ensuring a firm’s survival (Hart & Milstein, 2003). Cultivating a deeper level of CSR engagement means going beyond defensive and proactive approaches to address the needs of the firm’s constituents as a whole. CSR-focused innovation seeks to provide commercial value and address societal challenges at the same time. The notion of ‘innovation as a social/corporate responsibility’ shows that innovation and CSR can provide opportunities for innovative organizations to become more corporately and socially responsible. This combination is the essence of core strategic CSR innovation.
The Link Between CSR Practices and Strategic Innovation

There has been an urgent appeal for profit and non-profit organizations to incorporate responsible practices into their business activities. To achieve this goal, organizations are beginning to manage their social, environmental and economic needs using socially responsible practices. Practical product design and development work becomes key, one aspect of which is innovation. Innovation is a function of individual efforts and organizational systems used to facilitate creativity.

In sum, if organizations do not take CSR into account, they may not survive because they may fail to innovate (MacGregor et al., 2007). Firms conjecture that design may form the basis for the link between innovation and CSR. In the same way, maintaining CSR initiatives can lead to innovation through the use of social, environmental, or sustainability drivers to create new products and services.

**Proposition 3:** Those enterprises that possess the capacity for innovation can benefit society but are also encouraged to seek opportunities to seize commercial opportunities, maintain their social and business competences, and sustain their innovative competitive advantage strategies in increasingly demanding environments. (Figure 3.)

**Strategic CSR Innovation – From Cultural Perspective**

CSR practices and strategic innovation require an organization with a well-established foundation in the form of organizational culture. Culture consists of values and norms that either drive or fail to drive organizational change. A company must be cognizant of its position, including assumptions about the competitive arena, customers, suppliers and technology. Companies must create a culture with a deep sense of discovery and encourage decision-makers to explore new perspectives.

**Proposition 3a:** The higher the level of agreement and cultural cohesion regarding CSR strategic innovation at a firm, the greater the chance for innovative ideas to be generated and implemented as part of CSR.

**Strategic CSR Innovation – From People Perspective**

Strategic CSR innovation requires a broad-based perspective; dialogue about strategy should cross functional and hierarchical boundaries, and people outside the company should be consulted for an
outsider’s perspective, whether it be that of stakeholder, consumers or users. How companies assume its constituents – workers, customers, suppliers, and local community organizations, among others – in planning strategic CSR innovation is the key to the success of the endeavor. Indeed, people can be moved in and out of organizations to some extent, and as long as the internal processes and structures remain in place, performance will not necessarily be impaired.

**Proposition 3b:** The lesser discretion of people from inside and outside the company in CSR strategic innovation, the better the chance that innovative ideas will develop and be implemented as part of CSR practices.

*Strategic CSR Innovation – From the Process Perspective*

A strategic CSR innovation process combines parts of the following two positions. First, the boundaries of (conventional) strategic thought must be expanded to develop a rich menu of non-traditional strategic options. Second, CSR ideas and options should be analyzed, and senior management should determine strategic boundaries to create coherence and consistency. Thus, strategic CSR innovation outputs can be considered to include firm-specific assets, a process of creative exploration, and ‘a growth-visioning and synthetic process’ (Teece et al., 1997). Examples of processes include quality, miniaturization, and system integration in tandem with CSR innovation. Such competences are typically viable across multiple product lines and may extend outside the firm to alliance partners.

**Proposition 3c:** The better the combined strategic CSR innovation process, the better the chance for companies to develop specific competences and sustained competitive advantages via CSR practices.

*Strategic CSR Innovation – From the Resource Perspective*

A company should generally leverage its existing resources: i.e., its assets and capabilities. According to the resource-based view, companies see business opportunities through the lens of their existing assets and capabilities, whereas the dynamic capabilities view of the firm would suggest that the behavior and performance of particular firms may be quite difficult to replicate, even if they are
coherent and rational. When firm-specific resources are rare, valuable, imperfectly imitable, and characterized by the absence of another strategically equivalent resource or equivalent substitutes, superior business performance can be achieved (Barney, 1991). When a firm that is strategically innovative in terms of CSR does often leverage existing assets and capabilities, it assesses business opportunities without being limited by where it is at a given moment. Strategic CSR innovators not only focus on matching internal resources with outside opportunities but also create strong relationships with a network of partners with complementary capabilities.

**Proposition 3d:** To ensure that the future of firms that develop CSR-based strategic innovations will not be restricted by corporate capabilities, internal resources must be built up very carefully, and emphasis should be placed on the development of external networks. A strong network of partners will complementary assets and capabilities supplements internal resources.

**Figure 3.**

*Managing Reconfiguration and Transformation*

![Diagram](Based on “Combination, reconfiguration and asset protection skills” (Teece, 2007)*)

**CONCLUSIONS**

In this paper, the 'dynamic capabilities' approach is used to stress the need to exploit existing internal and external firm-specific CSR and innovation competences in response to changing environments. The links between CSR practices and strategic innovation are proposed to be tied to new strategic
considerations and the decision-making discipline needed to ensure that enterprises sense, seize, and reconfigure their opportunities differently when the market and/or the technology inevitably changes once again. The dynamic capabilities approach views competitive advantage as existing in a Schumpeterian world that requires innovations and new combinations; indeed, innovation is central to Schumpeter’s vision and his conception of firm strategy.

Based on capabilities rooted in high-performance routines that are themselves embedded in firm processes and conditioned by firm history, businesses require sensing, seizing, and reconfiguring/transformational capabilities or mechanisms if they wish to build and maintain competitive advantage. In suitable business models, the creation, integration, and commercialization of a continuous stream of strategic CSR innovation must be consistent with customer needs and technological opportunities. In this paper, the dynamic capabilities framework (see Appendix A.) integrates and synthesizes concepts and research findings from CSR, strategic management, innovation studies, and elsewhere. This framework moves beyond traditional approaches to help develop our understanding of competitive advantage, emphasizing the traits and processes needed to achieve good positioning in favorable industrial and economic environments.

Using the dynamic capabilities approach, firms can identify more transmission mechanisms that link CSR practices with strategic innovations. Managerial creativity, organizational innovation, dynamic sustainability, cost effectiveness, corporate social responsibility and the reputational approach also play important roles in shaping CSR strategic innovations. Hence, the effort to seek and improve firm-specific competences, capture and develop new market domains, sense and seize opportunities, and reconfigure assets and resources plays a vital role in forming and shaping sustainable competitive advantage.

REFERENCES


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Appendix A. Foundations of Dynamic Capabilities and Strategic CSR Innovation

**Sensing and Shaping Opportunities**

- Institutional CSR Practices
- Managerial CSR Practices
- CSR as an Analytical Tool for Sensing and Shaping Opportunities
- Organizational CSR Practices
- Global CSR Practices

**Seizing Opportunities**

- Incremental Innovations
- Radical Innovations
- Organizational Innovation Strategies for Seizing Opportunities
- Sustained Innovations
- Disruptive Innovations

**Managing Reconfiguration and Transformation**

- Cultural Perspective
- People Perspective
- Strategic CSR Innovation for Creating Sustainability and Building Competitive Advantage
- Process Perspective
- Resource Perspective

*Based on Teece (2007)*