EconomEtica

Centro interuniversitario per l'etica economica
e la responsabilità sociale di impresa
promosso dalla Fondazione Italiana Accenture

N.33 November 2011

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Voting with the Wallet

Working papers

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Abstract

The *vote with the wallet* is a new, emerging feature of economic participation and democracy in the globally-integrated market economy. This expression identifies the pivotal role that responsible consumption and investment can play in addressing social and environmental emergencies which have been aggravated by the asymmetry of power between domestic institutions and global corporations. In this paper, we examine (both in general and by using examples drawn from the financial and non-financial sectors) how "voting" for producers which are at the forefront of a three-sided efficiency which reconciles the creation of economic value with social and environmental responsibility, may generate contagion effects by triggering ethical imitation of traditional profit-maximizing actors, thereby enhancing the production of positive social and environmental externalities. Within this new framework policies which reduce the search and information costs of voting with the wallet may help socioeconomic systems to exploit the bottom-up market forces of other-regarding preferences, thereby enhancing opportunities to achieve well-being with reduced top-down government intervention.

Keywords: social responsibility, other regarding preferences.

Acknowledgment: I thank F. Adriani, S. Anderson, M. Bagella, K Basu, F. Bourguignon, R. Cellini, L. Debenedictis, T. Ellingsen, M. Fenoaltea, P. Garella, I. Hasan, L. Lambertini, S. Martin, C. McIntosh, T. Picketti, N. Phelps, G. Piga and P. Scaramozzino, M E. Tessitore, P. Wachtel, C. Whilborg, H. White, B. Wydick and all participants in seminars held at the XV Villa Mondragone Conference, at SOAS in London, at the Copenhagen Business School and the Universities of Catania, Bologna, Macerata and Milano Bicocca, and at the 2008 Poverty and growth network conference in Accra for the useful comments and suggestions received. The usual disclaimer applies.

1. Introduction

The standard textbook economic theory generally represents individuals as adopting purely self-regarding behaviour, or, more specifically, as maximizing their own monetary payoffs. This simplified paradigm has been strongly criticized by Amarthya Sen (1978), among others, who argues that *homo economicus* is a "rational fool", and that the reductionist assumption that individuals are driven only by their own monetary self-interest disregards the importance of two additional drivers of human behaviour - moral commitment and sympathy.[1]

[1] The issue has been dealt with, not without a certain amount of irony, by a number of well-known social scientists: Hayek called *homo economicus* the "family shame", and Frank stated that he would not let his daughter date a *homo economicus*.

Do people really behave like *homineseconomici*? Empirical findings from Ultimatum Games (Güth, Schmittberger and Schwarze, 1982, Camerer and Thaler 1995), Dictator Games (Andreoni and Miller 2002), Gift Exchange Games (Fehr, Kirchsteiger and Reidl, 1993, Fehr, Kirchler, Weichbold and Gächter 1998), Trust Games (Berg, Dickhaut and McCabe 1995, Ben-Ner and Putterman 2006), and Public Good Games (Fischbacher, Gächter and Fehr 2001, Sonnemans, Schram and Offerman 1999, Fehr and Gächter 2000) provide evidence which contradicts this simplified paradigm. Results from this research have documented, in fact, that the vast majority of the individuals participating in the experiments follow a broadened preference pattern which includes elements of (positive and negative) reciprocity (Rabin, 1993), inequity aversion (Fehr and Schmidt, 1999, and Bolton and Ockenfels, 2000), other-regarding preferences (Cox, 2004), social welfare preferences (Charness and Rabin, 2002), and various forms of pure and impure (warm glow) altruism (Andreoni, 1989 and 1990).

For the more sceptical, who believe that laboratory behaviour is an imperfect proxy for what people do in reality, the preferences revealed by actual consumer choices are a more reliable proof for the existence of other-regarding preferences. From this point of view, quasi-natural experiments on consumer purchases and the actual market shares of "ethical" products, which are generally sold at a positive price differential compared with equivalent "non-ethical" products (see Sections 2 and 3), represent the most important evidence for rejection of the anthropologically reductionist paradigm of the "rational fool".

Even more importantly, this theoretical and empirical literature documents that the presence of asymmetric information, contract incompleteness and limits to the enforcement of legal obligations make social dilemmas an everyday feature of economic life. These dilemmas, which are conventionally represented in Prisoner's Dilemmas, Trust Games, and Public Good Games, are typical situations in which pecuniary self-interest is not just uncommon from an empirical point of view, but is also sub-optimal in terms of the creation of economic value. This is because, in most of these dilemmas, team or other-regarding preferences and high levels of trust and trustworthiness may allow players to reach equilibria which are superior from both an individual and an aggregate point of view.[2] Based on these considerations, economists are becoming increasingly interested in studying the law of motion of crucial values which induce people to accept "social risk", such as trust, and, more generally, social capital, which is considered to be the 'glue' which holds the socioeconomic system together.[3]

[2] A further paradox is that when facing social dilemmas even game theorists do not follow Nash rationality (see Becker et al. 2005 findings on the traveller's dilemma)

[3] The multifarious concept of social capital includes trust, and is defined in the literature in different ways. Putnam (1993:167) defines it as "*social organization, such as trust, norms, and networks that can improve the efficiency of society by facilitating coordinated actions*", while Guiso et al. (2008) define it as "*the set of beliefs and values that foster cooperation*." According to Hong and Bohnet (2007), "*trust… consists of the investor's willingness to make herself vulnerable to others' actions*" while Fehr (2009) argues that "*an individual (let's call her the trustor or investor) trusts if she voluntarily places resources at disposal of another party (the trustee) without any legal commitment from the latter*".

This increased attention to invisible pillars of economic life such as social capital confutes the widespread belief that values are unimportant for, if not actually harmful, to, economic life. This belief has been fuelled by a simplistic extrapolation of the famous passage in Adam Smith's "Wealth of Nations", which explains how market mechanisms act as an invisible hand which magically transforms the pursuit of individual self-interest by each economic agent into something which is also socially desirable. As well known, the exceptions to the coincidence of private and social optimum are so numerous that they have become the rule. Natural or imposed limits to competition, negative externalities, public goods and asymmetric information are so widespread and pervasive that they severely limit the benefits of the invisible hand, and make the coincidence of private and social optimum an ideal situation which cannot be attained, just like the benchmark of frictionless motion in physics.

Another well-established metaphor in support of the optimistic view of the sufficiency of self-interest may be found in Mandeville. In the bee story, socioeconomic systems prosper like beehives simply because of the spontaneous coordination of self-interested actions by their inhabitants, while the introduction of values may even prove harmful, and endanger this spontaneous equilibrium. Even Keynes indirectly refers to this idea when he admits that "*for at least another hundred years we must pretend to ourselves and to everyone that fair is foul and foul is fair; for foul is useful and fair is not. Avarice and usury and precaution must be our gods for a little longer still. For only they can lead us out of the tunnel of economic necessity into daylight*."[4]

However, the increased economic interdependence generated by global market integration and the complexity and growth of financial markets provides quite the opposite picture, according to which a lack of ethics on the part of a single financial trader in a "too big to fail" financial institution may trigger a worldwide catastrophic event (a quite different position from that of Mandeville's libertine who, with all his vices, only creates positive economic effects).[5] If we return to Mandeville's metaphor, it is as if the bees (or at least some of them) were now transporting small nuclear weapons with their tiny legs, so that their lack of moral and civic values may endanger the survival not just of their own hive, but also of all the neighbouring ones.

If we now take this into account, and add the fact that the global financial crisis has demonstrated how important trust is among and within financial institutions for the survival of the market economy, we might rephrase our quotation from Keynes by arguing that in globally-integrated markets, foul is dangerous, while fair is becoming useful, since it contributes to the creation of economic value (as we shall see in the sections which follow).

On the positive side, the potential contribution of values and ethics to the increased prosperity of economic life in globally-integrated markets has only just begun to be explored. The imbalance generated by the interaction of globalized companies with institutions and rules which have remained largely national in nature has triggered a bottom-up reaction from a minority of "concerned" individuals who have started to "vote with their wallets". These individuals use their

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[4] John Maynard Keynes, "The Future", *Essays in Persuasion* (1931), Ch. 5

[5] Examples of this are the constant financial scandals (SocietéGenerale, Madoff, Parmalat, Enron) of recent years.

consumption and savings choices to vote for those products and companies which are at the forefront of a three-sided efficiency which consists of creating economic value in a socially and environmentally responsible manner. The spread of this practice has been supported by the fact that socially responsible consumption and savings impose only very weak conditions on individual preferences. We do not need a strong dose of altruism to vote with the wallet, merely a form of enlightened or long-sighted self-interest. This is because purchasing products from firms which are at the vanguard of environmental sustainability means supporting innovation towards more environmentally responsible productive processes, or providing incentives for a reduction in environmental degradation and its harmful consequences which produce negative effects not just for future generations but also for the concerned consumers and investors themselves. In parallel, choosing a socially-responsible product implies supporting those firms which are more efficient in reconciling the creation of economic value with the well-being of their workers: a goal which, in the end, is in the interests of concerned consumers who wish to maximize their surplus, but whose satisfaction is affected even more by the enjoyment of decent working conditions. This grassroots action has successfully triggered a reaction from corporations which have found it optimal to imitate partially the behaviour of socially responsible pioneers. This reaction has been termed "corporate social responsibility" (CSR). The main questions here are what the consequences of CSR might be for a company's shareholders, and whether companies can afford CSR while at the same time having to survive and remain competitive in the market arena (see Section 4).

The aim of our paper is to reflect on these new features in economic systems by analysing in depth the interaction among the three "new" actors: corporate ethical pioneers, concerned economic agents who vote with their wallets, and profit-maximizing incumbents who are moving towards corporate social responsibility.

The paper is divided into five sections (introduction and conclusions included). In the second section, we examine the idea of the bottom-up action of the wallet vote in general by considering its potential and the threats it might pose. In the third section, we consider its application to the fields of trade (fair trade) and finance (microfinance, ethical banking and ethical finance), stressing the isomorphic nature of certain crucial elements of the economics of social responsibility in the two domains: in both cases, the emergence of small market shares enjoyed by new-entry ethical pioneers (whose products are purchased by "concerned" consumers voting with their wallets) triggers partial imitation on the part of profit-maximizing incumbents, thereby generating important contagion effects. In the fourth section, we analyse the phenomenon of corporate social responsibility as a reaction triggered by the existence of the socially and environmentally responsible consumers and investors described in the previous sections. In the final section, we draw some conclusions.

2. Voting with the wallet: the potential of, and limits to, the bottom-up action of concerned consumers and investors

We are on the eve of a new phase in the evolution of economic democracy. To date, bottom-up participation has been mainly limited to political voting. In a metaphorical sense, this limitation corresponds to a situation in which mankind has been walking awkwardly by hopping on one leg.

The emergence of the “vote with the wallet” corresponds to a revolution in which human beings are learning to walk much more easily by using the left and right leg one after the other.

Why has this form of bottom-up action emerged only in recent decades? The explanation is simple. Before globalization, the balance of power among domestic governments, trade unions and corporations ensured the joint pursuit of economic growth and social cohesion. With global market integration, corporations have suddenly acquired the option to delocalize production to places where social and environmental obligations (and related costs) are lower. Institutions and trade unions have remained local rather than becoming global. They have therefore lost bargaining power and have become largely unable to counter the “race to the bottom” threat raised by globalized corporations. One example of how this transformation changes in-depth relationships among the three powers is provided by the role and effectiveness of strike action. If strikes might have been effective during the pre-global era in demonstrating the muscle of the unions and increasing their bargaining power, in the era of globalization they have become useless, or even harmful, as instruments for defending the labour rights of unskilled workers in high-income countries who work in industries which sell tradable goods. This is because in globally integrated economies, any success that they may have simply ends up by increasing the labour cost differential of production in high- or low-income countries, and therefore increases the probability that companies will delocalize, or else lose their competitiveness if they remain in high-income countries.

This is one of the reasons why in this modified scenario citizens have become progressively more aware of the need to move “from the streets to the shop”, acknowledging that their bargaining power can be regained by using their wallet vote to affect shares of corporate consumption. A minority of engaged and concerned consumers is becoming increasingly aware that a wallet vote is more effective than a political vote, given that even very small changes in terms of sales and market share can have a powerful impact on corporations. This is because for these corporations, small shortfalls on their target sales or expected earnings can generate significant negative effects on their stock market value, or on the reputation and survival of their managers. In simpler terms, if only a few individuals change their political vote, nothing will happen, while if only one goes to his/her bank and says s/he wants to move his/her account to another bank for social and environmental reasons, the branch director will try to persuade him/her not to do so, because this decision will impact on his/her performance and bonus.

One crucial point is that, in spite of our introductory discussion on the limitations of the restrictive *homo economicus* paradigm, and the need to broaden it , the strength of the vote with the wallet lies in the fact that it does not require extreme departures from self-interested preferences, since it is not a matter of altruism, but more simply of long-sighted self-interest. Buying an environmentally responsible product is to send a signal of approval through the market to those companies which are more effective in reconciling the creation of economic value with environmental responsibility, or which are more efficient in waste management and the abatement of pollution, and therefore contribute to reducing pollution and its harmful consequences on health and global warming. In this sense, voting with the wallet for a more environmentally-responsible company means pursuing one’s own long-sighted self-interest, given that environmental degradation can no longer be considered a matter for future rather than current generations.

In the same way, using one's purchases to show approval and economic consensus in regard to a company which is at the forefront in reconciling standard economic efficiency with social responsibility and care for workers' rights is an important action which creates incentives to increase the level of corporate attention to workers rights by rewarding this attention economically. This implies that concerned consumers who vote with their wallets are contributing to their own interest in enjoying decent working conditions as workers. We may state with certainty, in fact, that if an influential share of consumers were to become aware tomorrow of the potential of the vote with the wallet, and if, say, 50 percent of consumers supported firms at the forefront of the three-sided efficiency owing to their ability to create economic value in a socially and environmentally responsible manner, the world would change.

What, therefore, are the problems which prevent people from doing something which is ultimately in their own interest, and from thereby achieving an improvement in their well-being which seems to be within reach? The three main hurdles to achievement of this goal are coordination failure, information, asymmetry, and search cost differentials.

According to the first of these factors, in order to be effective, the act of voting with the wallet must be pursued by a large number of consumers at the same time. Let us imagine, as is often (but not always) the case, that this action entails a cost which is represented by the positive price differential between an "ethical" and a standard product which are otherwise identical. In this case, we face a multi-player prisoner's dilemma, where the payoffs are such that the socially responsible choice is Pareto-superior, if, and only if, a certain number of other consumers follow the same course of action. The cost differential paid by the concerned consumers is, in fact, more than offset by moves in a socially and environmentally responsible direction by the company involved and the economy (moves which are in the interest of the consumer), but only if the share of those voting with their wallets is sufficiently (minimally) high. If, on the other hand, each player expects the others to pursue short-sighted self-interest and buy the standard product, we end up in a suboptimal Nash equilibrium in which everyone finds it optimal to buy the standard product, and the market incentive which might stimulate companies to behave in a socially and environmentally-responsible manner is not produced. Expectations such as these are likely to be realized simply because social responsibility is not common knowledge, or because concerned consumers may think that other consumers are not aware of this opportunity (or that they are aware of it, but are short-sighted). This is a typical case in which a lack of hope and trust is self-fulfilling. Furthermore, just as in the standard prisoner's dilemma, the vote-with-the- wallet game is simultaneous and non-cooperative (it is impossible for all participants to coordinate their actions in advance), and this further reduces coordination opportunities. Needless to say, this is a multiplayer and not a two player game and the presence of a vast number of people makes coordination of a vast number of people even more difficult to achieve.

The second main problem, asymmetric information, plagues the social responsibility market as it does almost all other situations in economic life. The effect of asymmetric information in second-hand sales, job hiring and credit markets has been extensively analysed in the economic literature for decades.[6] The main pathologies it can create (moral hazard, adverse selection) can be solved

[6]Three essential references on asymmetric information are those of the three authors who jointly received the Nobel Prize for research in this field: Akerlof (1982) for moral hazard and the market

only if a counterpart with superior information has effective signalling strategies available. In our case, the seller has superior information about the ethical quality of the product. This characteristic is not, unfortunately, an experience good: that is, a feature by which asymmetric information can be eliminated by purchasing and tasting the product. In other words, if a consumer drinks more cups of socially responsible coffee, she makes no progress in her evaluation of the effectiveness of the seller in addressing social and environmental issues. This is the reason why a large number of labelling companies and rating agencies have been born in the "ethical industry". The survival of these companies depends on their reputation for producing reliable and accurate evaluations of the ethical stance of the firms that they observe. However, since their revenues are often correlated with the volume of labelled or rated ethical products sold, these organisations are often supposed to be erring on the side of leniency, especially toward large companies. A further limitation is that small firms may find the fixed costs of certification or monitoring unaffordable, so that they tend not to be rated. This results in a negative reputation signal being unintentionally sent to the market.

Finally, search cost differentials also play a role. It is often the case that ethical products are not as widely distributed as standard products. This implies that consumers who want to vote with their wallets are forced to pay additional search costs.

Coordination failures, asymmetric, information and search cost differentials are the three main factors which can explain the gap between the potential and effective market shares of ethical products sold by socially and environmentally responsible companies. A significant number of consumer surveys have documented the extremely large share of citizens who prefer ethical to standard products.[7] In principle, ethical responsibility acts like technological progress in vertical differentiation models: *coeteris paribus,* the addition of an ethical characteristic should shift all consumers toward the ethical product, exactly as in the case of new technology. Consumer surveys document, however, that even if a cost differential exists, the share of consumers willing to buy the ethical product remains high. This is perfectly rational, and compatible with a situation in which the satisfaction of other-regarding preferences (including forms of inequity aversion, reciprocity and pure or impure altruism) more than compensates for the cost differential between the two products. However, as well known, the contingent evaluation literature (Carson et al. 2001) has widely documented the existence of an upward bias in these declarations, since the individuals interviewed have had no problem in declaring that they are ethical in principle if this declaration entails no costs. This is why real-life situations, in which consumers actually choose between the two products, provide much more reliable figures on the actual willingness of consumers to vote with their wallets.

The recent studies most interesting from this point of view have included measurements of an actual willingness to pay in quasi-natural experiments. Hiscox and Smyth (2010) attached information on a corporate socially responsible stance to the display case of a candle seller in *ABC Carpet and Home* in New York, a store visited by more than 22,000 consumers every week. Another candle seller had its window just opposite the first one, and adopted the same social standards, but did not

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for lemons, Stiglitz for efficiency wages inlabour markets(Shapiro and Stiglitz, 1982), and Spence (1973) for signalling models.

[7] See, among others, consumer surveys from Italy (IREF), the UK (Bird and Hughes, 1997) and Belgium (De Pelsmacker, Driesen and Rayp, 2003)

advertise them in the experiment. The attractive element of this research is that the experimenters did not create an artificial laboratory environment. Instead, they slightly modified, with a "soft treatment", the standard scenario in which consumers found themselves when visiting the store. Furthermore, the treated and untreated products were so similar that search cost differentials were not a confounding factor. As should be the case in all experimental settings, this enabled evaluation (by comparing treatment and control) of the effect of the variation of a single characteristic (i.e. socially responsible advertising) on consumer behaviour. The experiment documented that the market share of the candles advertising their CSR stance rose by between 20 to 40 percent over the treatment period. The result persisted during a further treatment in which the same product was sold at a price which had been increased by15 percent.

In a different framework, Hiscox, Broukhim, Litwin and Volosky (2011) evaluated the effects on the willingness to pay and reservation prices relating to the CSR characteristics of products in online auctions on eBay. They showed that the treatment led to a 45 percent premium being paid on polo shirts. This implies that the treatment significantly increased the willingness to pay of the participant with the highest reservation price.

One main objection to the vote-with-the-wallet approach is that it implicitly legitimates market deregulation and the downgrading of standard political action. The answer to this objection is that grassroots action originates from an awareness that this loss of power is already an ongoing factor, and that grassroots action is intended to be a complement to, and not a substitute for, standard institutional and political action. Indeed, the grassroots action of voting with the wallet may give new bargaining power to political action. Unless we rely on the isolated actions of charismatic and enlightened political leaders, the likelihood of success for political action largely depends on bottom-up support from society. Cooter's (1988) well-known concept of an expressive law states that the effective enforcement and success of a legal rule depend on its consistency with the underlying social and moral norms of a society. Just as NGOs fighting the death penalty try to achieve their goal by convincing the majority of voters to be against it (and not just by trying to persuade political leaders), so creating a consensus for social and environmental responsibility may significantly increase the possibility of success of political actions.

Voting with the wallet also represents an important innovation which can improve the functions and "reputation" of the market. The well-known welfare theorems of neoclassical theory illustrate a fundamental benefit, but also a limitation, of market mechanisms. From the Edgeworth box we know that, starting from a given endowment of resources, the market enables individuals to find a Pareto-superior equilibrium through the exchange of goods or services. By definition, any market transaction between two agents with free will implies, if it is completed, that those who participate in the transaction are no worse off after than they were before it. However, certain transactions (such as, for instance, the extreme case of poor individuals who deliberately and freely agree to sell a kidney to improve their economic situation) do not contribute to the good reputation of the market, even though they still include the benefits discussed above (transactors with free will decide to make the exchange because they believe they will be no worse off after it has been concluded). This example reveals the limitations of the market: that is, its incapacity to affect inequality in the distribution of endowments through which economic agents arrive at a transaction.[8] Standard economic theory establishes that the inequality problem should be solved by institutions and their policies. However, (domestic) policies are generally oriented towards satisfying the interests of the median voter, and have difficulty with addressing the problems of the poor and global public goods. This is why concerned economic agents voting with their wallets may address both efficiency and equity issues with their consumption and investment choices by voting for products which promote inclusion and capacity-building for the poor. In this sense, a vote with the wallet may therefore make a positive contribution to the reputation of the market by partially amending this limitation, and enlarging the role and potential of market transactions. This is because, when socially responsible consumers buy an ethical product, they do not just enjoy the standard efficiency gains illustrated by the Edgeworth box but also contribute through their choice to the promotion of inclusion and equal opportunities for certain categories of transactors, thereby reducing inequality in the distribution of endowments.[9]

3. Socially responsible pioneers

One of the most important factors leading to the emergence of the economics of social responsibility has been the "alliance" between "concerned" consumers voting with their wallets and socially responsible non-profit-maximizing pioneers. Tiny market shares of products sold by such pioneers to responsible consumers have confuted both anthropological (individuals are 100 percent myopically self-interested) and corporate (only profit-maximizing firms exist and can survive on the market) reductionism, and made incumbent profit-maximizing firms aware of the potential of ethical purchases, thereby triggering their reaction, which takes the form of partial imitation. In the following sections, we briefly discuss the characteristics of these pioneers and ethical competition with reference to the specific cases of fair trade, ethical finance and microfinance. We would emphasize that we are interested in these specific cases here simply because they represent the most successful historical experiences related to voting with the wallet. It is, however, a much more wide-ranging concept, which will, in principle, be applicable to all areas of the market economy in the future. Finally, we discuss the features and potential of the competitive reaction from profit-maximizing incumbents which try to satisfy the increase in consumer sensitivity to the issue through their CSR strategies.

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[8] The kidney sale described above is, in fact, perfectly compatible with the Edgeworth box structure, with the only peculiar feature being that the endowment point is extremely close to the origin of the axis of one of the two transactors (meaning that the endowments with which the two agents arrive in the market are quite unequal).

[9] Note that, in order to examine the effect of this action in depth, we need to abandon the static analytical framework of the Edgeworth box. This is because any static analytical framework tends to fix individuals to their starting conditions, while only dynamic approaches may allow us to understand that policies of inclusion and promotion of equal opportunities may be dynamically convenient, even though they may appear statically inefficient (see also section 3.1 and the theoretical fair trade debate on this point).

3.1 Fair trade

Ropi is a small village in Ethiopia, located 320 km from the capital, and 70 km from the town of Shashemane. The village farmers produce wheat in the rainy season, but have no direct access to consumers. They are therefore forced to sell their crops to monopolistic intermediaries who take the product to Shashemane. In the rainy season, Ropi's farmers become net buyers of the very source of their living, and have to buy wheat from the same monopolistic intermediaries at a price which is usually double that of the rainy season. This is similar to that of other groups of producers, such as Kenyan farmers in Meru Central District and Tharaka, located approximately 200 km from Nairobi, on the eastern slopes of Mount Kenya (Becchetti and Costantino, 2008), and handicraft producers in the District of Juliaca (Department of Puno) located around Lake Titicaca. What this tells us is that poverty often results from a lack of market access, insufficient productivity, and low bargaining power which prevent producers from scaling the value chain. It also tells us that technological innovation *per se* does not solve the problem if it is not accompanied by an increase in the bargaining power and technological skills of these small, isolated producers.

Fair trade was born to address this issue, since it consists in the offer of an alternative distribution and sale channel to these groups, whose productive advancement is fostered by a price premium paid by consumers, and transferred by importers to the producers and their organisations in order to finance skill upgrading and local public goods. Fair trade can be therefore viewed as a means to promote the inclusion of marginalised farmers with a package of benefits which include, together with the price premium, improved market access, export services, price stabilisation, capacity building, environmental sustainability, and the provision of local public goods.[10] Fair trade products can be recognised by consumers from the label, which is available to producers' organisations if the overall value chain meets all the social and environmental standards specified in the fair trade charter.

Fair trade sales have grown significantly in the past decade. Between 2006 and 2007, total fair trade sales registered a 127% volume and a 72% retail value increase. Growth in Europe has been around 50% per year over the past six years. The Fairtrade Foundation documents that fair trade bananas have reached 50 percent of market share in Switzerland, and 25 percent in the UK, following their

[10] According to the IFAT (the main international organisation which gathers together producers and fair trade organizations), these criteria are: i) creating opportunities for economically disadvantaged producers; ii) transparency and accountability; iii) capacity building; iv) promoting fair trade; v) payment of a fair price; vi) gender equity; vii) working conditions (a healthy working environment for producers. The participation of children, if any, does not adversely affect their well-being, security, educational requirements and need for play, and conforms to the UN Convention on the Rights of the Child, as well as the law and norms in the local context); viii) the environment; ix) trade relations (fair trade organizations trade with concern for the social, economic and environmental well-being of marginalized small producers, and do not maximise profit at their expense. They maintain long-term relationships based on solidarity, trust and mutual respect that contribute to the promotion and growth of fair trade. Whenever possible, producers are assisted with access to pre-harvest or pre-production advance payment).

introduction into most supermarket chains.[11] Fair trade is interesting for the purposes of our research because it represents one of the most successful and well-established examples of alliance between not-for-profit corporate pioneers and concerned consumers who vote with their wallets. As such, it represents direct, non-experimental proof that the reductionist view of economic agents (as 100 percent myopically self-interested) and companies (whose only goal is profit maximisation) is a partial view of the reality.

Fair trade also represents an example of how consumption is becoming increasingly a symbolic action where the physical qualities of the product are only one of the reasons for making a purchase. Purchasing choices may be affected by the need to conform to a group (especially in the case of teenagers) or, on the contrary, by the need to distance oneself from the mass (when consumers search for exclusivity). More generally, by an act of consumption, consumers seek to satisfy complex preferences and their desire to buy goods which match their lifestyles. In this sense, fair trade products may be viewed as an interesting bundle in which a standard physical product is sold together with an intangible social and/or environmental content (Besley and Ghatak, 2007), where the latter component is fundamental for increasing the value of the bundle for consumers who cannot, however, verify its specific quality directly.

The theoretical literature attempting to analyse the pros and cons of this phenomenon has grown significantly over the past decade, although it is difficult to formalize its multiple characteristics in a single model, and a partial analysis of only one of them at a time runs the risk of misrepresenting the overall impact of the initiative (see, among others, LeClair, 2002; Maseland and De Vaal, 2002; Moore, 2004; Hayes, 2004 and Redfern and Sneker, 2002).

One main criticism of standard economic theory as applied to fair trade is that the price premium is a non-market clearing price which creates excess supply and provides the wrong kind of incentives to farmers. A second criticism is that, in a static partial equilibrium framework, producers may achieve the same level of satisfaction in an alternative scenario in which consumers buy a standard product without a price premium, and use the surplus to make a donation to the farmers (LeClair, 2002). The former criticism is valid only in a static situation in which there is equal bargaining power between demand and supply, while the Ropi story tells us that this is mostly not the case in the relationship between marginalised producers with no direct access to markets and monopolistic transportation intermediaries. In this latter case, even the standard textbook economic theory of monopsony tells us that market prices are suboptimal, and affected by this imbalance of powers, and that consequently higher prices may help to bridge the gap with socially optimal prices.

A second argument is that a fair trade product is not just the same non-ethical product sold at a price premium, but a completely different product, just as it is incorrect to consider organic and non-organic products to be the same goods with different prices. To be more precise, we might perceive fair trade as a *general purpose innovation* creating a new variety of products. In this conceptual framework, the price premium should be perceived not as a distortion, but as a different partitioning of value in the value chain between producers and importers (whose goals are detailed in the charter of fair trade principles). This innovation is exactly what creates additional demand for the final

[11]Consumers international (2010) Checked out: Are European supermarkets living up to their responsibilities for labour conditions in the developing world? Consumers international.

product, and it is justifiable if it satisfies consumers' ethical tastes (or insofar as consumers are willing to pay for it) (Becchetti and Huybrechts, 2008 and Becchetti and Costantino, 2010).

If we turn to the second criticism (that by LeClair), it must be observed that if we depart from a partial equilibrium static analysis, the fair trade circuit offers a number of advantages compared with the standard "purchase plus charity" pattern, the reason for this being that charity has no "antitrust effects": that is, it does not contribute directly (by opening a new distribution channel) to an increase in the bargaining power of marginalized versus monopsonistic intermediaries along the value chain. In addition, with the standard "purchase plus charity" pattern, there is no multipurpose innovation which creates a new range of products combining physical and ethical features, and satisfying the taste of "ethically concerned" consumers for variety and solidarity.

For these reasons, several more recent studies have demonstrated that fair trade, far from being a heresy, may contribute to solving certain market failures addressed by the standard economic theory. Along these lines, Reinstein and Song (2008) have developed a theoretical model showing how consumption by fair trade consumers is compatible with rational and informed behaviour which helps to address farmers' underinvestment problems in a competitive setting under asymmetric information. Poret and Chambolle (2007) provide additional theoretical evidence on the gains in efficiency which may potentially be achieved by fair trade through product differentiation. Last, Maseland and De Vaal (2002) document that under restrictive parametric conditions fair trade represents a first best over the alternatives of free trade and protectionism from the perspective of standard international trade models.

Beyond its limits a crucial aspect of the fair trade story is the capacity of this alliance between concerned consumers and corporate pioneers to trigger contagion, as also recognised in a recent document by the EU Commission.[12] When fair trade newcomers start retailing "public goods" (Besley and Ghatak, 2007),[13] they achieve small market shares. This result comes as a surprise to incumbent companies since, if we are to believe corporate and anthropological reductionism (section 3), there should be no space for fair trade deals in the market. The theoretical literature has documented that under reasonable parametric conditions, the not-for-profit pioneers trigger (partial) imitation on the part of profit-maximising incumbents, thereby providing a rationale for the phenomenon of corporate social responsibility (Becchetti and Solferino, 2010). In the specific case of fair trade, these models explain why large multinationals such as Nestlé, Starbucks, Sainsbury's and many supermarket chains have started producing, distributing and/or retailing fair trade products, while other multinationals such as Chiquita have introduced their own similar ethical standards.

What we have described above illustrates how the alliance between a vote with the wallet and corporate pioneers has transformed social responsibility into a competitive factor. The main issue of

[12]" *Fair Trade has played a pioneering role in illuminating issues of responsibility and solidarity, which has impacted other operators and prompted the emergence of other sustainability regimes. Trade-related private sustainability initiatives use various social or environmental auditing standards, which have grown in number and market share*." EU Commission 2009

[13]The industrial organization literature models competition in CSR by considering the latter an additional feature of the product (see, among others, Bagnoli and Watts, 2003 and Arora and Gangopadyhay, 1995).

interest today is the evolution of the competitive race between pioneers and imitators. By "decomposing" pioneers into three distinct actors - dedicated retailers (world shops), importers and labelling companies - we can see that their reactions to imitation by profit-maximising incumbents have been different.

The pioneers with the lowest levels of freedom (dedicated retailers) have strongly criticized any relationship with imitators by identifying it as a threat to their survival and to the "purity" of the fair trade movement. Importers, by contrast, have benefited from the opportunity to diversify their sales channels by accepting the possibility of selling to supermarkets as well, while opposing products with fair trade characteristics produced by imitators. At the other extreme, labelling companies have decided to place their labels also on imitators' products if they meet fair trade standards, even though fair trade products represent a tiny share of the imitators' revenues. The reaction of fair trade importers to this decision by the labelling companies has been to create a new label which advertises their "difference" and competitive advantage: that is, the fact that a given product comes from an organisation which is 100 percent dedicated to fair trade.

Far from being ideological, this is the optimal rational reaction of pioneers to the competitive threat raised by imitators. Imitators are generally much larger in size, and can easily replicate any specific product or initiative by the pioneers, and even engage in forms of social dumping (that is, selling fair trade products at a discount with respect to the pioneers) as a form of CSR policy. What they cannot do, if they continue to pursue profit maximisation, is convert more than a tiny part of their activity to fair trade standards, as this would dramatically reduce their margins. This is why the only possible optimal reaction of pioneers is to use a new label signalling to concerned consumers their unique competitive advantage, which cannot be replicated by imitators: their 100 percent dedication to fair trade.

3.2 Ethical finance

Ethically concerned investors may vote with their wallets by choosing ethical funds or ethical financial institutions, exactly as concerned consumers do by preferring to consume products from ethical pioneers or their closest imitators.

Financial intermediaries whose goals are not profit maximization are not the exception in the current economic scenario. As Canning et al. (2003) remark, in practice, even international organisations such as the World Bank and the International Monetary Fund operate like non-profit-maximizing financial institutions. In this section, we will briefly sketch three types of them, starting from the historical tradition of cooperative banks and then moving to the more recent examples of microfinance and ethical financial pioneers which directly create new opportunities for concerned investors to vote with their wallets, and promote three-sided efficiency through their financial support of projects and companies which create economic value in a socially and environmentally sustainable way.

The main historical differences between cooperative and standard commercial banks lie in governance (the one person/one vote rule, as against the one share/one vote rule), and in constraints on profit distribution whereby distributions cannot be cashed in by individual shareholders, and are accumulated in the form of capital reserves (anticipating the more recent concerns expressed in Basel II and Basel III rules for stricter capital requirements in order to prevent systemic instability and financial crises). These two features, accompanied by an attitude to proximity which aims at reducing asymmetric information and serving the needs of local investors, make their goals different from that of standard profit maximization. The cooperative banking system includes *banche cooperative* and *banchepopolari* in Italy, building societies and credit unions in the UK, and mutual savings and loans and credit unions in the US. Its role is by no means marginal. At a world level, financial cooperatives serve over 621 million people in the G-20 nations alone, provide US$3.6 trillion in loans, hold US$4.4 trillion of savings, and have US$ 7.6 trillion of total assets.[14] In 2007, cooperative banks had an average 25% market share of loans to small and medium enterprises (SMEs), while an average of 29% of their loans were SME loans. In Italy, they account for a 33.7 percent market share of deposits, and a 29.5 percent share of loan volumes; they make up 60 percent of all branches in France, compared with 50 percent in Austria and about 40 percent in Germany and the Netherlands (Bongini-Ferri, 2007).

The new generation of ethical and social banks is innovative in several respects compared with this tradition. First, microfinance institutions successfully address the issue of matching those with productive ideas with those with financial resources, in cases where the two do not overlap. In fact, one limitation of the traditional banking system lies in the difficulty in financing non-collateralized borrowers. Modern microfinance provides a series of mechanisms (group lending with joint liability, progressive loans, and notional collateral) which help to overcome this limitation, thereby allowing access to credit by individuals who are considered “unbankable” by the traditional banking system (see, among others, Armendáriz de Aghion and Gollier, 2000; Banherjee and Duflo, 2010; Gangopadhyay, Ghatak and Lensink, 2005; Ghatak, 2000; Laffont and N’Guessan, 2000; Chowdury, 2005; Conning, 1999 and 2005; Laffont and Rey, 2003; Stiglitz, 1990; and Ghatak at al., 1999). Second, ethical banks[15] select their lending opportunities not only on the basis of project profitability and capacity to repay the loan, but also on the basis of the greatest social and environmental value. In this way, they channel the resources of socially and environmentally concerned depositors who are even willing to accept lower remuneration for their savings in

[14] From http://icba.free.fr/IMG/pdf/G_20_MARCH_09.pdf, accessed April 30, 2009).

[15]BancaEtica in Italy is an example of this new vintage of ethical banks. According to its charter of principles, the bank’s goal is to use its resources to finance projects with the highest social and environmental value after satisfaction of the economic feasibility constraint. As a result of this goal, the bank earned an ethical premium from investors who demonstrated that they were willing to finance it at below market rates. The value of the “ethical premium” became clear in the passage from book to market accounting (with the introduction of International Accounting Standards in 2007), where the bank’s expected future revenues were discounted at a lower rate, leading to extraordinary profits. The BancaEtica model has been followed in Europe by other banks such as Triodos Bank (124 million euros of equity capital, 1.36 billion euros of savings), GLS Gemeinshaftsbank (35.5 million euros of equity capital and 567.8 million euros of savings) and Umwelbank (5.1 million euros of equity capital and 515.8 million euros of savings). Exactly as discussed in the fair trade section, the emergence of socially responsible pioneers in the financial industry and the consensus offered to them by “concerned” investors have caused a contagion effect on profit-maximising incumbents. One example of this has been the creation of BancaProssima by Intesa-San Paolo, the second largest Italian bank, with characteristics which are very similar to those of BancaEtica.

exchange for the promise that they will be used to create social and environmental value. A common characteristic of microfinance and ethical banks is precisely this “ethical premium”: that is, the capacity to obtain financial resources at a lower cost in exchange for the promise to create high social and environmental value.[16]

Microfinance is an example of how an entrepreneurial idea which is not based on profit maximization may be extremely fertile in generating many new financial and non-financial businesses. The Grameen Bank (which is considered to be the founder of modern microfinance, even though other established microfinance institutions were already operating when it was created) started from scratch a decade ago to become a large bank (with 400,000 employees and more than 3 million customers), funding an industry which counts more than 10,000microfinance programmes lending to around 155 million borrowers, of which 82 million live in conditions of poverty, according to 2009 data from the *Microcredit Summit Campaign*.

As well known, there are various models of microfinance institutions. On the one hand, the founder of the Grameen Bank, Junus, defines himself as a social entrepreneur, and declares that the specific goal of the Grameen Bank is to promote equal opportunities by allowing access to credit by “unbankables”. Other microfinance organisations, on the other hand, do not conceal their profit-maximising goals. The difference between the two is mainly in terms of lending rates, which are much higher in the latter case than in the former. It is therefore clear that only the first microfinance model is relevant to our analysis of socially responsible non-profit-maximising pioneers.

One of the most surprising features of microfinance is its unexpectedly low share of nonperforming loans in the absence of formal financial guarantees.[17] In this respect, one of the main data sources for the industry – the Micro Banking Bulletin (http://www.mixmbb.org/en), which created a panel of 1019 MFIs from different continents – reports an average sample loan loss rate of one percent in 2005. This success questions the standard theory, which regards formal guarantees as fundamental for the prevention of opportunistic behaviour by borrowers and the reduction of lenders’ losses when they default.

The recent history of microfinance provides a clear-cut example of how corporate profits and the creation of economic value at the aggregate level may not coincide. The well-known trade-off between profitability and the outreach of microfinance institutions establishes that the more these institutions try to promote access to credit by the low end of income earners, the less profitable they are. The obvious reason for this is that the fixed costs involved in bringing credit to the very poor are much higher than those of financing an established company. This is why the capacity of microfinance to relieve poverty is significantly aided by the opportunity to pay financial resources

[16] To provide an extreme example, Kiva (http://www.kiva.org/) is an electronic platform by which anyone can lend small sums “directly” to poor, uncollateralized borrowers on the basis of a simple promise of restitution of the sum without interest. Kiva has been extremely successful in pooling small sums from all over the world and channeling them without extra cost to its network of potential borrowers.

[17] Becchetti and Conzo (2011) use a randomized field experiment to document a self-reinforcing effect of microfinance on loan solvency which contributes to explaining its performance. They show that the granting of a loan by the MFI may act as an indication of the borrowers’ trustworthiness in their local communities, thereby increasing their reputation and payoffs from business activities.

at a lower cost from investors with other-regarding preferences who are willing to trade higher returns for the non-pecuniary satisfaction of contributing to the inclusion of the unbankables. Again, while reductionist predictions would have it that matching investors who do not maximize risk-adjusted returns with financial intermediaries who do not maximise profits is impossible, as it violates the purely self-regarding preference paradigm, the reality is actually quite different. In 2009, 91 specialist microfinance investment vehicles (MIVs) invested more than $6.2 billion of foreign capital in microfinance, an important part of which was represented by non-profit-maximizing investors serving Grameen-like microfinance institutions (CGAP 2010 and Morduch and Conning, 2011).

A third and final strand of ethical finance is represented by the so-called ethical investment funds. The actions of these funds correspond exactly in financial investment terms to consumers' vote with the wallet. Ethical investment funds try to stimulate corporate social responsibility with shareholder advocacy and selective investment strategies. In the former case, they propose and vote for CSR-oriented resolutions at shareholders meetings. In the latter, they use restriction criteria in the selection of stocks to be included in their portfolios, reducing the universe of investable shares to that of companies which meet certain social and environmental sustainability criteria (in many cases asking investors to formulate their own preferred ethical standards). This type of action, just like a vote with the wallet by consumers, increases the economic profitability of corporate social responsibility, and therefore contributes to stimulating such choices by listed companies.

Ethical investment funds are by no means a marginal element in contemporary financial markets. The Social Investment Forum Report (2007) states that socially responsible investments involve around 11 per cent of assets under professional management in the US, with a 324 percent growth (from US$639 billion to US$2.71 trillion) between 1995 and 2007, which is much greater than that of all professionally-managed assets (260 percent) over the same period. The 2010 report finds that this sum has risen to US$3.07 trillion.

The more recent empirical literature has evaluated the relative performance of ethical versus standard portfolios without obtaining conclusive results in one or the other direction (Bauer, Koedijk and Otten, 2002; Geczy, Stambaugh and Levin, 2003). What seems to emerge, however, is that ethical portfolio returns tend to have lower variance (Becchetti and Ciciretti, 2009). This finding can be related to the minimization of conflicts with stakeholders by socially responsible constituents, but also to the more patient attitude of ethical fund investors, who buy them with a long-term perspective.

4. The emergence of corporate social responsibility as an endogenous optimal reaction to voting with the wallet

Industrial organization models demonstrate that the optimal reaction of a profit-maximizing incumbent to the entry of an ethical pioneer is partial imitation, up to the point where the marginal cost of becoming more socially and environmentally responsible is exactly traded off by the gain of a part of the market share by individuals voting with the wallet (Becchetti and Solferino, 2010).

In a pre-globalized world with a balance of power among institutions, trade unions and corporations, there is no need in principle for corporate social responsibility. Companies can be left free to pursue profit maximization, and the reconciliation of their goals with socially desirable outcomes in the presence of market failures (negative externalities, public goods, etc.) is ensured by perfectly functioning institutions which create and enforce proper rules. The reality is much different from this ideal scenario, however. The political business cycle literature and, more generally, the economic literature have widely demonstrated that politicians and regulators are not "enlightened", in that they have their own personal goals, which often conflict with institutional ones. Even where this is not the case, they tend to be captured by the very entities that they are supposed to regulate. More problematically, globalization has created a dilemma between globalized corporations, on the one hand, and institutions and rules which have remained essentially domestic, on the other. This implies that there is insufficient governance and regulation to address the problems of global public goods (such as climate) and the misrepresentation of the interests of the world's poor in decisions taken by national governments.

Globalisation is at the origin of the emergence of corporate social responsibility precisely because of this imbalance between powers. Companies are free to set up their productive plants (or choose their suppliers of intermediate inputs) in countries where social and environmental standards are lowest. This is why, in this international regulatory vacuum, concerned consumers and investors are increasingly asking them to take responsibility for their actions in order to limit the negative social and environmental externalities of their policies.

The number of profit-maximizing companies listed on stock exchanges which advertise their socially and environmentally responsible actions is constantly growing. If these companies decide to spend money on this, the reason is that the reputation of CSR is important and may positively affect their revenues. That said, we may think of CSR as an endogenous reaction by such companies to the emergence of concerned consumers and investors voting with their wallets. This is because, as we will see below, the presence of the latter significantly increases market consensus and the gains of CSR strategies.

A standard definition of CSR, based on the EU Green Book,[18] is that it is whatever goes beyond legal obligations. This helps us understand why CSR was not an issue in the pre-globalised era for firms operating in countries where social and environmental standards were already very demanding. However, a more substantive definition of CSR is the one which acknowledges the way in which CSR modifies the relative power of corporate stakeholders. If the interests of shareholders come first for profit-maximizing firms by definition, CSR involves a shift of focus, and a greater level of concern for the satisfaction of a wider set of stakeholders, including workers, suppliers, consumers and the local community in the area in which the firm operates.

One main issue at stake in the CSR literature is the relationship between it and corporate performance. It is evident, in fact, that CSR can become something other than just green and social washing if, and only if, it does not endanger a firm's survival in the competitive arena. If we review CSR criteria, we soon realize that most of them involve costly actions on the part of companies. Taking better care of the well-being of workers, adopting more environmentally efficient productive

[18] EU Commission, 2001, Promoting a European framework for Corporate Social ResponsibilityCOM(2001) 366 Green Paper.

processes, and managing waste and reducing polluting emissions are, in principle, costly actions (the only directly cost-reducing CSR initiative is the limit on the compensation payable to CEOs). On the other side, however, there are at least six potential benefits which may compensate for these costs. The first is related to the impact of CSR on worker productivity and motivation, for two main reasons. The first is set forth by the theory of efficiency wages, which reverses the traditional nexus between productivity and wages. If wages should follow productivity, it is also true that under certain conditions productivity may follow wages. Efficiency wage theories state that when effort cannot be monitored due to asymmetric information, workers are less likely to shirk if they are better paid, since they risk losing good wages and, in general, more favourable working conditions (Stiglitz-Shapiro, 1982). Higher wages have also been shown to reduce turnover and its costs (Salop, 1979; Malcomson, 1981). Finally, the gift exchange version of this theory establishes that a "gift" from an employer (an unexpected voluntary transfer of monetary benefits to employees with no obligation to reciprocate) may trigger a productivity gift from those who have received it (Akerlof, 1982). More generally, gifts are actions which go beyond the boundaries of statutory "do-ut-des" rules and for this reason, they have the capacity to create stronger fiduciary relationships among members of an organisation, thereby increasing the possibility of creating fertile economic relationships.

A second line of thought related to the CSR worker-productivity relationship is that of intrinsic motivation.[19] If we follow it, and examine the extreme case of volunteers, we find that intrinsic motivation may be so strong as to induce individuals to "work for nothing" (Freeman, 1997) in organisations whose goals and ideals they share. This is the dream of any company which aims to increase the productivity of its workers. CSR may help to come closer to fulfilling this dream by reducing the distance between corporate goals and workers' ideals, therefore inducing the latter to do more and to go beyond their contractual duties for their organisations.

A second potential positive effect of CSR on corporate performance is its contribution to minimizing conflicts with stakeholders (Freeman, 1984). The impact of these conflicts on company costs also depends on the rules which define powers, and the effectiveness of bottom-up initiatives such as class actions.

A third effect is determined by the capacity of CSR to capture the consensus and the vote with the wallet of socially responsible consumers (which has to do with everything discussed in this paper). We have seen in Sections 2 and 3 that this kind of vote is already in operation, and contributing to increasing economic gains from CSR strategies. This third channel of influence clearly implies that

[19] One definition of intrinsic motivation is provided by Deci (1975), who argues that "*one is said to be intrinsically motivated to perform an activity when he receives no apparent reward except the activity itself*". A more recent extended definition by Deci and Ryan (2000) runs as follows: "*perhaps no single phenomenon reflects the positive potential of human nature as much as intrinsic motivation, the inherent tendency to seek out novelty and challenges, to extend and exercise one's capacities, to explore, and to learn. … The construct of intrinsic motivation describes this natural inclination toward assimilation, mastery, spontaneous interest, and exploration that is so essential to cognitive and social development and that represents a principal source of enjoyment and vitality throughout life*".

the positive potential of CSR in corporate performance crucially depends on the sensitivity of consumers to these issues.

A fourth effect specifically concerns environmental responsibility. Leadership in this field often also implies being at the forefront of technological innovation in sustainable products/processes, anticipating the regulatory changes which are expected to be increasingly demanding from this point of view, to counteract pollution and climate change.

A fifth effect is the positive impact of the perception of corporate social responsibility on the overall reputation of a company. Even though consumers may not be particularly sensitive to social and environmental issues, they may consider CSR to be a signal of the quality of a company's products. This signal is particularly important in industries where the consequences of low quality may be particularly harmful; examples of this include the airline industry and the financial sector. The banking industry is a typical case in which a scandal may have negative externalities on the sector overall, reducing the trust which is ultimately the crucial resource on which banks live. In this respect, corporate social responsibility provides an opportunity for rebuilding trust, by giving investors the perception that the risk of buying "financial lemons" is lower when sellers are "concerned" financial intermediaries. An empirical example of how CSR may positively affect reputation and corporate revenues is provided by Minor (2009). An analysis of abnormal stock returns on a sample of 184 cases of product recall shows that a CSR reputation allows a company to save US$600 million on average from the negative shock generated by this kind of event. The author's interpretation is that, in the presence of a high CSR reputation, investors are more likely to think that the cause of the event was an accident rather than negligence.

A sixth factor is that, when firms are so large that they have a significant impact on demand for input, their environmentally responsible policies may help them to economize on materials, thereby avoiding contributing to an increase in input prices.

Do the six potential economic benefits of CSR compensate for its costs? Since the emergence of CSR, many empirical studies have attempted to evaluate its impact on corporate performance, but without obtaining conclusive results. This is because the outcome of the competitive race between CSR and non-CSR firms is undetermined by definition, because it depends on factors which are in continual evolution, such as the sensitivity of consumers who vote with their wallets.

The only general conclusion which can be drawn is that an increase in citizens' concerns for social and environmental responsibility will increase the space and feasibility of CSR policies. Again, an improvement in the technology which enables citizens to reduce their search and information costs on the ethical features of products will greatly increase returns, and reduce the costs of corporate socially responsible policies.

5. Conclusions

One of the currently most promising directions in social science research lies in the progressive integration of single disciplines (such as economics, psychology, or sociology) which enriches each of them and contributes to reducing all the forms of reductionism which limit the capacity to understand human action. With a stronger emphasis on the role, determinants and effects of social capital, and with empirical research on the determinants of life satisfaction,[20] economists and social scientists are becoming increasingly aware of the importance of investigating the links between the visible part of the economy (productivity, growth, consumption, investment, and savings) and its invisible pillar (social capital and a broadened pattern of preferences) in order to gain deeper understanding of the motivations behind individual choices.

This paper has sought to make a contribution in this direction by discussing some of the promising paths in recent research from a unified (voting with the wallet) perspective. First, we have argued that the results of laboratory and quasi-natural experiments, but even more so the preferences revealed by purchases of ethical products, urge us to adopt a broadened paradigm for human preferences which includes elements of reciprocity and inequity aversion, and forms of pure and impure altruism. Second, we believe that the alliance between ethically-concerned individuals and corporate socially responsible pioneers (two actors not motivated solely by myopic self-interest) is both the best proof of the validity of this broadened paradigm and a powerful lever with which to tackle social and environmental imbalances in the socioeconomic system.

The crucial factor driving this change is the vote with the wallet: that is, an additional form of participation and economic democracy by which individuals – in their own long-sighted self-interest, if not for other regarding reasons as well – use consumption and investment to reward companies (ethical pioneers) which are at the forefront in reconciling the creation of economic value with social and environmental sustainability. As we have discussed in the paper, this action has the crucial effect of triggering a partial imitation of the pioneers' ethical stance on the part of traditional profit-maximizing companies. It is therefore contagious, and contributes to the rise in the phenomenon of corporate social responsibility.

The mechanisms that we have outlined are extremely powerful. Let us consider a general equilibrium model in an economy which possesses all the standard characteristics (externalities, public goods, and asymmetric information) which prevent decentralized equilibrium from achieving socially optimal outcomes. In this framework, in the presence of a share of individuals with other-regarding preferences on the demand and supply sides, the vote-with-the-wallet mechanism may bring the system closer to social optimum without top-down intervention, doing so merely by exploiting the forces of social responsibility: individuals with other-regarding preferences on the supply side find themselves better off if they create socially responsible corporate pioneers and start selling ethical products. These products increase the variety of products sold, and conquer small market shares, since they are bought by the share of consumers with other-regarding preferences on the demand side. The emergence of these new corporate actors, and their small market share, induce

[20]Empirical research on the drivers of life satisfaction has boomed in recent decades since the wide availability of new data has for the first time allowed economists to test their hypotheses on arguments of individual utility functions directly. In spite of several methodological problems (lack of cardinality and limitations in the interpersonal and inter-country comparability of life satisfaction values) this literature has produced an incredibly consistent set of "stylised facts" and a number of checks which document their reliability. The life satisfaction literature has found discrepancies between subjective and objective well-being, and provided new methods for measuring the shadow value of non-marked goods (for a survey, see, among others, Frey and Stutzer, 2002 and 2010; Clark et al., 2006).

incumbent profit-maximizing companies to imitate them, thereby enlarging the supply of ethical products.

We have shown in the paper, however, that the levered potential of the vote with the wallet is limited by coordination failures and by search and information costs. This limitation shows us the way forward for policy action. The promotion of ethical ratings, improvements in information technology on the social and environmental responsibility of producers (such as software which allows an iPad to download files on company characteristics from product QR codes), and green or ethical procurement rules, are all directions which policymakers may follow to enhance bottom-up participation, and make a contribution to a market solution for market failures.

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Una versione di questo credo è stato pubblicato come:

Ben-Ner A and L. Putterman (2010), Trusting, Trustworthiness, and CSR: Some Experiments and Implications in L. Sacconi, M. Blair, R.E. Freeman and A.Vercelli (eds.) *Corporate Social*

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