



Social Capital in the Food Sector

A Brief for True Cost Accounting Considerations

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True Cost Accounting Briefs

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This Brief is part of a series of research summaries that explore the application of true cost accounting approaches to the agriculture and food industry. True cost accounting is a holistic valuation tool that assesses all four types of capital (produced, natural, human, and social) involved in the production, distribution, and consumption of goods and services. The Brief provides an overview of the concept of social capital, how it is linked to food- and farming-related businesses, and why it determines business failure and success. It also describes how measuring and valuing social capital can help businesses manage social risks and opportunities, and how they can turn social capital into one of their assets.

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Social Capital in the Food Sector

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As a fundamental human need, food is not only a source of life, but is the driving force of our economies and societies. One can tell much from a dish. What people eat is an important aspect of their cultural heritage, and is influenced, among others, by their shared history, lifestyle, values, and beliefs.

Given their central role in agricultural production, processing, and marketing, food- and farming-related businesses (hereafter referred to as businesses) strongly influence our food systems. They shape agricultural landscapes, create employment, contribute to rural development, and, above all, shape the food choices of almost 8 billion people. It follows that we need to better understand the conditions under which our food is produced, and how businesses influence different aspects of our lives.

True cost accounting offers a tool for this. It is a new form of bookkeeping that provides a framework for incorporating natural, social, and human assets into business reporting, so as to make them comparable with financial assets. With a focus on social capital within the food sector, this Brief explores the mutual dependency between businesses and society. The Brief highlights some risks and opportunities for businesses emanating from social capital and explains why taking account of this non-financial asset is essential for achieving sustainable business and food systems.

What is social capital?

Social capital encompasses networks, relationships, and trust amongst individuals and organisations. It also refers to the

degree of adherence to norms and values, as well as common understanding within a society. Social capital arises from the human capacity to consider others, and to think and act generously and cooperatively. It involves supportive social structures that encourage pro-social actions and discourage exploitative behaviour.

From a business perspective, social capital can be increased or decreased through social impacts and social dependencies. Social impacts - also referred to as “flows” of social capital - are the results of business activity. They can occur internally, and externally, and be both positive and negative. Internal social impact encompasses business activities, such as employment practices, that affect employee welfare, amongst. It can include the presence of explicit policies promoting good working conditions, diversity in hiring employees, or non-discrimination. Externally, social impacts can extend to actors throughout the entire supply chain, such as business partners and their employees, consumers, and local communities. They can include long-standing supplier relationships built on trust, enforcement of labour rights along supply chains, or the promotion of women’s empowerment and entrepreneurship.

Businesses can increase their positive social impacts by, for example, supporting workers’ right to self-organise by forming trade unions. They can also reduce negative social impacts through actions such as actively monitoring the use of child labour across their entire value chain.

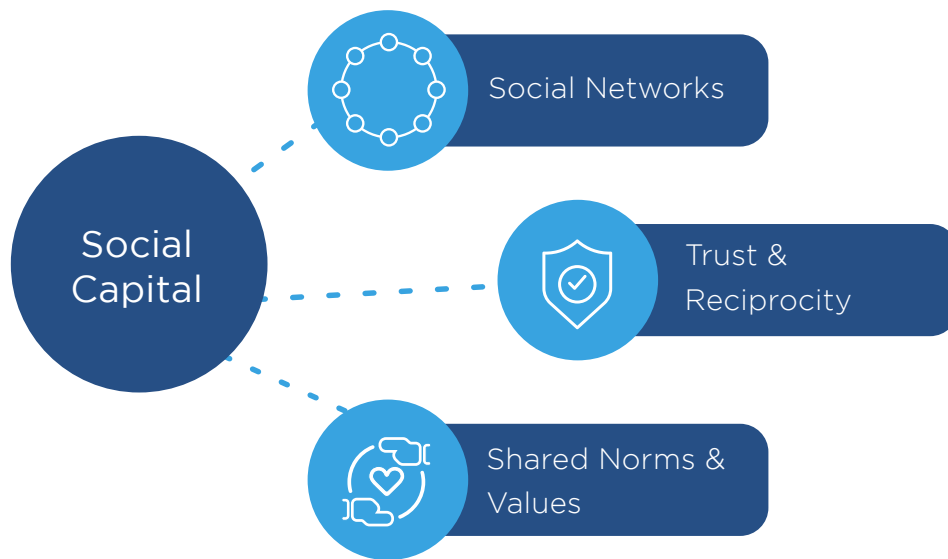


Figure 1: Advantages of social capital assessments
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Social dependencies refer to the extent to which businesses rely on social capital to run their operations. Such dependencies include business relationships, trust, common understandings, and adherence to norms and values that are required to function as a business. Businesses' ability to operate and grow is, for example, dependent on a productive workforce, efficient and reliable value chains, acceptance from local communities, loyal customers, satisfied investors, and supportive local authorities and governments.

Unlike produced or natural assets, social capital cannot be "sold" to generate income. However, this does not mean that social capital lacks value. Rather, it adds value! Social capital improves the performance of the other forms of capital, hence making them more profitable. For example, trust among business partners can facilitate business cooperation, while consumer

confidence in a product will increase brand loyalty. These are two essential conditions for long-term business success.

Social capital is also important for the stability of communities and societies. It is the glue that holds societies together, and without which there can be no economic growth or human wellbeing. The absence of social capital contributes to what economists call transaction costs, namely additional costs in terms of finance, working hours, or inconvenience in carrying out a business undertaking. Without the support of the local community, for instance, a business will have a hard time building a new factory, even if all necessary legal permissions have been secured. Any resulting protests may lead to delays in construction work, which costs extra time, money, and can damage the company's reputation due to negative publicity.

“Face the truth, or the truth will face you”

Due to their massive influence as providers of a basic human need, food- and farming-related businesses need to be careful not to damage or destroy social capital. Unfortunately, this is often the case. Social issues in modern agricultural value chains include the neglect of labour standards and human rights, excessive working hours, low wages, or the unequal treatment of individuals or groups. Socially “blind” business practices can also contribute to food loss and waste, food insecurity and malnutrition, and the lack of social security.

It is possible for businesses to earn profits at the cost of others in the short term, but ignoring their negative social impact will jeopardise businesses’ bottom line in the long run. The private sector is increasingly being held accountable by different stakeholders for its action, or non-action. Yet, while reputational damage may affect revenues due to reduced sales, or production costs may rise due to fines and compensation payments linked to legal non-compliance, most social costs remain hidden. Because they are not signalled through conventional accounting and market systems, such costs are not factored into business operations. Notwithstanding, social costs constitute unexpected risks that may affect businesses’ future net profits or endanger their “license to operate.”

The risks to businesses that ignore social capital – and other forms of non-financial capital – are likely to increase rapidly in coming decades. This is in part due to growing social pressure for governments to enact and enforce stricter laws and regulations regarding marketing and labelling practices, human and labour rights, consumer rights, and many more. Some of these social issues have been embodied in global frameworks, such as the United Nations’ Sustainable Development Goals (SDGs),¹ helping to

drive political change at various levels, and to demand greater social and environmental accountability from business actors.

There are business opportunities in social capital

The benefits of investing in social capital extend beyond cost savings and other immediate business opportunities. By building up their social capital, and turning it into an asset, businesses can increase the value and resilience of their operations.

- As they gain a reputation for positive social impact – such as providing employee benefits or promoting ethical supply chains that pay a fair price for commodities – businesses are more likely to establish, and maintain, a highly competent workforce and business network.
- By demonstrating that they are aware of the social risks posed by their operations, and are ready to take countermeasures to mitigate these, businesses can increase their credit worthiness, and are likely to receive better insurance conditions.
- Businesses with a net positive social impact can differentiate their products from those of their competitors. This in turn can yield dividends in the form of securing more customers. Similarly, a commitment to data security and customer privacy will gain consumers’ trust.
- Businesses that can show how their interventions help local communities – for example by providing day care services – will be in a better position to engage with policymakers and regulators.

¹ For example: SDG Target 5.1. (end discrimination against women); 8.7 (eradicate forced labour, modern slavery, and child labour); 8.8. (protect labour rights); and 16.6 (encourage companies to integrate sustainability information into their reporting).

Reduce Costs & Risks

Capture Opportunities

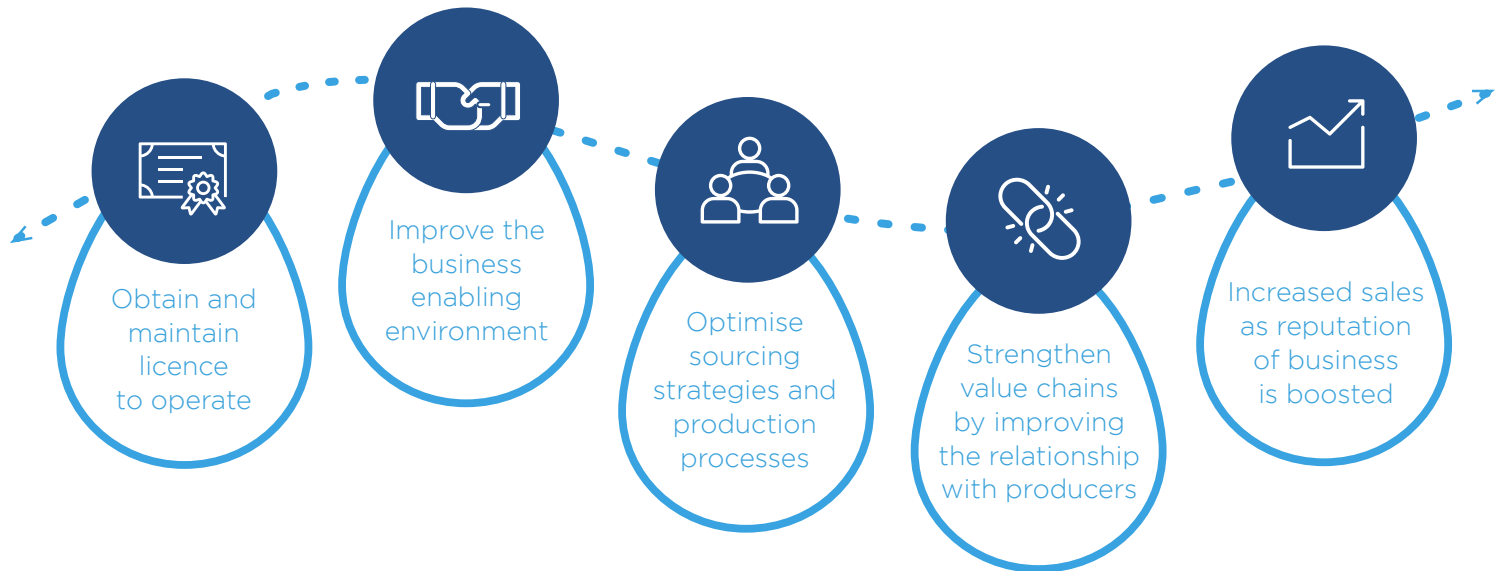


Figure 2: Advantages of social capital assessments
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Why investing in social capital is beneficial for businesses

It is not enough for businesses to introduce socially responsible actions. They also need to continuously monitor, adapt, and innovate in their social measures.

Measuring social capital allows a business to grasp its social assets. It also provides insights on the extent of its social impact and dependency on society.

Valuing social capital enables businesses to capture the cost and benefits associated with these social impacts and dependencies. It also helps communicate a company's worth in a language that people can understand. In addition, measuring and valuing their social impacts and dependencies allows businesses

to **manage** their social capital like any other asset or liability. Such information can be incorporated in internal management and decision making. For example, businesses can assess which of their operations lead to social improvements, or where to initiate counter measures or increase investments. Furthermore, by factoring in social impacts and dependencies in risk assessments, businesses can assign monetary costs and benefits to social risks, which contributes to a better understanding of the magnitude of potential threats.

Reporting social capital helps businesses to communicate the added value they bring to the outside world. For example, companies can highlight their investments in improving the wellbeing of employees as

well as wider society. This provides a basis for other stakeholders to assess the costs to individuals and society if other businesses do not shoulder similar responsibilities. Hence, the transparency generated through reporting social capital leads to a better comparability of companies in this respect.

One concrete way in which such information can be used is when businesses enter political discussions. By tabling evidence on their positive social impacts, businesses can “claim” rewards in the form of lower taxes, or other incentives. An example of

this is the ongoing discussions towards a new German supply chain act,² that will incorporate legislation on labour practices, and human rights due diligence.

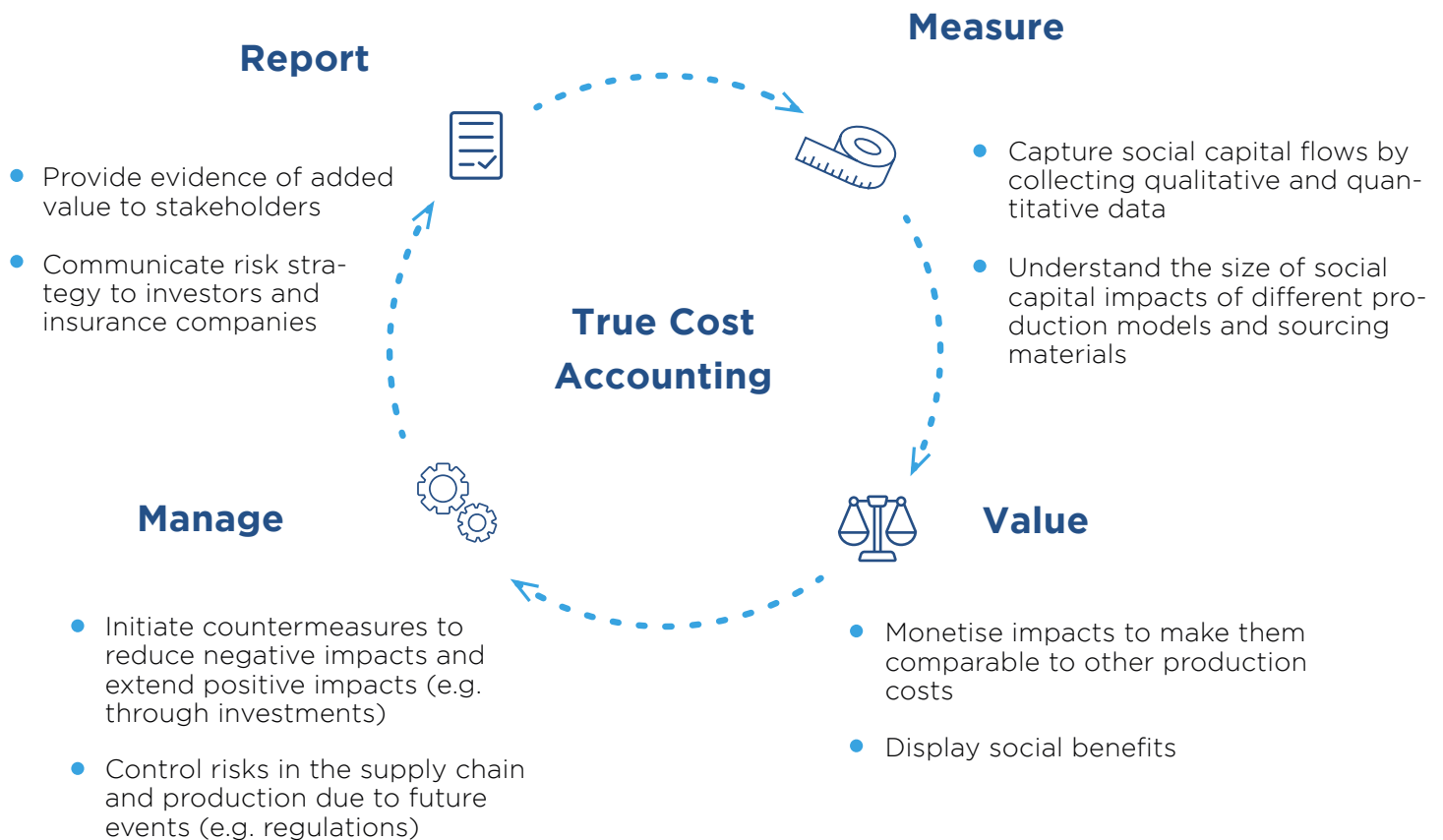


Figure 3: TCA assessment cycle © P. Korneeva/ TMG Research gGmbH 2020

² Federal Ministry for Economic Cooperation and Development (2019). Ministers Müller and Heil advocate fair supply chains. Press release, http://www.bmz.de/en/press/aktuelleMeldungen/2019/februar/190220_pm_008_Ministers-Mueller-and-Heil-advocate-fair-supply-chains/index.html

True cost accounting: An integrated tool for tracking social capital

As highlighted above, the opportunity to increase their business performance, and reduce their business costs and risks, are strong reasons for companies to assess their social impacts and dependencies. True cost accounting is a comprehensive tool that allows businesses to perform such assessments, alongside the analyses of the three other forms of capital (produced, natural, and human).

In addition to analysing a company's social impacts and dependencies at corporate level, it is also possible to assess social capital in more detail, such as for a specific agricultural raw material or a food product. An advantage of true cost accounting is that it can be used for internal management purposes, while also enabling a company to augment traditional annual financial statements with an overview of its social capital costs and benefits.

Which businesses should assess their social capital?

All businesses can gain tangible information, and a valuable reporting tool, from measuring, assessing, managing, and reporting social capital. It can be expected, that "socially blind" businesses will have a greater learning curve than more socially aware businesses. However, businesses that are already taking measures to increase their transparency, and add-value through certifications, will benefit from social capital assessments, too. For example, while organic producers follow a clear set of guidelines regarding the environmental aspects of production, an organic certification in itself does not say much about the social dimensions of sustainable systems. Even businesses that are participating in certification schemes that pay great attention to the social conditions under which food is produced (such as Fairtrade standards) can benefit

from measuring and valuing their social capital. By monetising their social impact, in addition to assessing their social practices, such businesses can demonstrate their overall added value, and compare their performance to that of other companies.

Conclusion

As the glue that holds societies together, social capital may seem like a rather complex concept at first sight. But after having demonstrated that food- and farming-related businesses can widely benefit from the interconnectedness with society and from cooperative, pro-social behaviour, it almost goes without saying that businesses have to play an active role in this continuum. Not only can employers generate positive impacts internally, but suppliers, consumers, and the "outside world", will also benefit from targeted, and socially responsible practices. Even when this is not intended, many business activities can still do harm due to decisions that are solely focused on short-term profit, and unaware of broader consequences. It is high time, therefore, that businesses make drastic changes to how they assess their societal impacts. True cost accounting is a tool that makes business-related activities – both positive and negative – visible and comparable. By monetising their impacts on individuals and society as a whole, businesses are better able to recognise harmful activities, adapt their behaviour, and report their achievements. This is a win-win outcome that can help businesses to continue, with justified self-confidence, on a more sustainable path.

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