Globethics Repository



Ethics and sustainability within SMEs

This page was generated automatically upon download from the Globethics Repository. More information on Globethics see https://www.globethics.net. Data and content policy of Globethics Repository see https://repository.globethics.net/pages/policy.

Item Type	Preprint
Authors	Painter-Moreland, Mollie;Dobie, Kris
Rights	With permission of the license/copyright holder
Download date	2026-11-13 05:25:24
Link to Item	http://hdl.handle.net/20.500.12424/174031

Ethics and sustainability within SMEs:

Enabling, conditioning and contaminating relationships

Mollie Painter-Morland, University of Pretoria/ DePaul University

mpainter@depaul.edu[1]

Kris Dobie, Ethics Institute of South Africa

kris@ethicsa.org

Abstract:

In this paper, we seek to investigate the role ethics plays in the functioning of SMEs in the African context. We go beyond corporate social responsibility to probe some broader ethical concerns relating to business ethics, corporate governance and corruption prevention. This study of ethics in the context of SMEs seemed to underscore the intricate and intimate relationships that exist between business ethics and corporate social responsibility. This seems self-evident, as both these "disciplines" relate to building sustainable relationships with stakeholders, yet these areas remain quite distinct academic fields in most countries. This study of SMEs in Africa provided us with an opportunity to make the intricate relationships between these areas more visible. We argue that it is the relationships between SMEs, employees, customers, communities, competitors, government and the broader business sector that either enable or foreclose the possibility of ethical business practices in SMEs. Our research also revealed that ethical practices, or the lack thereof, have a strong impact on the sustainability of SMEs. Certain relationships, such as those between SMEs, local suppliers, employees and local communities, can be described as enabling. Other relationships, such as those that have to be entered into with corrupt governments, are contaminating, and therefore distinctly debilitating. What seems to be needed, is to expand on and strengthen certain conditioning relationships, such as those that exist between peers within a certain industry, professional associations, and civil society. What these conditioning relationships could bring about, is the sharing of best practices, peer-to-peer interactions, relational checks and balances, story-telling, networking, and skills transfer opportunities.

[1] We would like to acknowledge the research assistance of Ms. Hanrie Greebe of the Centre for Business and Professional Ethics in setting up and conducting many of the interviews, and for her language editing, and of Mr. Michael Röthel for literature sourcing.

Ethics and sustainability within SMEs:

Enabling, conditioning and contaminating relationships

1. Introduction:

Small and medium-sized enterprises (SMEs) have been described as the engine of many economies in the developing world. In fact, one can even say that they are crucial in sustaining economies worldwide. Fox (2005) reports that on average, SMEs represent over 90% of enterprises and account for 50-60% of employment at a national level. Some of the respondents in this study put this figure closer to 80% or even 90% in some African countries. Tarus et al (2007) mention that Kenya's Economic Recovery Strategy is based on the assumption that 88% of new jobs would be created by SMEs. It is clear that businesses that emerge in response to community needs and in an attempt to secure the livelihood of their owners, are the lifeblood of many in Africa. To use a metaphor central to the African context, the flow of goods and services seem to be life-giving water that in many respects brings relief to a parched land. However, without proper care and constraint, even life-giving water can be the carrier of disease, detrimental to health of those who consume it. The flow of that which could have been life-giving, could equally easily become a quick flood with few short-term gains but many long-term costs. Or even worse, it could remain a few trickles that dissipate in the parched land long before it could have much positive effect.

SMEs are facing many ethical challenges that seriously compromise the contributions they could make to the long-term economic longevity of their communities. Our study into the functioning of SMEs indicated that the free flow of economic activity in response to need can indeed be a life-giving force in Africa, and that SMEs already yield many benefits to local communities and developing economies. However, there is some need for ethical guidance, encouragement, and constraint. We will argue that these constraints won't necessarily have to rely on the promulgation of stricter regulation or legislation. In fact, care must be taken not to stifle the free flow of entrepreneurial activity through expensive regulation and measures designed for organizations in developed countries. Rather, what seems to be necessary is a groundswell of ethically enabling relationships

and reciprocal constraints. There is also a dire need to rid SMEs of the debilitating relationships that draw them into the quagmire of corruption and other dishonest business practices.

2. Methodology:

This paper presents our interpretation of a qualitative empirical study in which we sought some responses to a series of open-ended questions from respondents representing SMEs in Sub-Saharan African countries. Our initial aim was to focus on the most developed economies in the region – determined by the GDP per capita. To widen the representation of our study we decided to focus our attention predominantly at intermediary organisations that deal extensively with SMEs through development or support projects. The thinking was that these organisations would be aware of the realities in a number of SMEs and would have concern for their sustainability. The final representation of respondents ended up being more reflective of the distribution and availability of these organisations. There is however significant overlap between this distribution and the countries with the highest GDP per capita.

The data was gathered by means of telephonic interviews and electronic surveys. Twenty one (21) respondents were from these intermediary organisations, while 5 respondents were themselves owners or operators of an SME. The intermediary organisations included chambers of commerce and other business associations, microfinance or development NGO's, as well as private enterprises that focus on SME development through finance and technical support. Even though the majority of respondents were from intermediary organisations, we were still conscious of the need to get an African perspective on Ethics in SMEs. Of all the respondents only one was non-African.

The general methodological approach taken in this study is that of Grounded Theory. Our interest was in how respondents viewed ethics within the SME environment, how they talked about the causal factors of unethical/ethical business practices, and what they believed is necessary in terms of building more sustainable SMEs [see attached

questionnaire]. Two of the authors analysed the raw data in order to identify recurrent concerns, or insights, which allowed us to see certain concepts/themes emerge as salient. The recurring themes/concepts were labelled and then placed within certain categories that could bring us towards a theoretical framework. This was done without reference to concepts, themes or categories developed in the SME literature.

Although we recognise that Sub-Saharan Africa is by no means a homogenous region, we do not have enough data to view each country in isolation. It was clear from the interviews that some economies are more developed than others and therefore have different issues. However, we reflect on the issues that emerge strongly from all our data by focusing on the similarities rather than the differences.

The researchers were not experts in the field of SMEs, but rather ethicists whose academic background and practical experience were in Business Ethics and Corruption Prevention. What should however not be denied, is that as authors of this paper, we approached the data from our own background, philosophical predispositions and experience as ethics practitioners. We were certainly not "blank slates". Emergent themes and theories should not be interpreted as "facts" about SMEs, but should rather be seen as indicative of the kind of theoretical proposals that could emerge in a conversation between ethicists and practitioners operating in the SME environment. In what follows, we attempt to convey our impressions of trends that emerged in the research data. We will then proceed to relate our findings to available literature on ethics within the context of African SMEs in order to see if there is support for some of our theoretical propositions.

3. Patterns emerging from the data:

When asked about their understanding of the notion of "ethics in SMEs", the theme that emerged most strongly related to "honesty", "straight dealing" and "not cheating". This was often linked to the second most prominent theme, which referred to governance issues such as proper accounting, auditing and honest tax paying. After these, labour

issues were most salient as most respondents made reference to “honesty”, “straight dealing” in “how they treat their staff”. Another strong theme was the issue of fairness in how SMEs treat the community and clients.

When asked to define ‘ethics’, respondents had wide ranging answers, relating to individual and societal expectations around proper behaviour, as well as conformance to rules and proper accounting. Respondents defined ethics as a concern for the values operative in society, rules of behaviour that aim at sustenance/sustainability of the business, or codes of conduct towards various stakeholders. Another defined ethics as moral conduct that individuals and groups willingly abide by. Values, or virtues that are mentioned are: honesty, consistency, commitment, care, fairness, openness and transparency. Some of the participants specifically identify the building of linkages to the community, the environment and employees as central to what ethics means. A particularly lucid definition of ethics that one participant offered is: ethics is a stance of responsibility and responsiveness in doing business worthy of the cause of humanity (including workers, clients), community, environment and government…” This definition perfectly captures the relational dynamic that we have come to identify as a central theme underscoring ethics in the SME environment. Repeat mentions of notions like honesty, fairness, moral conduct towards others, brought us towards identifying the notion of *“being true” to societal values as well as formal rules of practice* as a central category.

When asked about the impact of SMEs in society nearly all respondents’ answers focussed on the positive impact, predominantly in job creation. Many also perceive SMEs to be the “engine of the economy”. SMEs are what keeps countries going. They are also responsible for bringing products and services closer to communities. Within these responses we found that the *relationships* between SMEs and their stakeholders were once again salient. What seems clear is that the positive contributions that SMEs are making relates to the way in which they meet the needs of their country, community, and closer circle of family and dependents. SME contributions to society include creating jobs, distributing goods and services to areas or people that would otherwise not have access to them, creating a market for small suppliers, decreasing the dependence on

imported goods and working against monopolisation. SMEs also create significant income for the government and incentivise further entrepreneurship. One participant even attributed the "overall economic and social improvement of society" to SMEs. SME activity can therefore be described as belonging to a more general category of spontaneous *responsiveness* to need – their own, and that of their community. In fact, one could even say that it is a response to personal or community need in the absence of other opportunities of formal employment, or other access to goods and services. Since adversity is the mother of invention, those in need of a livelihood find ways to sustain life. In more theoretical terms, this brings us to recognise that sustainability could be positioned at the very heart of SME activity. It is a response to the *desire to sustain* lives, families, communities and countries. In this sense, sustainability concerns go far beyond the sustainability rhetoric employed by some larger corporations in the first world. Building a sustainable business model can be viewed as an integral part of all SME activity in Africa, not some add-on standard that should be imposed to constrain "business as usual".

This is also reflected in the answers relating to SMEs' social responsibility projects. Some SMEs are involved in activities that play an important role in supporting their immediate communities. This ranges from supporting schools and the aged, or even providing community infrastructure such as water wells. These activities are mostly undertaken by individual businesses (not co-ordinated) and are not as "hyped" as corporate CSR projects.

However, the dark flipside of this responsiveness to need is the fact that many SMEs might be operating according to what Rossouw has described as "survival morality", which by definition is concerned with "bread first, morals later". The argument is that many SMEs or at least, those in early stages of development, are so concerned with surviving in a competitive environment that ethics will be compromised if there is any business advantage to be had. This is reflected in the responses. Business pressure, and sometimes pressure from an unethical environment, leads companies to "cut corners", reduce product quality, and over-promise or over-commit, which eventually impacts

negatively on the sustainability of these operations. The question that one may pose is whether this depiction of "bread first, morals later" completely undermines the concern for ethical sustainability. This question may be addressed by some of our conclusions later in the paper.

The most prominent responses to the question around the "important ethical problems or issues for SMEs" related to administrative dishonesty and to labour issues. Under *administrative dishonesty* we have grouped issues such as corruption, tax avoidance, misrepresentation in audits, and ignoring licensing procedures. These issues relate predominantly to relationships with government institutions, although investors are increasingly concerned administrative honesty. The *labour* issues centred predominantly on fair wages and the treatment of staff. The latter includes disrespect as well as bad working conditions. Other labour issues included employing under-aged workers, not allowing freedom of association, not providing proper benefits or job security, and indulging in tribalism. The third most prominent theme around ethical concerns related to the quality of goods and services. These include: over-pricing, misrepresentation in terms of product quality, and selling pirated goods. These are typical issues in survival mode, short-term focussed businesses. Dishonesty around products and pricing seem to be contaminating relationships with customers.[2]

Theoretically, it seems as if most of these ethical problems, or examples of unethical behavior can be related to *unfair relationships* with stakeholders or the breakdown of trust. The way in which we interpret how participants describe unethical behavior, is that it relates to the *tainting or even the breakdown of relationships*.

When asked about factors that make ethics difficult many of the responses indicated that unethical behaviour is often the reaction to an environment in which unethical business practices are widespread. The existence of systemic corruption in the broader environment in which SMEs operate was consistently highlighted as one of the most

[2] Environmental issues might be conspicuous in their absence. Although they were referred to environmental issues received a low mention in comparison with the other issues.

serious challenges they face. The most prominent factor that was mentioned was corruption in interactions with government. SMEs necessarily have to interact with government agents (especially for licensing) and due to the inequality in power and resources, they have little or no bargaining power, or voice, in these relationships. Businesses that are not run above board are even more vulnerable to such extortion. In many countries this includes a large proportion of unregistered small businesses that operate outside of the formal economy. Competing with unethical competitors was also mentioned as a central concern. This led us to conclude that many SMEs operate within a context of *contaminating relationships*, where the pressures to go along with unethical practices are very strong and positive peer-pressure is rare. Many respondents indicated a dire need for more awareness around ethics issues in business in general, but among SMEs in particular. Of specific concern is the shortage of positive stories and role-models.

The lack of quality controls, delays, and inconsistency in pricing are inevitable side-effects of the way in which SMEs originate as a response to need. Respondents indicated that there are very few laws, local or otherwise, that constrain activities in the SME arena. Where there are basic standards, these standards cannot be enforced. In most cases, the owners of SMEs are not aware of these ethical standards, or they lack the basic business skills to implement them properly. The need to develop standards and monitoring systems is mentioned by some respondents, but other participants mention that burdensome government regulation tends to undermine ethics, rather than aid the promoting thereof. This desire for guidance and legal parameters, coupled with an aversion towards an overregulated environment, presents us with the paradox of the SME environment. Where the business environment is over-regulated, SMEs cannot afford the compliance measures that need to be put in place and therefore cannot survive. Multiple taxation was also raised as an issue that puts SMEs under the kind of competitive pressure that fosters dishonesty.

Respondents indicated that many of the ethical problems have a direct impact on the sustainability of businesses. They indicated that the following factors hinder long-term

business relationships: poor quality products, short-term thinking (survival mode), lack of business experience or management skills, and inconsistent delivery from suppliers (sometimes related to infrastructural difficulties). On the positive side, honesty, reliability and professionalism amongst small business owners were identitied as factors that facilitate long-term business relationships. All of these factors mentioned impact on the ability of SMEs to be *trusted* business partners. They include ethical and non-ethical issues. In relation to the most prominent ethical issues there is a definite correlation between sustainability and *being straight in business*. The non-ethical issues relate particularly to management and other technical skills, as well as inconsistencies from suppliers.

The character of the business owner or manager, and their commitment to integrity and sound business practices, were repeatedly singled out as the crucial determinant of a SMEs approach to ethical business practices. The power of a single individual to set the tone from the top could however have negative consequences when there is a lack of such ethical leadership. When organisational control is centralized within a single individual (CEO), a single family, or a few powerful politicians, it tends to breed ethical problems like conflicts of interest, nepotism and favoritism, and also undermines the crucial checks and balances on which organisational fairness normally relies.

The factors that participants identified as central in establishing a culture of ethics include: encouraging competition, developing strong reputations and nurturing long-term relationships with clients, encouraging freedom of association of employees, and less political interference. Participants indicated the need for protection against unethical individuals, unethical competitors and corrupt politicians. All of these factors have to do with the relational dynamics within which SMEs operate. What makes business relationships *enabling*, seems to be the way in which it facilitates and sustains *long-term* business relations. Participants identify reputation, trust, loyalty, consistency and punctuality, which in itself could signal fairness and respect. Both trust and respect are central to sustainability. Respondents made multiple references to the relationships

between ethics (specifically *being straight in business*), a concern for *long-term relationships* and sustainable business practices.

It is clear that these more long-term concerns do not seem to figure as strongly as they should in the relational dynamics in which SMEs find themselves. It seems that SMEs find themselves in contaminating or debilitating relationships, which often overshadow the enabling relationships with stakeholders that could support the propensity towards ethical responsiveness amongst SMEs. Also, there seems to be a great need for strengthening certain constraints that could guide the relationship between SMEs and their stakeholders and develop the conditions of trust and respect that are central sustainability imperatives.

4. Theoretical propositions:

4.1. Enabling relationships:

The most positive contributions that SMEs make to their communities, is described in terms of their ability to create jobs, opportunities, and to stimulate growth in areas where there would otherwise not be much economic activity. SMEs provide markets for local products, and bring products and services to areas without easy access to these. The most enabling relationship that SMEs therefore have, is their relationship to the communities in which they operate. However, SMEs can only sustain these relationships if they can sustain their businesses. We shall see (below) that these relationships also operate as conditioning constraints, but for the purpose of this section, we will focus on the way in which building long-term relationships with immediate stakeholders in the community can assist SMEs in weathering the storms of a turbulent business environment and building ethical, sustainable businesses.

The most important ethical relationships in terms of business sustainability seem to be with customers and suppliers. These relationships have to do with trust and predictability. It is as important to *be* a trusted business partner as it is to *have* trusted

business partners. Respondents seem to believe that building such a trusted enterprise is inextricably linked to also being administratively honest. Truly sustainable enterprises cannot only be honest in trade relationships, they also have to be honest in the internal administration of their enterprises, which relates to their governance relationships. A further enabling factor would be to operate in an ethical environment, without the debilitating effects of unethical competition.

Creating feedback loops from customers, local suppliers, and local community organisations, can alert SME owners to new customer needs. Feedback loops can make SME owners aware of factors that may impact on customer buying power and concerns that customers and community members may have about the products, services or externalities of an SMEs business activity. Responsiveness to various stakeholders seems to be one of the most important aspects of sustaining those enabling relationships that make the difference between business success and failure. We will later seek to provide support for this idea in the literature review. It is the concern for nurturing long-term relationships with these various stakeholders that provides the most important impetus for consistent ethical business behaviour within SMEs.

Another very important enabling relationship is the relationship that SMEs could have with their employees. Labour is in most cases readily available due to large numbers of unemployed people in many developing countries. SMEs therefore seem to make the mistake of viewing employees as a dispensable and replaceable resource. However, staff turnover costs, such as the loss of skills and the time and productivity lost in retraining new staff, must be brought to the attention of SME owners. Furthermore, positive workplace conditions enhance motivation and productivity and minimize sick-days and other occupational health and safety concerns.

Participating in business networks such as the Afrikaans Trade Institute, the Nigerian National Association for Small and Medium Enterprises and the Association of Ghana Industries can also go a long way towards providing SMEs with condensed research results about business trends, risks and opportunities. These networks can play a role in

the dissemination of best practices and arrange skills transfer opportunities. As such, these business networks can function as a link between SMEs and training institutions such as universities, colleges and civil society organizations that have access to funding which could sponsor much needed training in the SME environment. These networks are an ideal platform for positive role-modelling and sharing of good-practice stories.

4.2. Conditioning relationships:

The question of how unethical behaviour can be controlled, constrained, or in more positive terms, how ethical behaviour can be *conditioned,* remains one of the most important dilemmas in the SME environment. There is clearly a need for standard-setting, quality control and the development of sound governance processes. However, respondents describe over-regulation within the SME environment as counter-productive. Alternatives that may be explored relate to constraints which could emerge out of the interactions that SMEs have with each other as well as their concern for long-term relationships with customers, employees, supply-chains, government and the local community.

The question that emerges is whether it is possible to enhance the mechanisms and support-structures for self-regulation within the SME environment. It is important to note that the formal business networks mentioned above also play a tremendous role in creating a business environment that conditions SMEs to behave ethically. The Association of Ghana Industries has played a major role in the development of the Ghana Business Code. Besides raising awareness of the need for sound governance and ethical practices, this also provides SMEs with a stronger power-base when interacting with possible corrupting government players. The approach here is to argue for reciprocal relational constraints amongst the players within the SME environment. The idea is that SMEs voluntarily hold themselves and each other to certain standards. For instance, the development of aspirational standards and specific sets of benchmarks within certain industries can be an option. This could transpire if there were to be opportunities where SMEs can meet and discuss their most urgent needs and communicate their respective

expectations of one another. An important part of this is peer-to-peer interaction, especially the sharing of those success stories where a commitment to ethics shows long-term positive results. The challenge is for SMEs to find the time and resources for these events. Furthermore, it is unlikely that SMEs in developing countries could do this on their own. Institutions are needed that could seek funding, organize, and facilitate these events. Civil society and especially research and training institutions have a role to play in this. The more challenging aspect of these proposals is that competitors within a certain industry will have the responsibility to provide checks and balances on each other and to report unethical behaviour when it occurs. Subsequently the need for whistle-blowing resources or other avenues for complaints arise. For instance, professional associations could play a very important role in providing access to whistle-blowing resources, or setting standards for their members and providing some resources for monitoring compliance. The problem however is that many of the professional associations are often understaffed and have little control over their membership.

Customers can also play a crucial role in placing certain constraints on business practices within SMEs. There are two important factors for customers to have any material effect, i.e. choice amongst competitors and access to information. If the customer has no choice of suppliers of certain goods or services, unethical business practices cannot be punished by withholding repeat business. The maintenance of a sound competitive environment is therefore crucial. Furthermore, if customers don't have access to information about substandard goods, unfair pricing, or the environmental effects of unethical business practices, they cannot withhold their support on ethical grounds. Here, civil society institutions and standard setting-bodies need to play a central role. They are needed to gather information, provide access to research and resources for whistle-blowing, to gather complaints and direct these to the relevant authority.

Supply chain relationships can also play a large role in constraining SME behaviours. Government and large businesses can raise the bar on ethical business practices by raising the standard of ethical expectations from SMEs in their supply chain. This could relate to sound governance practices, employment practices, anti-corruption measures

and quality standards for products and services. The problem in many cases however seems to be that these players aren't committed to these standards themselves and that they have a contaminating influence, or they develop standards that make compliance too expensive for SMEs (see below). What seems to be crucial is that the standards set by large business enterprises and government must simultaneously raise the bar on ethical behaviour *and* be responsive to SME needs. We will further reflect on this challenge in the last section of this paper.

Employees within the SME environment are often the most disempowered party in terms of having a voice against the unfair treatment they receive. Since many SMEs discourage or undermine workplace democracy, it is very important that employees have access to some bodies where they can make their voices heard. Many industries do have strong workers' unions which may be less organised within the SME environment. These unions should actively seek to support employees in the SME environment by recruiting members within SMEs, advising them on their rights and seeking avenues for recourse in the case of unethical treatment.

4.3. Contaminating/debilitating relationships:

Debilitating relationships that SMEs have to deal with include relationships with their own national governments as well as with unethical businesses in their environment. The contaminating effect of SMEs' engagement with government was repeatedly mentioned by many of the respondents. Especially bribery seems to be a recurring example of unethical behaviour affecting SMEs in a few of the countries we studied.[3] SMEs clearly seem to believe that they have no recourse to bodies or support structures that could assist them in maintaining their integrity in the face of demands for bribes.

Within the macro-economic contexts, globalization poses threats to local markets and tends to create the kind of environments in which it is very difficult for SMEs to survive.

[3] It is however important to note that respondents from some countries specifically mentioned that they do not believe corruption is a problem for SMEs.

Much research has been done on the constraints that the World Bank, IMF, international aid organizations and other international bodies place upon developing countries (See Patrick Bond's "Against Global Apartheid' etc). The types of preconditions placed on organizations wanting to gain access to funds or contracts serve to undermine, rather than protect SME sustainability. Ironically, some of these preconditions may in be intended to raise the bar in terms of ethical standards and to provide checks and balances, but the truth is that they are not responsive to the needs of local SMEs. Instead of enhancing ethical behaviour, these constraints force SMEs to engage in deceptive practices, thereby further undermining integrity and transparency in the SME environment.

4.4. The interaction between enabling, conditioning and contaminating relationships:

What makes the patterns emerging from this research particularly interesting is that it allows us to see the relationships between the fields of business ethics, CSR and corruption prevention much more clearly than many theoretical studies of these disciplines allow for. Within SMEs, it becomes clear that sustainability is totally reliant on the way in which ethical relationships with various internal and external stakeholders can be fostered over time. The practical implications of the notion of "Integrated Sustainability" mentioned in the King II Report (IoD, 2002) becomes clear when one takes into consideration that the ethical challenges SMEs face have everything to do with the fact that they operate within enabling, conditioning and contaminating relationships. Their relationships with customers, the local community and employees can be enabling only insofar as there is a real stakeholder engagement model operative that gives voice to a variety of internal and external stakeholders. Constraints exist only if there is stakeholder and peer pressure and insofar as civil society organisations and networks are doing research and sharing information. Peers, competitors and professional organisations also have to be engaged in order to build in reciprocal constraints. What these relational constraints could enable, is the sharing of best practices, peer-to-peer interactions, relational checks and balances, story-telling, networking, and skills transfer opportunities. Meaningful skills transfer can only occur if networks are built across the boundaries that seem to exist between the private sector (big business *and* SMEs),

government and civil society. If relationships with governments and international bodies remain contaminating and debilitating, not much will come of all the other positive initiatives.

Ethics comes down to building sustainable relations across sectors and within communities and organizations. This requires coordinated efforts between initiatives aimed at promoting business ethics, instilling good governance, preventing corruption, and the pursuit of broader social and economic goals in society.

5. Research trends from the literature review:

In this section, we relate the results of our research study to important trends in the literature in order to answer some of the questions originally posed in view of the ISBEE conference. How are SMEs defined? How do SMEs view ethics? How do they view their role in society? And what is the relationship between all these ethical concerns and the sustainability of SMEs?

It seemed clear from our research that there are many different definitions operative within the SME environment in Africa. Some definitions are clearly taken over from the developed world, considering organisations with fewer than 250 employees to be SMEs.[4] Many formal definitions were mentioned, which place African SMEs at smaller sizes. The most prominent response was that an SME is an organisation with fewer than 100 employees and a working capital of less than $100 000. Some respondents did however mention that even these scales were not reflective of what is on the ground. The varied definitions make it rather difficult to interpret the relevance of some of the responses we received and to test the theoretical propositions we make. For instance, though many SMEs function outside of the formal economy, there are others that, as a result of their

[4] Jeppesen (2005:467) reports that in South Africa, for instance, SMEs are defined as firms with fewer than 200 employees and assets of a certain size. However, distinctions are also made between survivalist firms (90% non-white owned), micro firms (60% non-white owned), and small firms (80% white owned). The vast majority of SMEs in South Africa are informal enterprises operating in the tertiary and service sectors. These differences in size, ownership and business purpose, make it very difficult to make general statements about SMEs .

supply chain relationships or government contracts, have to function within the compliance environment operative in the formal economy. The fact that many SMEs can get away with operating outside of these "formal rules", changes their relationship to ethics. For them, ethics may have more to do with building the kind of trust that enables sustained business relationships. This may not necessarily require reverting to legal compliance mechanisms. It may in some cases even entail building the kind of relationships that can help them resist certain contaminating government practices. For others, ethics is the application and conformance to the existing rules. The differences that exist amongst SMEs have lead researchers to argue that more detailed and targeted initiatives will be necessary to meet the specific needs of specific kinds of SMEs in different contexts. These initiatives must be tailored according to the priorities and objectives that SMEs and their countries have. If the focus is economic development, a much different approach will be required from when the focus is social development, equity and poverty reduction (Jeppesen, 2005: 472).

This also has an impact on how SMEs view their role in society, or how terms like "social responsibility" are understood. Helg (2007) made the important point that Western philanthropy equals business necessity in Africa. Many SMEs respond to the immediate concerns of their families and communities without formalizing it as "CSR projects" or framing it in these terms. Their role in society is described as creating jobs, bringing goods and services to those who need it etc. What this brings us towards, is the realizing that the academic distinctions that we make in order to make sense of SME activity, cannot so easily be "read back" into their actual operations. A mistake that is too often made is to assume that the private sector is similar all over the world. This causes Northern governments and donor agencies to apply their advice, interventions, and policy prescriptions uniformly to situations that are in fact not the same at all. It also discounts the fact that SME owners have different motivations and ambitions in starting and running their businesses. Some may be interested in growth and expansion, but others merely want to provide an economic safety net for their families at certain times of the year (Jeppesen, 2005: 464-465). The dangers of using corporate models of developed countries as a benchmark to judge SMEs have been pointed out by many others (Spence

and Rutherfoord, 2003). Rethinking the way in which ethics and CSR are understood seems to be an urgent priority.

Perrini (2006), for instance argues that research into larger firms' CSR practices typically focuses on how effective corporations manage stakeholder demands. In the case of these large firms, stakeholder legitimacy is required for triple bottom-line success: economic prosperity, social cohesion and environmental protection. Perrini argues that these terms do not translate well to the reality of SME environments and that research on CSR in SMEs should rather be focused on social capital. Social capital focuses on the connections between individuals and depends on the existence of social networks and the norms of reciprocity and trustworthiness that arise from them (Perrini, 2006: 308-309). From Helg's (2007) study into CSR in Nigeria it seems that this holds true, but also extends to larger enterprises. The lack of pressure from consumers and civil society means that stakeholder legitimacy is not a driver of CSR in Africa (Helg, 2007: 10). It would seem that what becomes an important driver is the need to give back to society in an attempt to reverse or overcome "*failures of social capital*" (Helg, 2007: 36). The drivers for CSR are not pressure from stakeholders, but rather aspirations to increased social capital. Spence et al (2003) also stress the importance of social capital in the functioning of SMEs in the UK and Germany. Perrini (2006:308) cites Putnam in arguing that social networks improve the efficiency of society by facilitating co-ordinated action, and generating the norms, virtuous circles, trust, reciprocity, co-operation and collective well-being that conditions ethical behaviour. The conclusions that we drew with regard to enabling and conditioning relationships that are built on trust, underscore this perspective. Perrini provides further support for our contention that local engagement through social and civic activity can be linked to sustainability because it enables and nurtures the trust relationships upon which SME activity strongly relies.

Spence et al (2008) argue that a shift is necessary from the mainstream approach that describes SMEs or entrepreneurial activity as exclusively aimed at economic benefit, towards counter-cultural/critical approaches and reformist approaches. They also point out that the critical approach, which largely rejects the profit-maximizing motives of

entrepreneurs, or the reformist approaches which tend to argue for forms of social entrepreneurship, do not take us far enough. The conclusion that Spence et al comes to, is that entrepreneurship should not be described in bipolar terms, i.e. as either economically motivated or socially motivated as the reality is far more complex. SMEs respond to needs, i.e. their own needs, and those of others, and the focus of their activity may shift over time according to a multitude of factors and dynamics. The needs of entrepreneurs and those they interact with and depend on go far beyond the merely financial. The success and sustainability of the business depend on how well these diverse needs are met over time.

What we would like to argue is that the variety of needs that SMEs typically fulfil embeds social activity within all business activity, instead of making it an additional, add-on constraint on "business-as-usual". UNIDO's (2002: iv) research made it quite clear that CSR must be integrated into the core business strategy of organisations if it is to survive global recession or insecurity. UNIDO argues that "CSR as a philanthropic add-on is vulnerable to cost-cutting". The study uses the case example of Richards Bay Minerals in South Africa to argue that business-community interaction works best if it takes the form of partnerships rather than benevolence. These partnerships are aimed at skills transfer, ownership and self-sufficiency, and is planned and executed at the pace dictated by the community (UNIDO, 2002:44). This research also seems to support our position that corporate social responsibility practices and general business ethics and good governance initiatives are all engaged in the pursuit of sustainable business practices and should be seen as essentially part of the same process. The relational dynamic enables and conditions ethical business practices and fosters the kind of trust required for sustainability. Insofar as SMEs are responsive to social needs, they will also be able to operate within certain ethical constraints and build the kind of long-term relationships that make sustainable businesses possible.

Another question posed in view of the ISBEE conference is how ethics and sustainability may be related in the SME environment in Africa. Our research indicated that there is a very strong relationship, but that this relationship may play out in a different way than in

developed economies. Much of the research on ethics and sustainability within developed economies focuses on the relationship between ethics and financial performance.[5] The terms that these studies employ does not translate so easily to the SME environment. As indicated above, "social" and "ethical" performance is not viewed in exactly the same terms as what is understood by "corporate social responsibility" and "compliance" in developed countries. Therefore studying the relationship between "compliance" dynamics and financial success will not make sense in the same way as it does in developing countries, at least not for those SMEs operating on the fringes of the formal economy. What is clear is that trust needs to be built to sustain business relationships, and that for different SMEs, this may mean somewhat different things. However, what seems to apply to all SMEs is the need to figure out how to sustain the kind of trust relationships that allow them to continue operating over time. In Africa, this trust may be procured in ways that are slightly different from those in other parts of the world.

Fafchamps (1999) argues that market exchange is the most prominent form of resource allocation in Africa. He points out that in developing countries we have to take into account the functioning of different kinds of market forces. Small transaction sizes and the fact that legal enforcement of contracts is unlikely means that businesses have to find ways of sourcing trusted business partners. This is mostly done through long-term trade relationships and business networks where information of other trusted business partners is shared. As Fafchamps states: "Increased trade efficiency can be achieved by emphasizing long-term relationships with other agents and information sharing within business communities." Instead of contract-based reciprocity, African markets involve individuals who form relationships and networks to deal with transaction costs. Fafchamps quotes Granoveter who says: "…markets are embedded in webs of social

[5] See in this regard, Curtis Verschoor, 'Corporate Performance Is Closely linked to a strong ethical commitment', *Business and Society Review* 104(1999), 407-415. Also: Curtis Verschoor, Does superior governance still lead to better financial performance? *Strategic Finance*, 86(2004),13-14 and Curtis Verschoor, Is there financial value in corporate values? *Strategic Finance*, 87(2005), 17-18
Joshua Margolis, and James Walsh, James. Building the Business Case for Ethics. *Bridge paper by the Business Roundtable Institute for Corporate Ethics* (Charlottesville, 2006). Also "Business Case": UNIDO "Corporate Responsibility: Implications for Small and Medium Enterprises in Developing Countries (2002), p.8

relationships that help shape them."[6] This is not to say that "anything goes", because the social relationships provide strong incentives for trustworthy operators and disincentives, such as trade exclusion, for those who disappoint. Fafchamps' approach emphasizes the fact that most institutional approaches to the ethical problems created by what he calls a "flea market economy" focuses on two things, namely relationships, and the sharing of information in communities and networks. In this environment, characterized by high search and verification costs, market participants find it in their interest to enter into long-term trading relationships. The importance of trust relationships is highlighted. Referral systems also play an important role. In this system, it is not necessary to know a person to be informed about that person, as information is typically shared by a common acquaintance who provides a recommendation. Socialization at weddings, funerals, sports events, religious activities and business conferences are also indicated as an integral part of business (Fafchamps1999:7). Networks are central and because of this, the more connected entrepreneurs are more likely to succeed and promote their own network of associates. Nepotism is the inevitable result of this, and small groups of business owners tend to capitalize on this advantage instead of creating broad-based opportunity. However, Fafchamps (1999:9) warns against stigmatizing this form of networking and he highlights the advantages, such as better exchange of information within the group, easier monitoring of compliance with obligations, extra sanctions for deviant behaviour etc. Further research is required to determine how to deal with the negative effects of nepotism, such as the way in which it undermines equal opportunity, whilst maintaining some of the benefits of network trust. A possible research project can be a comparison between the extent of nepotism in formal networks (with explicit ethical codes) as opposed to informal networks.

The question of how the ethical bar can be raised through other forms of business interaction is an area that a number of researchers have covered in more depth. As such, it

[6] Originally, African market exchanges employed the form of reciprocity that operated within gift-exchange, which requires some coordination and concern for the common good, but few explicit obligations (p.1). There was some expectation of reciprocity, but it is more often than not a return in the distant future, it did not need to be equal, and this return was affected in terms of community benefit, not individual profit. Though this reciprocity seems troubling to the Western mind, it is built on a kind of trust and care for the communal fabric of society that merits contemplation.

provides support for our contention that checks-and-balances can be created within the supply-chain relationships that are part of the normal course of business although one has to remain aware of the downsides of these kinds of mechanisms. Fox (2005) indicates the importance of maintaining sustainable supply chain relationships as a mechanism in improving ethical business practices within the SME environment. The establishment of a variety of "business linkages" that facilitate the transfer of assets and skills are also indicated as crucial in the success of SMEs. Raynard et al (2002) acknowledge the role that Trans-National Corporations (TNC's) can play in developing CSR in developing countries' SMEs through their supply chain relationships. At the same time they warn that expensive certification and monitoring required by TNC's can provide barriers for SMEs attempting to enter developed markets. In fact, the rhetoric of seeking the "moral highground" in terms of labour standards may in some cases be a convenient ruse that TNC's employ to pass on the costs for monitoring and auditing CSR standards to their supply chain, who can often not afford this additional burden. This in fact increases poverty instead of advancing sustainable development. The problem with these standards also include the fact that they typically reflect the prevailing technologies and best practices of the countries in which they were developed and are not suited to the SME context in developing countries (UNIDO, 2002: 49).

Before one even gets to the trade barriers that can be imposed by TNC though expensive certification processes, there are other more tangible trade barriers that are not artificially imposed, but relate simply to the ability of African SMEs to be trusted suppliers. International companies will have the same problems in identifying trusted business partners as local African businesses do. 't Hooft (2006) discusses a case where a large European retailer entered into a development project with suppliers in Ghana. The major difficulties identified by the retailer in sourcing business partners reflect those issues raised by participants in our study. This related predominantly to getting continuity in terms of the timely delivery of quality products, in other words, those ingredients necessary for trusted trade relationships. The retailer had the resources to develop the capacity of Ghanaian enterprises to achieve higher standards. African SMEs will need to focus on these issues internally, not only to enter international markets, but also to sustain

local relationships. TNC's can (as part of their international CSR outreach) assist enterprises in achieving these standards, thereby strengthening positive role-modelling in developing countries. This more constructive (enabling and conditioning) relationship between TNC's and African SMEs points to a possible alternative – CSR by trade rather than CSR by exclusion. Some standards and best practices will always be a part of such relationships, but it is important that these be developed with sensitivity to the constraints that SMEs face.

A debilitating relationship that needs to be addressed is the one with government institutions. Macculoch (2001: 10) mentions that in 1996 "*a firm in Tanzania could expect to submit 89 filings per year compared to 21 in Ghana, 29 in Namibia and 48 in Uganda*." While many respondents (particularly from Tanzania) indicated that the situation has improved significantly it is worth reflecting on both the number of opportunities for rent extraction (bribery), as well as the administrative burden that SMEs face in such an environment. Macculoch argues that such a regulatory system creates a disincentive for SME's to grow and join the formal economy. The more formalised they are the higher the regulatory burden. Many of the debilitating relationship issues that were indicated by respondents have their origin in these issues.

6. Conclusions and further research questions:

Our research has brought us to recognize the role that enabling, conditioning and contaminating relationships play in the functioning of SMEs. These relationships influence how these SME's view and respond to ethical challenges and live out their social responsibility. Many of the relationships that could potentially be very enabling, as well as conditioning, are currently in their infancy. The need for peer-to-peer sharing of success stories, skills transfer and mutual support structures seems to underscore the importance of strengthening more formal business networks. However, more informal social and civic networks are equally important in creating the social capital that SMEs need to be sustainable. The development of these trust relationships is crucial in creating the conditions for sustainable SMEs. Our literature review provided further support for

the development of a unique approach to ethics in SMEs within Africa. We argued for the need of relational constraints and multi-stakeholder checks and balances that condition ethical behaviour. We have also found that certain relationships are distinctly contaminating, especially with regards to corruption. A stronger relational bulwark against this kind of contamination is necessary.

Many questions however still remain that will require further research. It has become clear that there are many differences amongst SMEs and that understanding their social role and ethical behaviour depends very strongly on how they view their purpose, what their specific needs are, and what they can afford. For instance, it will be important to distinguish between SMEs of a slightly larger size, operating in the formal economy and the multitude of micro enterprises that function outside of it. It is also important to distinguish SME activity that is aimed at economic development, from that which is mostly concerned with social development. A one-size-fits all approach will certainly not work.

This also raises the question as to how TNCs should approach CSR standards and best practices in their interaction with SMEs. Though TNCs can play a role in raising the bar on ethical practices in SMEs, there is a need to be responsive to the constraints SMEs face. Developing an inclusive process by which standard approaches, models and best practices can be rethought in cooperation and consultation with SMEs in various contexts is long overdue.

Acknowledging the important differences between and within SMEs in Africa also allows us to view CSR and ethical business practices in a different way. SMEs can be socially responsive in ways that do not conform to typical CSR models, and show a concern for “straight-dealing” that cannot be measured in terms of typical compliance mechanisms. In fact, SMEs may be equally concerned with internal and external trust relationships, hence rendering the dichotomy between CSR and everyday ethical business practices void. To what extent this happens in practice, however requires further research.

Another interesting area of research is to determine how the positive peer-to-peer interactions and networking practices that we have been arguing for are to be distinguished from unbridled nepotism that undermines equal opportunity and leads to discrimination against new entrants. Relational dynamics can certainly also become problematic if it undermines fairness and sound fiscal discipline. It seems as if various sets of relational counter-balances will be needed to counteract nepotistic impulses. Exactly how this would work is also a question for further research.

What seems clear though, is that the development of trust relationships is crucial in SME sustainability and that the relational dynamics that could either foster or destroy this trust are always already in operation. It is crucial to recognize this fact in order to strengthen the relationships that have a positive impact on sustainability and to curtail others.

References:

Fafchamps, Marcel: 1999, 'Networks, communities and markets in Sub-Sharan Africa: implications for firm growth and development', *The Centre for the Study of African Economies Working Paper Series*, Paper 108.

Fox, Thom: 2005, *Small and Medium-sized Enterprises (SMEs) and Corporate Social Responsibility: A Discussion Paper*. (IIED)

Helg, Asa: 2007, *Corporate Social Responsbility from a Nigerian Perspective*, Masters Thesis, Handelshogskolon VID Goteborgs Universiteit.

Institute of Directors in South Africa. 2002. *King Report on Corporate Governance for South Africa.* IODSA: Johannesburg.

Jeppesen, Soeren: 2005, 'Enhancing comperiveness and securing equitable development: can small, micro and medium-sized enterprises (SMEs) do the trick*? Development in Practice*, 15: 3&4

Macculloch, Fiona: 2001, Government administrative burdens on SMEs in East Africa: reviewing issues and actions. *Economic Affairs*, 21(2): 10-16

Margolis, Joshua and Walsh, James: 2006, Building the Business Case for Ethics. *Bridge paper by the Business Roundtable Institute for Corporate Ethics* (Charlottesville).

Perrini, Francesco: 2006, 'SMEs and CSR Theory: Evidence and Implications from an Italian Perspective, ' *Journal of Business Ethics*, 67:305-316

't Hooft, Suzanne:2006, 'Up-lifting power: Creating sustainable consumer-driven supply chains through innovative partnerships in Ghana', *Corporate Citizenship in Africa*, Sheffield: Greenleaf

Spence, L.J. and R. Rutherfoord: 2003, "Small Business and Empirical Perspectives in Business Ethics: Editorial", Journal of Business Ethics 47(1), 1-5.

Spence L.J. Schmidpeter R., Habisch A.: 2003, 'Assessing Social Capital: Small and Medium Sized Enterprises in Germany and the UK,' *Journal of Business Ethics*, 47(1): 17-29

Spence, L.J., Blundel, R.K, Zerbinati, S.: 2008, *Entrepreneurial Social Responsibility: Scoping the Territory*. Paper for the ISBEE Congress 2008, Cape Town, South Africa, 15-18 July. Ethics in Small and Medium Sized Enterprises Stream.

Verschoor, Curtis: 1999, 'Corporate Performance Is Closely linked to a strong ethical commitment', *Business and Society Review* 104, 407-415.

Verschoor, Curtis: 2004, Does superior governance still lead to better financial performance? *Strategic Finance*, 86,13-14

Verschoor, Curtis: 2005, Is there financial value in corporate values? *Strategic Finance*, 87, 17-18

UNIDO.Corporate Responsibility: 2002, Implications for Small and Medium Enterprises in Developing Countries (Vienna)