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**ETHICS AS A FEATURE OF ECONOMIC DEVELOPMENT –
FACT OR MYTH**

**ETIKA KAO ODLIKA GOSPODARSKE RAZVIJENOSTI – ČINJENICA ILI
MIT**

ABSTRACT

Business ethics is the reflection of culture and development of countries. Most contemporary economists would agree with Lynn Sharp Paine (2008) who states, in his Value shift, how institutions, especially big corporations, have realized that they are not exempt from sophisticated evaluation criteria. Success and status in market is not measured just by financial indicators but more attentions is given to the companies personality therefore ethics is imposed as an imperative of personality. Criticism towards socially responsible behavior of corporations to employees, consumers and wider community poses high demands on corporations. Corporations are trying to show themselves as socially responsible, consistent in ethical conduct as a basis for success in the long run.

Barković (2009) said that in all transition countries business ethics is very low therefore the top business move was how to deceive opponent, evidence to that lies in the number of failed investments in the eighties.

Examples of lack of ethical behavior have far-reaching consequences to the complete economic success. In the time of economic crises it is more evident relocation of production from developed countries to areas where labor cost are much lower than labor cost in domicile countries. Do ethics have boundaries? Is ethics and to what extent a feature of developed economy? Is ethics form of actions that is not bound to spatial framework of the country or is it ethics a variable which under pressure of success can change, adjust to market conditions? These are just some of the questions that I am trying to give answer in this paper.

This paper shows opinions and views of economists on the subject, research results of paradigm of corruption index and data analysis that show views about role of ethics on the overall performance of economy.

Key words: *ethics, business decision making, recession, country development.*

SAŽETAK

Poslovna etika je odraz kulture i razvijenosti zemlje. Većina suvremenih ekonomista složila bi se s Lynn Sharp Paine (2008.) koji u svom djelu Value shift navodi kako su institucije, posebice velike korporacije, shvatile da ni za njih više ne vrijedi izuzeće od sofisticiranih kriterija procjenjivanja. Uspjeh i status na tržištu ne mjeri se samo financijskim pokazateljima, naprotiv sve veća pozornost posvećuje se osobnošću korporacije, pa se time sve više kao imperativ osobnosti nameće etika. Kritičnost prema društveno odgovornom ponašanju korporacija prema zaposlenicima, potrošačima i široj zajednici, postavlja pred korporacije visoke zahtjeve. Korporacije se sve više trude prikazati uređenim, društveno odgovornim, te dosljednim u etičnom postupanju, kao osnovom za usješćenošću na dugi rok.

Barković (2009.) navodi da je u svim tranzicijskim zemljama poslovna etika jako niska, pa je vrhunski poslovni potez bio kako prevariti protivnika, čemu je dokaz obilje propalih investicija u gospodarstvu osamdesetih godina prošlog stoljeća.

Primjeri izostanka etičnog ponašanja imaju dalekosežne posljedice na ukupnu gospodarsku uspješnost. U vremenu gospodarske krize sve je očitije izmještanje proizvodnje iz razvijenih zemalja u područja u kojima je cijena rada znatno niža od cijene rada u matičnoj zemlji proizvođača. Ima li etika granice? Je li i u kojoj mjeri etičnost odlika razvijenog gospodarstva? Je li etičnost obrazac postupanja korporacije koji nije vezan uz prostorni okvir zemlje ili je etičnost varijabla koja se pod pritiskom uspješnosti može mijenjati „prilagođavati“ uvjetima na tržištu? Ovo su samo neka od pitanja na koje nastoji odgovoriti ovaj rad.

U ovom radu analizirana su mišljenja i stavovi poglavito ekonomista o ovoj temi, rezultati istraživanja paradigme indeksa korupcije, te su analizom podataka izneseni stavovi o ulozi etike na ukupnu uspješnost gospodarstva.

Ključne riječi: etika, poslovno odlučivanje, recesija, razvijenost zemlje

1. Introduction

Ethics basically defines rules of moral beliefs, gives critical review, imposes reflection and questioning of views. Ethics raises the question of choices, it defines priorities. Regulated societies are defined by high standards thus high degree of defined “rules of the game”. Kregar (2008) states that “Capitalism does not mean lack of moral requirements and legal standards.” On the contrary, it presumes proper functioning of institutions, rational, effective and legitimate law and moral attitude. Besides that, he assumes that the basis of acquisition is work, dedicated work, and work as a life calling. By Kregar “market economy and capitalistic enterprise demand careful balance between self-interest and profit orientation, between pretense and resourcefulness, on one hand and toward honesty, modesty and diligence, on the other.”

Recession and drop of economic activity on one side are imposing the need to fight for every customer, best service, the most quality product; on the other hand, it imposes the need to think about the costs. Competitiveness, globalization, speed of information dissemination gives the option of choice both for the customer and for the enterprise. Cost reduction in the time of economic crisis becomes imperative, so the question of ethics takes new dimension. The paradigm of ethical and unethical behavior is determined by cultural, and personal experience, as well as a system of values that each person carries. Prism of problem considering changes with our role in it, that is how Truman Harry, S. (1952) states. “Recession is when your neighbor loses his job and depression when you lose yours.”

According to Weber, M (1934) “Capitalism is not based on unlimited greed. Greed creates bandits not entrepreneurs. Capitalism destroys societies of tradition but creates new and developed societies, new morals. The universal rule of absolute dishonesty (*absoluter Skrupellosigkeit der*

Geldmachung) in gaining money was specific characteristic of countries whose civic and capitalistic development – by western development was “backward”.

2. Market economy and ethics

Market economy gives the choice of better, more quality, cheaper or by any other criteria desirable product for consumer. Based on competition, is basing on selection. Solidarity is not characteristic of market economy therefore slower or those who less successfully recognize changes in environment or/and not react quickly enough to the same, are failing. By comparing ethics and economics, Babić (2002) says “common denominator of ethics and economics rests in part on the assumption of rationality that is the result of human free will and the ability to rational reasoning and evaluation that they are inherent properties that distinguish humans from other living beings”. Fruther, Kregar J. (2008) says how “capitalist entrepreneurial freedom does not mean just possibility of freedom (in sense that it is allowed what is not forbidden) but also a burden of making self-decision in the light of community moral standards (because one cannot do what freedom allows, but moral prohibits). Capitalism that has emerged without presumptions of developed societies (in sense of elementary honesty), rule of law (*Rechtsstaat*, *rule of law*) and social solidarity (reciprocity), to survive in global environment must fight for these values.”

Father of modern economics Smith (1759) states that a human being is capable of making moral judgments based on compassion and not only on the basis of selfishness. It is compassion that opens space for moral and ethics. Market economy does not include just producers and consumers, it includes all those in the process, hence employees, environment and wider community.

Aleksić (2007) says that successful international and domestic organizations became aware of the fact that in the competitive arena business ethics allows growth and development, increases efficiency and productivity. Many studies have shown that business ethics and profitability are not mutually exclusive and companies that incorporate business ethics in their business system show better results than those that did not do so.

Karpati (2001) states that business enterprise encounters many obstacles, but consistency in decision-making in the context of ethics brings long-term results.

3. "Enron scandal" the question of ethics and business decision making

Enron is a company whose ruin represented the biggest bankrupt in American history. Enron was the 18th biggest company in the USA; it was dominating in the energy sector in USA as well as in the world. With its downfall 4500 people lost their jobs, tens of thousands investors in Enron shares lost their money, because its value from 90\$ per share in August 2000 fell to just 26 cents per share at the moment of Enron collapse. Enron has for years cheated its investors and business partners about successfulness of their business performance by showing false data in their bookkeeping, transferring their debts to companies that were formed by their leaders with international partners, whose books were hidden from independent auditors. Based on false records they received credits from banks and financial funds, sinking deeper and deeper until finally, when big deceit was discovered, ruined many. About 11.000 Enron's employees and former employees lost their pension, because all the Enron pension funds have collapsed, since they were prohibited to own anything else except Enron shares, therefore they could not sell them to buy different shares to make the whole fund much safer. While company was sinking into ruin, leaders were increasing their paychecks and bonuses. Chairman of Enron Kenneth Lay, whose wealth was estimated to 123 mil. \$ only in shares, plus some more tens of million in real-estates and other values, increased his salary in 2001 and just in that year acquired another 25mil.\$. Just a few days before the final bankrupt 500 leading executives and managers paid bonuses worth of total 55 mil.\$.

An example of Enron is very often mentioned in the context of ethics as a good example, how unethical behavior is not worth in the long term, because the fraud is eventually discovered, and the consequences of such behavior are immeasurable.

The impact of this example to the wider community, to former employees, business partners, financial funds etc. was enormous and it is certain that these stories raise issues of morality, ethics and different attitude of environment towards companies and their business.

These kinds of stories are influencing the change of behavior of community to ask questions about responsibility of employees that knowingly failed regardless of their passive or active role in it, but also raising questions of oversight in control both banks and government that had to notice and react to such omissions. Such experiences encourage higher criticism of the company's business in the environment, call for disengagement and even condemnation of other companies, but also the need to build business identity on other principles. However, the question is what is the comfort to all those who in this story were doing honest work and earned their salary, to lose everything because of unfair game of part of employees?

Furthermore, the question arises, if consistency in ethical business is worthwhile, can companies that are doing ethical business in the time of recession survive. If they can, why then examples of successful businesses show tendency to invest in countries where labor costs are lower, and are very often using their position and power of money to exploit.

Why so far the developed habit of critical thinking about modern capitalism did not, with its decisions and consumer decisions to avoid such products, brought change in behavior, imposed new models of behavior in transition economies?

4. Analysis of corruption index and development of country

Corruption index as an indicator of the degree of "moral depravity" or unethical in one country is an indicator of organized country or degree of its readiness to identify, prevent and condemn unethical behavior especially public sector. Transparency International defines corruption as abuse of public service for personal gain. Štimac (2004) says that corruption is reflected as a brake of progress, since it retains acquired privileges of individuals at the expense of overall gain, it "legitimizes" individual usurpation of public goods and wealth, discourages creativity and entrepreneurship, encourages young and talented individuals to emigrate, and also creates inequalities. Corruption is presumed one of the main reasons why investments are avoiding certain countries, and today European Union requires of their candidates willingness and readiness to battle corruption. These kinds of demands were stated in Dayton agreement, Pact of Stability and Cooperation as well as in European Union programs such as CARDS. When analyzing all the previously stated reasons question arises if the corruption and unethical behavior are something bad, why is it so difficult to put an end to such generally accepted "bad" behavior?

Answers to this question primarily we need to find in the cause and circumstances of their formation. Štimac defines causes and circumstances for favoring the corruption in transitional and democratic countries. As causes and circumstances in transitional countries are given old relationships to everything common and social, breakdown of system of state and "social" ownership, creation of atmosphere for "free predatory competition" in privatization and denationalization of the will of former communistic personnel to keep their power and privileges; lack of knowledge and experience of state and its mechanisms and institutions in citizens that for the first time have the opportunity to be in the politics; unclear and very often contradictory rules and loopholes in the law as a result of ignorance for the matter that needs to be legally regulated, too much rules, too much possibilities for political interference, lack of public opinion and their controlling role, lack of open market as a measure and regulator for competition, lack of anti-monopolistic laws etc. On the other hand, developed democratic countries are characterized by globalization of economy and internationalization of financial market, "new products", privatization of some former public services, at times even decentralization that draws into public affairs more people than before that leads to accumulation of elective functions which makes

politicians actions less transparent and finally there is the question of financing of political parties and their election campaigns which in many countries are not clearly regulated by law.

Analysis of the real sector (businesses) shows how the ethics in business decision making is highly correlated with the development of the country. Real and public sector constitutes one economy, therefore ethicality of one reflects on the ethicality of the other because one criticality within the economy develops over time and is not related to the business sector, but rather in a way of thinking about the basic principles of business. Table 1 shows results of an analysis conducted in the countries of Europe. Croatia is not in this table, because by application of this new methodology new report puts her in the countries of Eastern Europe and Central Asia. Nevertheless, data for Croatia are analyzed below.

Table 1 The review of the Corruption Perceptions Index in the countries of Europe in 2012.

Country Rank	Regional Rank	Country Territory	CPI 2012 Score		Surveys Used	Standard Error	90% Confidence interval		Scores range	
							Lower	Upper	MIN	MAX
1	1	Denmark	90		7	2,0	87	93	83	98
1	1	Finland	90		7	3,0	85	95	83	100
4	3	Sweden	88		7	1,9	85	91	82	97
6	4	Switzerland	86		6	2,6	81	90	73	90
7	5	Norway	85		7	1,6	82	87	78	89
9	6	Netherlands	84		7	2,0	81	88	73	89
11	7	Iceland	82		6	4,1	75	89	71	98
12	8	Luxembourg	80		6	2,8	75	85	71	89
13	9	Germany	79		8	2,3	75	83	73	89
16	10	Belgium	75		7	2,4	71	78	71	89
17	11	United Kingdom	74		8	1,3	72	77	69	81
22	12	France	71		8	2,4	67	75	57	79
25	13	Austria	69		8	2,4	65	73	59	79
25	13	Ireland	69		6	3,5	64	75	54	78
29	15	Cyprus	66		4	2,4	63	70	62	71
30	16	Spain	65		7	2,9	60	69	52	73
32	17	Estonia	64		8	3,0	59	69	50	75
33	18	Portugal	63		7	2,5	59	67	54	73
37	19	Slovenia	61		8	3,9	55	67	45	73
41	20	Poland	58		10	2,0	55	62	47	65
43	21	Malta	57		4	2,4	53	61	52	63
46	22	Hungary	55		10	3,5	49	61	37	71
48	23	Lithuania	54		7	5,3	45	63	31	71
54	24	Czech Republic	49		10	2,9	44	53	34	62
54	24	Latvia	49		6	4,0	42	55	31	58
62	26	Slovakia	46		8	4,3	39	53	30	62
66	27	Romania	44		8	3,7	38	50	32	60
72	28	Italy	42		7	2,4	38	46	37	55
75	29	Bulgaria	41		8	3,8	35	47	29	62
94	30	Greece	36		7	3,6	30	42	21	49

Source: <http://www.transparency.org/research/cpi/overview>

Latest survey of global corruption index conducted in the end of 2012 shows that Croatia with 46 points is in the upper half of the countries but significantly below the average of the European Union. This result indicates that the new, updated and substantially more precise methodology, which is based on the findings of a number of independent expert institutions from around the world,

Croatia is on the degree of perception of corruption in the public sector and among politicians on the 62nd place in the world among 176 surveyed countries with 46 out of 100 possible points. Although 46 score is far below average of European Union, Croatia is better than Italy, Rumania, Bulgaria and Greece but weaker than Slovenia. It is interesting a high placement of Austria – 25th on the scale with 69 points or Finland that shares first place with 90 points. Curiosity comes from the fact that in the time of data release there was a trial in Croatia for a corruption case of former Prime Minister for the commission on the Austrian Hypo bank loan as a substitute for privileged position in the Croatian market. Likewise, Finnish Patria was suspected of corruption of the Slovenian politicians about procurement of Finnish armored vehicles.

Even though corruption index is based on assessment, and assessments are always subjective, Štimac (2004) states that “rich and those who “in their own homes” do not bribe are either incorruptible, since they possess live public opinion and effective justice, or often most aggressive bribers in poorer parts of the world”. Furthermore companies from USA or France aren’t any better than those that come from, for instance, Singapore. Krstić (2012) says how Croatia not only has problems with its own corruption but also from its import. The problem is that import of corruption comes from so-called developed countries with high democracies and high scores, wherein when capital is coming it looks for a suitable ground, it seeks associates that will not ask too many questions, that will be well paid to do their jobs even if it would harm the country where the project is realized, but to work for the gain of that capital.

5. Conclusion

Regulation of the country is reflected in its standards, but also the mechanisms by which it monitors, condemns and regulates forms of deviant behavior in relation to what is considered socially acceptable. Criticality in the evaluation on the one hand, but also corporation effort that within their own environment have regulated organizations whose decisions are based on principles of ethical behavior, are the features of developed countries. Self-criticism of large corporations is the basis for business decision making will they choose to invest in the country that is prone to corruption, that is country prone to “look through the fingers”, perhaps even support unethical behavior. Basic setting for market play is adjustment to market conditions, corporations from developed countries show large degree of skill and resourcefulness in identifying potential issues from the environment, as well as turning them into a challenge. Competition to these businesses, gives skill and with time experience to overcome the most difficult obstacles. In an effort to sustain their position in the market, these businesses decide to spread their activity to the areas where tolerance threshold to unethical behavior is higher. Desire for success ability to recognize potential problems and turn the minto challenges set before these corporations yet another new challenge; to change the environment they are coming to and try to enforce rules and behaviors that they apply in their home country or retreat from its own pattern of behavior, and put their own performance in front of the issue of ethics.

Analysis of corruption in transitional countries shows tendency of big corporations, to use unethical behavior in those countries where the same is not prohibited, question arises about limits where the ethics begin and where end. Ethics is a set of acceptable behaviors, which bring order, clearly define rules of the game and put consistency in front of corporations that encourages its use as a basis of business decision making. Ethics should not be determined by borders, corporations should build their identities on what it is, respecting the specificity of countries in which they are investing and respecting the man in the same way as in their own countries. Ethical company should be a promoter of new system of value, even if the environment inclines to unethical behaviors. However, companies are made of people, with all their virtues and flaws, as well as the tendency to, more or less apply their own forms of deviant behavior in countries that are suitable ground for such activities. Business ethics is culture of conduct that takes acquiring and built, and first of all, it takes time. Time and globalization carry new information, and with development of criticality and own

attitude to ethics, business decision making as well as systematic value that will accept, transitional countries have the possibility to determine their own acceptable and undesirable behaviors.

From previously mentioned it is possible to derive some conclusions. First of all, criticality is possible in societies that have tradition and experience in defining criteria what is and what is not moral (ethical). Some international examples show how the attitude toward corruption is not possible to derive general conclusion, especially if we are aware that corruption index is based on assessment. This experience does not happen overnight, it builds upon gradually, primarily on painful experiences such as Enron. These kinds of experiences impose the need not just for deeper analysis but also for clearly defined set of rules, adoption of ethical codes as a written proof that company that has them was defining their own set of values, and that that set of values is clear and transparent. Having an ethical code does not mean that corporation is using it, but just the thought it self to set an ethical code is a reflection of management awareness and attitude to ethical and unethical behavior. In the age of globalization in modern societies, informations are available and fast, so negative trends draw reactions that can have far-reaching consequences. In this kind of environment, most companies will decide to have correct business relationship based on ethical (moral) principles. At the same time, countries that have lower labor costs, which are for that matter more interesting to foreign investors, often do not have enough experience or accept these predetermined rules out of necessity. Price that they are paying is not fair, but that is the price for gaining healthy critical thinking, that takes time. Companies that invest in countries with low labor costs, give people the choice, minimal wage is better than losing a job. It is questionable whether the owners and executives of such companies are always happy about their business decision even if they gain financial result. Even though such companies are building a reputation of successful ones since they are well accepted in the countries they invest to, also in their own countries because of the business result and taxes they are paying, in the end every company is made of people. No matter how much they deny this sense of discomfort, even if they justify it by their successfulness, management that is made of people know or at least sense that the set of rules they are implementing are not correct, and they are always fearing that they will be discovered and what would be the reaction of the customers of their services in their own countries to their hypocrisy. We should not believe that business decisions will not be discovered, time is always an ally of the truth, and therefore it is questionable whether the profit made in such short term can justify the loss of trust forever. Although ethical behavior as a pattern of behavior is expected from corporations that originate from developed countries, it is not necessarily so. Ethical behavior is not so much conditioned by the origin but more on the system of values that accepts or refuses certain forms of behavior. Even though there is a tendency of corporations to change their behavior in less developed countries, yet the assumption is that such changes are exceptions not the rule, so the majority of corporations will choose business setting where they feel safety of operations and regulated system.

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