



## SUSTAINABILITY WITHIN SMES: AN OVERVIEW OF THE PERCEPTION OF ENTERPRISE SOCIAL RESPONSIBILITY BY PRACTICING SME MANAGERS.

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### Abstract

*The Small and Medium Enterprises (SMEs) play a vital role in triggering economic growth and equitable development, particularly in developing countries like India. Though their significant economic contribution of SMEs is well understood, their responsible business practices have not been extensively studied for any meaningful interpretation. Individually each of these SMEs may not have a significant influence like large corporates whose cumulative social and environmental impacts are significant. Many company's Sustainability initiatives, particularly CSR are disparate and uncoordinated, run by a variety of managers without the active engagement of the CEO. Such firms cannot maximise their positive impact on the economic, social and environmental systems in which they operate. The main question is how the SMEs are socially, economically and environmentally responsible to their stakeholders and external constituents and how they perceive and act on their other normative responsibilities. How SMEs are responsible to their external stakeholders including their cultural, social or governmental relationships in ways that coincide or conflict with their obligations to the other primary stakeholders, eg. their employees, owners, customers, and suppliers. There is an urgent need therefore to understand the responsible business practices adopted by the SMEs. Much of the Anecdotal evidence on SMEs in the world over appears to suggest that the ethical orientation of the SMEs is a product of the ethical orientation of its owner. What they do is what they believe. Therefore this paper attempts to examine the perception of Sustainability Practices on SMEs by analysing the motives of implementing ethical and CSR practices by practicing SME managers.*

### Introduction

Small and Medium enterprises have been playing an important role in the overall economic development of a country like India, where millions of people are unemployed or underemployed. As per a recent survey SSI Sector comprises of 95% of the total industrial units in the country. In India Small and Medium industries occupy 12.3 million units, contribute to 40 percent of industrial production and 35% of their exports.(Facts for you Pge.24). In countries like India where the disparity levels in income are quite stark and the industrial growth has not been widespread and uniform, the role of the SMEs in creating employment is quite significant. They also provide lively hood opportunities through simple, value – adding processing activities in agriculture based economics, nurture entrepreneurship and economic systems, through linkages with the large enterprises. (Vasanthi IIMB 2010). Many large scale organizations depend on the SMEs for the supporting spare parts and raw materials

While their economic contribution is well understood with their supporting available data, their responsible business practices have not been extensively studied. Within the business ethics field, the presumption of the unit of analysis as a large firm has always been the norm. Unfortunately, there is much less to report in terms of research on CSR or Sustainability practices on Small and Medium sized enterprises. SMEs are facing many ethical challenges that seriously compromise the contributions they could make to the long term economic well being of their communities. Ethics is always concerned with the good, the self and the other (Rossouw, 2002).SMEs emerge as a response to personal or community need in the absence of other opportunities of formal employment, or other access to goods and services. (Mollie painter).

### SMEs vs large Corporations

There is a growing consensus that SMEs demonstrate distinctive characteristics which make them different from large organizations According to Wyncarczyk etl(1993) there are three ways in which small firms differ characteristically from large firms :- they are in terms of uncertainty and vulnerability, active engagement in innovation, and in terms of evolution and change. Compared to large corporations SMEs are :-

- Independent and owner managed
- Stretched by a broad range of tasks
- Limited cash flow
- Facing persistent survival challenges
- Built on personal relationships
- Mistrustful of bureaucracy and controlled by informal mechanisms



SMEs have to juggle the normative concerns that are part of their every day practices much more carefully, and without the necessary institutional support and resources to which larger companies have access. Therefore the content, nature and extent of their participation in SR practices and ethics is likely to be different. (Jenkins, 2006).

### **Definition of SMEs**

SMEs are defined in different ways in different parts of the world. Some define them in terms of assets, while others use employment, shareholder funds or sales as criteria. Some others use a combination of revenue and employment as a hybrid criterion. In India, it is defined in terms of investment in plant and machinery. The MSME act of 2006 defines them as

- Enterprises engaged in the production/manufacturing of goods for any industry
- Enterprises engaged in rendering/providing services

Enterprises in the manufacturing sector are defined in terms of investment in plant and machinery (excluding land and buildings) and further classified into

Small enterprise – investment up to Rs. 2.5 million and Rs. 50 million

Medium enterprises – investment between Rs. 50 million and Rs. 100 million.

Service Enterprises : defined in terms of their investment in equipment and further classified into

Small enterprises – Investment above Rs. 1 million and up to Rs 20 million

Medium enterprises – Investment above Rs 20 million and up to Rs. 50 million

The clarity in definitions help in clearly charting various focused programmes and policy interventions for the various categories of firms.

### **The Concept of Sustainability**

According to Global Reporting Initiative (GRI) the goal of sustainable development is to ‘meet the needs of the present without compromising the ability of future generations to meet their own needs’. The Key indicators of sustainability are Economic Performance, Social performance and Environmental Performance. It is also known what is being with regard to the three Ps ie, People, Profit and Planet. Another term generally used is triple bottom line performance.

The economic dimension of sustainability concerns the organization’s impacts on the economic conditions of its stakeholders and on economic systems at local and national level. Financial performance is fundamental to understanding an organization and its own sustainability. The Environmental dimension of sustainability concerns organizations’ impacts on living and non living natural systems, including ecosystems, land, air, and water. Society performance focuses attention on the impacts organizations have on the local communities in which they operate. It is the risks associated with bribery and corruption, undue influence in public policy – making etc.

Large scale firms are guided by GRI to publish annual sustainability reports based on the triple bottom line parameters. Several studies have been done to analyse the quality of the sustainability reports published by them. The GRI now has come out with certain guidelines for the SMEs to follow certain codes of conduct using the GRI G4 guidelines and make a report on the sustainability practices.

### **Sustainability Practices and Ethics in India**

There is a clear documentation of sustainability practices in large organizations in India. (Mitra, 2007, Sood & Arora, 2006). In recent years, CSR in SMEs in India has been gaining increased attention from practitioners, NGOs and international agencies, but not significantly scholars. In a recent study conducted on CSR practices it was found that while large multinationals had formulated a CSR policy, which they make it public, CSR is not at all institutionalised in SMEs. The reason for the lack of institutionalisation of CSR include limited resources to CSR, lack of pressure from the customer and inability of see any direct benefit in doing CSR.

Much of the documented evidence suggest that the ethical orientation of SMEs is a product of the ethical orientation of its owner. And therefore we can conclude that the owners/managers in SMEs determine the ethical orientation of the firm.

There are a few studies examining the value orientation and ethical dimensions of Indian managers in large corporations. Chavan & Lamba, 2007 examined the cultural influences on the judgement of Australian, Malasian and Indian SME managers to whistle blowing as an internal control mechanism.

In another study done conducted in the Pune Industrial belt in Western India, it was found that compliance to the Government laws was seen as being socially responsible. Many SME owners were of the opinion that philanthropy and CSR are one and the same. Ravenkar, 2004 said that many of the SMEs are at a stage where they are struggling to establish themselves and do not have the manpower or resources to address these issues. In a comparative study undertaken on constraints and



contingencies of small businesses in Bangladesh and India, the authors found that many SMEs had similar constraints and contingencies across countries and bribery related variables tended to be fairly similar (Amin & Bannerjee, 2007).

Tarun Kumar, 2004 conducted a survey in an Industrial cluster in northern India, and he found that since most SMEs were led by owners, the value system and philosophy of the owner played a significant role in determining the CSR practices undertaken. Many of the SMEs were unable to see any clear benefits by following or practicing CSR. Very few companies had social reports, codes of conduct or stated ethical practices. But the study explores that many of the SMEs are involved in some kind of developmental activities. Many CEOs of these SMEs were members of Rotary or Lions Clubs and supported various developmental activities initiated by these clubs.

In a study conducted by the UNIDO (2008) on CSR perceptions and activities in SMEs in five industrial clusters in India, it was found that regardless of the geographical region they hailed from, SMEs tended to behave similarly towards CSR. Many of them considered 'taking care of their employees internally' and 'being involved in community welfare' as their CSR responsibility. Vasanthy Srieenivas IIMB, says that 'the influence of the personal values of the entrepreneurs in determining the choice of CSR activities found support'. When markets and large businesses put pressure of the SMEs, they are forced to follow certain CSR practices such as worker education, health and safety compliance which are undertaken in the normal course of business.

The role of cluster wise sustainability practices assumes relevance now. The leather cluster for example is plagued by pollution. The operations in leather tanning – washing, stripping, bleaching, chrome tanning and basification – involve the use of very toxic chemicals and its effluents tend to pollute ground water. The adoption of common effluent treatment plants and eco-friendly technologies has not become very widespread due to the lack of awareness among small firms and also partly due to lack of enforcement of environmental laws among small players (EXIM, 2000).

### **Why SMEs**

The Small and Medium Enterprises significantly contribute to India's economic growth. These serve independently and as ancillary to a large firms and help generate employment and industrialise the rural and backward regions of India. They employ nearly 40% of India's work force and contribute around 45% of India's manufacturing output.

The field of Business ethics and sustainability is usually centred around large, specially multinational corporations (MNCs) as the primary unit of analysis. Some of the aspects are transferable to SMEs also. Still, these small companies have their own frames of reference. They are almost always close to the communities they operate. They are usually local, not global companies. They are family-owned or owned by a small group of investors or entrepreneurs rather than by anonymous shareholders. So the internal and external stakeholder relationships have to be redefined for SMEs.

The business activities of SMEs are performed in proximity to the locals. This enables them to be aware of local needs, manage expectations and develop sustainability programmes appropriately. Now that the CSR clause in the Companies Act, 2013 covers companies that have a net profit of five crore INR and above, it is expected that while micro enterprises will not qualify, many small and medium enterprises (SMEs) will.

The sustainability practices of these enterprises are driven by the personal interests of promoters who hold a significant financial stake in the business. They tend to be in clusters and engaged in similar business activities. While the quantum of revenue available for CSR with individual SMEs is expected to be small, all eligible companies in a specific geographical cluster, who single handed as well as collectively impact the same community, can pool their resource to create a sizeable CSR fund.

### **Enterprise Social Responsibility**

Not only Corporations which are major firms, be responsible for CSR activities, Small and Medium Enterprises too need to lend their share in carrying out responsible business. As the study is based on CSR in SMEs, the term is coined to suit to the SMEs.

### **Methodology.**

A questionnaire was developed including the motives and business benefits arising out of sustainability practices based on academic literature and business benefits on the activities that were pursued as ESR. It was distributed to organizations in north Kerala and some telephonic interviews also were carried out. The information is collected using both primary and secondary data.

Sample Profile. Table 1.

|           |               | Frequency | Percent |
|-----------|---------------|-----------|---------|
| Age       | less than 30  | 37        | 11.2    |
|           | 31-35         | 45        | 13.6    |
|           | 36-40         | 30        | 9.1     |
|           | 41-45         | 52        | 15.8    |
|           | 46-50         | 102       | 30.9    |
|           | more than 50  | 64        | 19.4    |
|           | Total         | 330       | 100.0   |
|           |               |           |         |
|           |               | Frequency | Percent |
| Education | SSLC/Plus Two | 33        | 10.0    |
|           | Graduate      | 84        | 25.5    |
|           | Post Graduate | 86        | 26.1    |
|           | Diploma       | 73        | 22.1    |
|           | Technology    | 48        | 14.5    |
|           | 6             | 6         | 1.8     |
|           | Total         | 330       | 100.0   |
|           |               |           |         |
|           |               | Frequency | Percent |
| Gender    | Male          | 274       | 83.0    |
|           | Female        | 56        | 17.0    |
|           | Total         | 330       | 100.0   |
|           |               |           |         |
|           |               | Frequency | Percent |
| Education | SSLC/Plus Two | 33        | 10.0    |
|           | Graduate      | 84        | 25.5    |
|           | Post Graduate | 86        | 26.1    |
|           | Diploma       | 73        | 22.1    |
|           | Technology    | 48        | 14.5    |
|           | 6             | 6         | 1.8     |
|           | Total         | 330       | 100.0   |

Descriptive Statistics . Table 2.

|                                     | Mean | Std. Deviation | Analysis N |
|-------------------------------------|------|----------------|------------|
| Increase profits                    | 3.00 | 1.205          | 330        |
| Long term sustainability            | 4.02 | .969           | 330        |
| Company tradition                   | 3.43 | .944           | 330        |
| Recruit/retain employees            | 3.51 | 1.005          | 330        |
| Attract Investors                   | 3.42 | 1.122          | 330        |
| Promote transactions/partnerships   | 3.33 | 1.053          | 330        |
| Enhance community trust and support | 4.11 | .973           | 330        |
| Avoid regulation                    | 2.76 | 1.119          | 330        |
| Enhance reputation                  | 3.85 | 1.065          | 330        |
| Favourable media coverage           | 3.15 | 1.186          | 330        |
| Improve public welfare              | 4.03 | .987           | 330        |
| Altruism                            | 3.90 | 1.003          | 330        |
| External pressures                  | 2.83 | 1.148          | 330        |
| Competitors are doing               | 2.90 | 1.250          | 330        |
| Buyer expectations                  | 3.22 | 1.074          | 330        |

## Results

Among the factors described above Improve public welfare scored the highest mean of 4.03. Followed by Long term sustainability. Enhance community trust and support holds a major opinion of 4.11 mean. Avoiding regulation and competitors are doing holds the least mean. The summaries and respondents with their mean score and standard deviation has been given in the table 2 descriptive analysis.

A factor analysis has been carried out to explore latent factors that motives in undertaking ESR activities. A total of 5 factors has been identified and explained. These factors have been named as External stakeholder management, Internal stakeholder management, long term sustainability and reputation. These five factors disclose the overall perception of ESR by practicing managers. A summary of the factor analysis has been given in Table.3.

**Table 3. Rotated Component Matrix<sup>a</sup>**

|                                     | Component                       |                                 |                |                          |            |
|-------------------------------------|---------------------------------|---------------------------------|----------------|--------------------------|------------|
|                                     | External stakeholder management | Internal Stakeholder management | Public Welfare | Long term Sustainability | Reputation |
| Increase profits                    |                                 | .538                            |                |                          |            |
| Long term sustainability            |                                 |                                 |                | .627                     |            |
| Company tradition                   |                                 |                                 |                | .685                     |            |
| Recruit/retain employees            |                                 | .768                            |                |                          |            |
| Attract Investors                   |                                 |                                 |                | .497                     |            |
| Promote transactions/partnerships   |                                 | .540                            |                |                          |            |
| Enhance community trust and support |                                 |                                 | .647           |                          |            |
| Avoid regulation                    |                                 |                                 |                |                          | .592       |
| Enhance reputation                  |                                 |                                 |                |                          | .720       |
| Favourable media coverage           |                                 |                                 |                |                          | .467       |
| Improve public welfare              |                                 |                                 | .693           |                          |            |
| Altruism                            |                                 |                                 | .642           |                          |            |
| External pressures                  | .800                            |                                 |                |                          |            |
| Competitors are doing               | .752                            |                                 |                |                          |            |
| Buyer expectations                  |                                 | .565                            |                |                          |            |

## Findings and conclusions

The study supports the earlier studies that long term sustainability, Enhance community trust and support, Improve public welfare are some of the motives that have been mostly picked by the SME managers.

SMEs emerge as a response to personal or community need in the absence of other opportunities of formal employment, or other access to goods and services. Sustainability could be positioned at the very heart of SME activity. Sustainability concerns go far beyond the sustainability rhetoric employed by some larger corporations in the first world.

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 (un-coordinated) and are not as 'hyped' as corporate CSR projects.

The dark side of the responsiveness to need is the fact that many SMEs might be operating as 'survival morality', which by definition is concerned with 'bread first, morals later'. The argument is that ethics will be compromised if there is any business advantage to be had. 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.

Regarding the understanding of the notion of 'ethics in SMEs', the theme that emerged most strongly related to 'honesty', straight dealing' and 'not cheating'. Another prominent theme referred to governance issues such as proper accounting, auditing and honest taxpaying. Another issue was labour issues which reflects on 'how they treat their staff' On important ethical problems or issues for SMEs - responses were related to administrative dishonesty and labour issues. The issues



which are highlighted in administrative dishonesty are corruption, tax avoidance, misrepresentation in audits, and ignoring licensing procedures. These issues relate to relationship with Government institutions. The labour issues are centred on fair wages and the treatment of the staff. It includes disrespect for the staff as well as poor working conditions. Other issues are employing under aged workers, not allowing freedom of associations, not providing proper benefits or job security and indulging in tribalism. The third ethical concern relate to the quality of goods and services. These include over pricing, misrepresentation in terms of product quality, and selling pirated goods.

When enquired about the factors that make ethics difficult, it was found that unethical behaviour is very often is a 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 serious challenges they face. Of these, the most serious factor was corruption in interactions with the government as they have to constantly interact with the government as they have little or no bargaining power.

Competing with unethical competitors is another concern. There is a shortage of positive stories and role-models. Lack of quality controls, delays, and inconsistency in pricing are inevitable side-effects of SMEs emerging in such an environment. Respondents in the study indicate that many of the ethical problems have a direct impact on the sustainability of businesses. According to them the following factors hinder long term business relationships – poor quality products, short term thinking, lack of business experience or management skills, and inconsistent delivery from suppliers. On the other hand, honesty, reliability and professionalism amongst small business owners were identified as factors that facilitate long term business relationships.

The factors 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. Since SMEs contribute significantly to the economy and are geographically widely spread in a country like India, their adoption of Sustainability and ethical practices is crucial for a balanced development. The present clearly identifies the fact that there are many differences among the sustainability practices of SMEs and large scale organizations. While large scale organization or companies with more than 5 crore profit for a period of three consecutive years, have to set apart 2% of their profit for CSR activities. Therefore SMEs' understanding of sustainability practices depends on how they view their purpose, what their specific needs are, and what they can afford.

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