

SURVEY OF ETHICAL BEHAVIOUR IN HUNGARIAN METAL AND MACHINERY SUPPLY CHAINS

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Abstract

In today's business world, ethics and responsibility appear as vital value. Globalization of markets, free access to information, and increasing social and environmental problems have an impact on global ethics, and urge the integration of ethical issues into everyday business practice. In this article, we present the results of our qualitative investigation of business ethics at network level. Our research involves experts from the Hungarian metal industry and machinery supply chains as well as corporate executives; we ask them on the role of ethics and ethical behaviour in renewing their contracts, in their relationship-specific investments or business relationships in general. According to our experience, it is common for buyers to compete even a long-lasting business relationship through tender. Although machine building is a technology-intensive area, we see that the relationship-specific investments do not play important role in this sphere. We think that the companies feel the network effects in their supply chain but still manage their dyadic business relationships much more actively.

Key words: business ethics, relationship-specific investment, tender, supply chain

1. INTRODUCTION

Globalization of markets, free access to information, increasing social and environmental problems have an impact on global ethics, and urge the integration of ethical issues into everyday business practice (Lindfelt & Törnroos, 2006). Based on a global survey, 74% of the population in 24 countries claimed that corporate social responsibility is an essential factor in buying a product or making a decision on a service. 84% of respondents believe that companies should do more for society (Ipsos MORI, 2013).

Business relationships are usually formed with the expectation of continuity, which is accomplished by repetitive transactions (Håkansson & Snehota, 1995). During years of cooperation commitment to trust develops. Long-term co-operation within the network requires adaptation, where, for example, relationship-specific investments make dependence more complex (Håkansson & Snehota, 1995). Ethical behaviour may increase the willingness and intent of the players to continue investing

and further improve the competitiveness of the network (Praxmarer-Carus, Sucky, Durst, 2013). In contrast, unethical treatment can weaken prospects for future performance (Hunt, Vitell, 2006).

Gundlach and Murphy (1993) emphasize the role of ethics in long-term business relationships, adding that the importance of ethics is independent on the ethical model of the parties involved. By doing so, their recommendations are related to the general principles of virtue. In fact, all the theories of ethics can be used in business studies. The ethical and deontological approach emphasizes the social approach while the teleological and utilitarian perspectives follow the economic (cost-benefit) aspect (Halinen & Jokela, 2014).

This paper is structured as follows: First, we summarize briefly the most important issues of business ethics and then present our qualitative research on business ethics at network level. We summarize some relevant Hungarian empirical findings as well while we collected our data in Hungary. We ask experts in the engineering industry and companies about the role of ethics and ethical behaviour in relation to the automatic renewal of contracts, relationship-specific investments or their business relationships.

2. LITERATURE REVIEW OF ETHICAL BEHAVIOUR

Ethics is a system or code that is based on moral obligations and rights; it shows how we should behave; it deals with the ability to distinguish it from being misled and with the commitment to do what is right (Hoffman et al., 2014). Business ethics is one of the types of applied ethics. Business ethics means the use of ethical values for business conduct. Business ethics is relevant to both the behaviour of individuals and the behaviour of organizations. It can be applied to every part of a business: from corporate strategy through how companies are managed by their employees and suppliers, up to sales techniques or accounting practices. Ethics goes beyond the legal requirements of companies, so it is about their own decision-making and value-driven behaviour (Hungarian Business Leaders Forum, 2016). In our paper we will continue to rely on this definition.

Actually business relationships are not automatically long-term, and the continuity of connection is often broken (Coltman et al., 2009; Pereira et al., 2011). Moreover, long-term business relationships are not always desirable or preferred (Grayson & Ambler, 1999; Villena et al., 2011). Relationships may arise, for example, as a result of a tendering process.

Ethical behaviour is particularly questionable in asymmetric business relationships where resource ownership and use are unequal (Mouzas & Ford 2007). According to Mouzas and Ford (2007), interdependence does not necessarily mean the same access to resources and it may also happen that the actors themselves choose this situation. This means that asymmetry within the network is not necessarily a disadvantage. For example, Valtra, a Finnish tractor factory, has established a well-functioning network of 200 suppliers with a dominant, central role (Halinen - Jokela 2014). Ethical behaviour does not exclude the formulation and implementation of clear economic, technical requirements towards suppliers.

A Hungarian survey from 1996, which conducted a questionnaire survey with 1300 executives of 325 companies (Chikán 1997), has a fairly mixed picture of ethical behaviour. According to the authors, the institutional management of business ethics was in early stage in the mid-nineties, for example, with only about 10% of companies having codex. The companies that dominantly export to developed countries have demonstrated more ethical behaviour. At the same time, they found that the ethical behaviour of Western European companies operating in Hungary were not outstanding in those years from the aspect of ethics. Later, Szegedi (2001) finds that the responsibility of Hungarian companies is basically towards buyers and owners. She adds that the ethical sensitivity is expected to improve.

In fact, Szegedi's prognosis is supported by Hajnalka Csáfor (2010), who examines the companies of the Northern Hungarian region, concludes that the most important motive for the large companies under consideration is to "comply with the core value system of a company" to continue their CSR activities. This is followed by "acting as an ethical company". According to the study, it is almost equally important for companies - "contributing to sustainable development" and "fostering the company's reputation" and "expanding the customer base and acquiring new markets". So Csáfor believes that short-term, tangible gains are more important for SMEs.

During the investigation of the relevant literature, we found the cultural specialty that in the case of business ethics and fair behaviour issues in Hungary, the authors often deal with unethical business behaviour and corruption (e.g. Fazekas et al., 2013; Czibik et al., 2011).

With regard to the relationship between trust, interdependence and risk, we face the so-called relationship-specific investments that involve physical and human resources investments that are designed to solve a specific business problem and whose withdrawal and relocation represents significant costs (Erramilli and Rao, 1993; Heide, 1994). Relationship-specific investments influence the timely change and development of the relevant business relationship, as well as through the ARA model the embeddedness of the relationship (Gelei - Dobos - Kovács, 2010). (The ARA refers to the three linking relationships of the business relationship, more concretely the relationship among actors, resources and activities. (Håkansson, Snehota 1995))

A relationship-specific investment is not easy to revoke because it can cause cost-intensive security problems. For example if a company is constantly worried about its relationship-specific investments, this may cause not to trust their business partner. This means that these difficult-to-migrate, relationship-specific investments can make the company doubtful due to the additional difficulties encountered. From this point of view, the company's doubts and worries can logically lead to a decline in trust level.

The confidence-building effect of the reciprocal relationship-specific investment in the supply chain is clear. Although earlier researches have not shown any direct link to this relationship, the empirical research of Suh and Kwon (2006) has shown that a partner-specific investment affects trust. Anderson and Weitz (1992) claim that asset-specificity reduces dissatisfaction with the relationship. This commitment also has a positive impact on both sides (Anderson and Weitz, 1992; Heide and John 1990). Furthermore, the partner-specific investment has also positive relationship with the

expectations of the continuity of the relationship (Heide and John, 1990; Suh and Kwon, 2006).

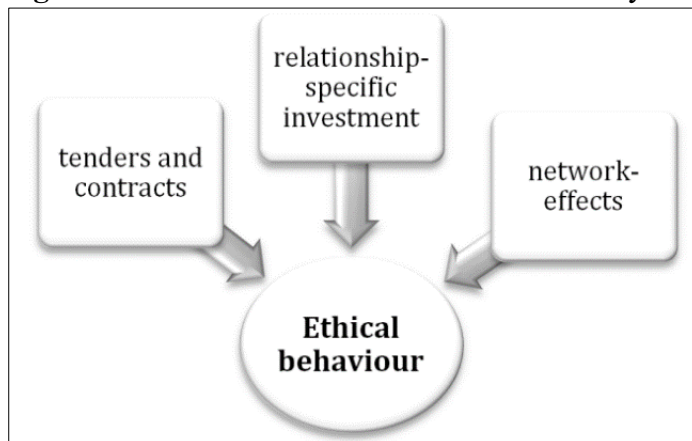
According to Williamson's (1985) transaction-cost theory, economic operators behave opportunistically in certain circumstances, so if one of the business partners has relationship-specific investment, then the possibility of opportunistic behaviour can cause them much damage. Relationship-specific investments limit the transactions of the affected parties, as without the use of any investments, other companies would only be able to produce products more costly (Laaksonen, Pajunen, Kulmala, 2008). This can lead to the concentration of the market in addition to the interchangeability of the partners.

Relationship-specific investments have a certain level of alignment that can increase the lack of mobility, change or substitutability (Johanson, Mattsson, 1987). Thus, common commitment increases mutual dependence and increases valuable resources of the relationship (Laaksonen, Pajunen, Kulmala, 2008). Successful cooperation contracts can provide many benefits through the implementation of high-level business confidence; such as increasing flexibility, widespread utilization of relationship-specific investments (Sako, 1992), decreasing transaction costs (Barney, Hansen, 1994; Dyer and Chu, 2003), improved co-operation and greater openness among partners (Tomkins, 2001). However, cooperation contracts cannot regulate all areas, so these relationships can end with the opportunistic behaviour of one party (Laaksonen, Pajunen, Kulmala, 2008)

Piricz (2013) empirically investigated the relationship between trust and relationship-specific investments regardless of sector. According to her results, there is a moderate positive relationship between confidence and the asset specificity of the partner. However, she adds that a higher level of trust may be necessary for asset specificity (Piricz 2014). Actually, in practice, this positive relationship works in reverse, which means that asset-specific investments can be achieved by a high trust level.

As a summary of the above literature review we created Figure 1. This serves as the base of our empirical research. In our qualitative research we analyse the companies in Hungary operating in the metal and machine industries through in-depth interviews in terms of business ethics and, more specifically, fair behaviour.

Figure 1. The theoretical structure of this survey



Source: Own study

3. THE QUALITATIVE RESEARCH AND ITS RESULTS

The methodology of this research - which involves analysing companies operating in Hungary, in metal and machinery supply chains through in-depth interviews - has been developed at the University of Turku (Finland). The in-depth interviews are semi-structured, so based on relatively detailed sketch points and during the conversation we were not obliged to touch each point (Malhotra, 2007). Our goal is to exploit the flexibility of this methodology (Yeung 1995) and to give the respondents freedom to explore this sensitive subject.

The novelty of our research is the networking approach of the subject and network-level research. Globalization and the spread and development of supply chains are a clear demand and challenge for researchers to raise their B2B research into network level (Veres 2008; Veres 2009). The qualitative methodology provides an excellent opportunity to introduce roles in the network (Yeung 1995) and to present fair and unfair situations and solutions. Thus, it is possible to get acquainted with the social, cultural and economic embeddedness of businesses. The in-depth interview shows a situation and status at a given moment that is the result of many historical, economic, social and technological events and processes (Ragin 2008).

We have seen several reasons why we focus on companies operating in the metal and / or mechanical engineering sectors. Firstly, these firms operate in relatively sophisticated networks because of its sectorial feature. Secondly, these sectors are very significant for the Hungarian GDP. In Hungary, the mechanical engineering industry and, in particular, the role of automotive production has become particularly significant in recent decades. Gergely Gabler (2014), chief analyst at Erste Bank, for example, noted a significant 3.3% GDP growth in the second quarter of 2014 (compared to the previous year), saying that "industrial production pulled growth and within the automobile industry, presumably manufacturing" (<http://www.autoszektor.hu>). Gergely Ürmösy - also an analyst at Erste Bank - adds that in 2010 vehicle industry represents 20 percent of the whole manufacturing industry. But the same value is close to 30 percent in 2014 (Panulin 2015). Thus, a new investment of a multinational car factory in Hungary can result in a measurable change in the Hungarian GDP.

Recently, the relevant Hungarian investments are aimed at increasing mass production, pointing to quantitative approaches.

In our preliminary empirical studies in Finland, we found that the concept of ethics for managers was both too abstract and difficult to understand, and on the other hand, we often met the almost philosophical question of whether there was any ethical business at all. This issue has been raised even in one of the least corrupt countries in the world, Finland. Therefore, instead of ethics, we started to use the more concrete fair behaviour expression in data collection.

So far, ten in-depth interviews have been conducted in Hungary between 2015 and 2016. We have data from three expert discussions and seven in-depth interviews with company-leaders from different levels. The companies represented by the managers are indeed diverse in terms of both size and market orientation but the respondents are mainly small and medium-sized and multinational companies that are

either exporting or are essentially on the domestic market. In spite of this, our research is not representative; our conclusions must be treated with this restriction.

Ethics and contract. According to our experience, companies have quickly adapted to cooperation with international companies, which is particularly characteristic of the automotive industry (Bartlett - Seleny, 1998; Lorentzen, et al. 2003). The Hungarian metal and machine industry is a highly concentrated market where some big companies can play a dominant role. In terms of contracts, medium-sized businesses often feel:

- "We are working with very large companies where we do not have a lot of talk about contracts. Our market consists of 10-15 buyers. If we are pushed out of an area, we cannot go back there again."
- "After contracting, the customer often asks to start work sooner, or later, but the deadlines are fixed, this is very bad to our capacity planning." (If they started work earlier than the agreed date.)

So the role of writing is very important in this area, due to outsourced inventories, expensive technology, capacity planning and large value of orders.

The widespread practice of tendering is relatively new in the Hungarian business. Some of the respondents regard this as a natural condition while others are surprised that even an old business partner makes them compete in this way. We find that renewal of connections is often automatic in old, stable partners, while others tend to apply the tenders in contract renewal. But all this - unlike the Finnish respondents (Jokela et al., 2016) - does not mean the termination of the relationship among Hungarian companies. Hungarian leaders do not even cease contacting if the partner pays badly or hastily, rather they switch to e.g. pre-transfer. Managers believe that the business relationship would cease immediately if they brought some unresolved causes to court.

We have found that price is also the most important factor in negotiations and contracts, although some suppliers say that technical content should be at least as important in this sector.

- "What would characterize the competition? So it's not a competition! Only on a price-based basis we cannot compete. It's not a fair race category. We pay our employees well, so our costs are different. "

Not all managers are so pessimistic about this issue, but more respondents explained similar cases.

- „Once we thought that the price (which is recommended by the competition – author's comment) could not be maintained and we have also indicated this to the buyer. Our opinion was correct as the company that commissioned under the realistic price fell into bankruptcy within 5 years but the buyer did not care about it."

It is also not uncommon that the buyer demands a price-cut by the progress of the delivery, saying that during the production of large quantities the producer got experience to reduce production costs. But it also happened that a supplier was successful in refusing the post-contract price reduction proposal.

Based on our data it seems that there is a different attitude in the field of renewable energy production, which is extremely innovative. The business partners – regardless of size - are more closely associated with the rapidly evolving industry. Besides this condition a company can get rid of the price-centric business if it is able to provide complex, high-quality services to its stable customer base that knows they can count on their supplier at any time, such as breakdown. These customers are willing to pay higher prices for high availability and for more services.

In addition to the price, payment condition is the most sensitive issue. Hungarian companies seem to be reluctant to borrow, as they often cannot offer adequate security to the bank. Therefore, they use their income not only for trying to finance their operations but they are trying to develop and expand from this fund. In such a situation, late payment is very sensitive to the supplier. According to one of them, if the buyer pays six months after delivery, it is the same as if he had not paid at all.

The history of a particular business relationship serves as a good preference but it is no guarantee of winning the next tender. Renewal of contacts is, therefore, often not automatic and the tender always has to restart.

- "The renewal of the contract depends on the amount, but is largely based on competitive bidding. This becomes more and more common and this is healthy, even if a firm has had a prior contact with the buyer. This is strange for the Hungarians. The world does so, but we have not done it."
- The expert also adds that "the tendering process is not always objective, I know many examples for this; we still have to learn this."

Strategic procurement is based on trust, that is, if there is no long-term, proven business relationship behind it, other supplier cannot enter. On the other hand, especially in the automotive industry, multinational companies do not only live up to expectations, and set specific standards in the upstream supply chain (Chang et al., 2012) but strive for extremely stable and long-term co-operation. Therefore, the change of supplier is very risky:

- "We change supplier in a critical case only. We cannot stop the car assembling factory for 1 day either."

According to the above quote of a TIER-1 supplier, their business buyers operate with a maximum of 1 day stock. In the automotive industry, producers generally do not like the SME suppliers because it means too much risk. A multinational manufacturer can move capital to solve problems more easily and at different level than a SME. Brányi (2015) also points out that a company with a dominant role in the supply chain can directly influence the chain's competitiveness.

Ethics and relationship-specific investments. We have found that special investment in the metal and machine supply chains in Hungary is not widespread. This

construct is even less typical when the buyer provides a guarantee in connection with a specific investment. We can identify this practice only in very innovative fields, such as the renewable energy industry.

The following opinion gives a good summary of this topic:

- "We had to buy more than one machine what we did not have before. In the Hungarian corporate culture the customer has to deliver nothing else but the order."

We have the view that in the Hungarian market the customer does not care if a relationship-specific investment will be repaid and the customer does not allow to suppliers to calculate this in price. Those companies, which sell unique products, complex business solutions, also do not think of asset specificity but say that "a profitable business requires 1-2 complex, green or brownfield investments per year, or a complete plant; because it includes requirements assessment, planning, manufacturing, installation, and on-site support."

One of our experts tells a possible explanation of the situation:

- "It is important to separate the pioneers and the followers. In Hungary, we cannot really talk about the first category just about followers. Costs are most commonly covered by EU or national tenders, so they jointly apply."

Based on our data, the joint application is not common, but it seems that the Hungarian companies generally appear to be the so-called followers group.

- "The buyer has never contributed to our development if they were to contribute, he would like to have a stake in the company."

This is a bit of an extreme opinion, but merely points out that asset specificity is not characteristic even in technology and capital-intensive metal and machine supply chains.

In Hungary, trust is still low in international comparison (TÁRKI, 2009). This lower level of trust can be identified in this sector as well. The high degree of literacy and the more lengthy processes are the consequences. Such environment does not really have a positive impact on the relationship-specific investments or their spread.

Ethics and network-context. In this topic we want to know if the respondents feel any effects of their buyer's buyer or their supplier's supplier, or whether there is a dominant actor in their network. If so, what their roles are. We also discussed who sets the norms of industry or their network.

A few received typical opinions:

- "We are medium-sized (firm) not only from statistical aspects but also due to our place in the supply chain. We are stressed from above and below and also sideways."
- "According to our position in the food chain we already have to finance our activity but the firms below us are unable to finance themselves."

So we have the view that generally respondents are aware of various network affects. The network effect seems to be natural for involved companies. In addition, companies often see their place well in their supply chain.

- “Who is the dominant actor of supply chain? Just look at the direction of capital flow and you will immediately know it.”
- “There is no freedom for anyone. The network effect is the environment, the circumstance we live in.” (An expert.)
- “The impacts of multinationals are strong. They misuse their power including unwritten rules too.” (An expert.)
- ”I remember a case when a project was postponed one year because one subcontractor did not indicate serious problems and did not strive to cooperate.”

In most cases, respondents recognized the dominant player in the supply chain. This firm is usually located closest to the final customer or this is the largest producer, the assembler. For example the assembly factory makes sign his own contract with his suppliers and this situation gives him both responsibility and power. They seemingly instruct their suppliers and they are not really interested in their suppliers.

As we stated before our qualitative research has limitations due to number of respondents and nature of this methodology. However this investigation may serve a solid foundation for further quantitative research.

4. CONCLUSION

In our survey two types of connection were identified. Most of our respondents' turnover has been realized from long-term, committed business relationships. In these cases there is a high degree of trust, common value creation is important and parties behave practically always ethically.

But everywhere you can find the so-called "fallen" buyers who purchase a much smaller value or order a product/service package. Their numbers are larger than the old, well-functioning business relationships and the amount of their turnover is small compared to the previous group. They usually require and receive fewer services. In these cases, the unethical behaviour is much more common, for example, they disappear without payment after a few successful and cooperative transactions. Nevertheless, this segment is also important, while they also generate revenue. Managers however think that the unexpected unethical cases and losses cannot be avoided despite growing experience either. They state this is part of business risk.

Kolos et al. also found that networking is widespread for Hungarian companies (2006). But feeling of network effect is still somehow passive. Businesses perceive interdependence, sometimes experience the negative effects of inadequate cooperation or retention of information, but do not recognize that life in the network could be developed. Companies apparently do nothing to solve network-level issues or problems and to develop their supply chain. In their dyadic relationships,

companies are much more active, more aware and brave in implementing the solutions.

In order to spread relationship-specific investments, a wide range of ongoing, trust-based information flows are needed. According to our research this has not been realized in the Hungarian metal and mechanical engineering industry. We have seen that information exchange is rather limited, usually at the level of daily, operational communication. Hardly any strategic information is shared between the parties, and sometimes we have found that some subsidiaries do not even or rarely get strategic information from the mother company.

We have found that in the metal and machinery supply chains the size of the participants and their position in the chain, are the two most important factors affecting fair behaviour. Only very innovative areas – such as producers in alternative energy sector – are exceptions where business relationships are more balanced. Above all, the personal attitude of leaders plays a decisive role for business ethics.

In the future it might be worth researching how SMEs could avoid unethical situations and decrease their losses based on good samples in alternative energy sector. Generally SMEs may need more support and knowledge about networking, more concretely how they could improve and develop their relationships in their networks.

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