

Retail Therapy

The Ethical Considerations of Retail Buying



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The Ethical Considerations of Retail Buying

One area where little has been written is in the ethical aspects of the relationship between retail buyers or category managers and the suppliers that provide them with product. This relationship is particularly sensitive to ethical considerations and this paper looks at both the areas of sensitivity and some suggested strategies to help protect the interests of all stakeholders. But what do we mean by 'ethics' and 'ethical considerations'? The Oxford Dictionary defines ethics as "relating to morals, treating of moral questions, morally correct, honourable". Likewise morals are defined as "concerned with the distinction between right and wrong". Developing an ethical framework, therefore, involves putting in place principles that allow individuals and organisations to make decisions that take into consideration factors including whether decisions are right or wrong.

Why are Ethical Considerations important?

Public expectation has changed and will continue to change as a result of significant ethical lapses by large corporations and the significant increases in senior executive salaries. The public demands that those being paid large salaries demonstrate a level of ethical uprightness above and beyond that of the rest of society. This is not only true for business people but for prominent sports and media personalities as well. A failure to reform 'both head and members' of the retail sector, particularly in the merchandise function, will result in significant consumer backlash against not only companies but whole industries. In Australia, this is no better highlighted than in statements such as "the buying power of supermarkets enables them to beat farmers down in price so that they are selling whatever they produce for less than the price of production just to keep the supermarket business" (Rumble, 2007).

Due to these issues, business ethics should enter into every financial discussion (Gentry, 2007). Adopting the rhetoric of ethical reform and not the substance will lead to increasing consumer cynicism and ultimately an increased regulatory involvement. As Porter and Kramer (2006) state "any business that pursues its ends at the expense of the society in which it operates will find its success to be illusory and ultimately temporary".

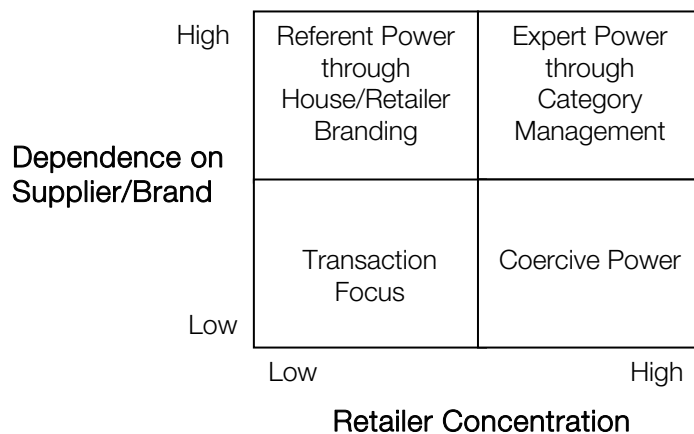
The 2005 - 2006 KPMG Forensic Integrity Survey showed that nearly 75 percent of respondents had observed misconduct in their companies in the previous 12 months, 50 percent said that, if discovered, there would be a significant loss of public trust. Those with codes of conduct in place saw less but when asked who they would report it to, 81 percent

said they would tell their line manager. In corporate cultures where achievement of results is the clear priority, that is akin to letting the lookout man know that you think a robbery is taking place. Chain Store Age conducted similar research which suggests that over 40 percent agree that corporate ethics are improving, 28.5 percent disagree and over 30 percent are neutral on the question. When the question was narrowed to corporate ethics within their own company the number agreeing leaps to almost 70 percent and less than 10 percent disagreeing (Clark, 2006). This highlights one of the major issues relating to changing ethical behaviour; it is always some else’s problem. *We* are ethical, *they* are unethical. The public are not confused – ethics are getting worse (Grande, 2007).

The difficulty that arises from both the Chain Store Age and KPMG surveys is that neither appears to include ‘leaning on suppliers’ amongst the unethical behaviour being questioned. It is seen as normal business practice. There is a widespread failure to define not only *what* is ethical or unethical but *why* it is deemed to be so. There needs to be the development of a framework that enables businesses and individuals to “weigh one social benefit against another, or against its financial costs” (Porter & Kramer, 2006).

The context of the Buyer/Supplier Relationship

The use of high levels of data and objective benchmarks has had a dramatic impact on the balance of power between suppliers and retailers and raises a crucial question for discussion –Can an effective relationship exist where there is a significant imbalance in power between the supplier and the retailer? This question applies equally to large suppliers dealing with small retailers and retail giants dealing with all but the largest and/or most indispensable suppliers. Dapiran and Hogarth-Scott (2003) suggest that there are two aspects that impact upon the power aspect of the buyer-supplier relationship; the degree of retailer concentration and the dependence retailers have on particular suppliers and brands. The diagram illustrates the relationship.



As the authors point out it is this combination of factors that helps to explain the difference in uptake of house brands/private labels in the UK (where there is relatively low retailer concentration) and Australia (where concentration is high). This is particularly evident in the grocery sector. The research also highlights that the use of power in the retailer/supplier relationship is not necessarily a conscious decision but is present nevertheless. It further suggests that where a sector has high retailer concentration, such as in the grocery, hardware or whitegoods sectors, supplier survival may be dependant upon making themselves indispensable to the retailer; low dependence on the brand is likely to result in a coercive strategy being adopted - an issue of great concern for antitrust lawyers in the U.S. and across the globe (Banks, 2003).

The issue of manufacturer control was examined by Lindblom and Olkkonen (2006) with reference to the use of Category Management within the FMCG sector. Their findings were that manufacturers clearly believe that while it is the retailers who are in charge of Category Management tactics, large manufacturers possess a relatively strong weight of control compared to smaller manufacturers in this regard. If the manufacturer can bring strong brands to the relationship, they can increase their control over the Category Management tactics that are used, i.e. the strong consumer brand loyalty helps offset the retailer power. Conversely, small manufacturers feel that payment of such costs as an advertising subsidy is more important than large manufacturers do – in a sense they feel that they have to ‘buy the right’ rather than ‘earn the right’. Large manufacturers will earn the right by use of expert or referent power, for example in-depth understanding of target customers, or through their command of large/loyal customer base.

Developing an ethical framework

Recent events that have thrust the discussion of ethics into the spotlight include the 2001 collapse of the 7th largest company in the US, Enron. Not long after, there were tremors through European industry with issues at the Parma group in Italy. In the last two years Australia has seen Coles Myer plead guilty to charges laid by the ACCC that resulted in a fine of almost \$5 million and Woolworths brought to account for breaches of the price fixing legislation in the mid 1990s resulting in fines of \$8.9 million as well as being found guilty of similar offences to Coles, incurring another \$12 million fine. While legislation has been put in place in the U.S. and both Coles and Woolworths have introduced measures to prevent a recurrence of these breaches, will these measures be enough to rebuild public and regulator confidence in large corporations?

Adopting an ethical position is more than just ensuring that you do not break the law. Public perceptions of 'right' and 'wrong' are continually evolving. Simply adhering to the legal requirements will only leave you in a position of vulnerability regarding public perception. Likewise adopting an ethical position is more than just adopting the terminology of an ethical position. We have seen this sort of thing happen repeatedly in the business community; 'Every Day Low Prices' and Balanced Scorecards are just two examples that come easily to mind. Adopting the terminology while ignoring the practice has two effects; it discourages those who are serious about change and it undermines any genuine attempt to introduce that change. What it does *not* do is provide any impetus for change.

For example, ethics are still not a high priority for companies when recruiting and developing managers. Of 22 management competencies, ethics and integrity are ranked 14, well below career development at 7th (Velthouse & Kandogan, 152). This duplicity of adopting the terminology without adopting the practice is usually the result of an internal conflict within the individual and/or the organisation. This conflict is brought about by the need to do the 'right' thing *and* the need to satisfy certain short term financial targets. It would be the exception to find a buyer or category manager who is prepared to sacrifice a substantial bonus to do the right thing (or to have their line manager allow them to jeopardise the line manager's bonus.)

Lindfelt (2006) argues that it is not reasonable to even expect an organisation to act consistently with a written code of ethics. In multinational businesses, ethical frameworks may vary from nation to nation. A universal code of ethics is, to a degree, going to impose one of those frameworks on the whole organisation. This may lead to a lack of resonance between local custom and mores and international company codes. Interpretation of the universal ethics code will be done by individuals. Ex-pat managers will interpret based on the originating culture, local managers on the basis of local culture. The application of the code will continually change so assessment of company ethics is more appropriately measured in terms of the learning process and the developing understanding of the underlying principles rather than strict adherence to the letter of the code. The ongoing question for international retailers is therefore not one of "is the organisation adhering to its ethical code?" but "is the organisation improving its adherence to its ethical code?"

The conflicts between words and deeds are further exacerbated by competing interests, some of which are:

- Shareholders: Increased ROI, share price and dividends
- Suppliers: Increased volume, profit and consistent cash flow

- Employees: Reward, recognition and a degree of job security
- Customers: Increased value (this is more than just price)
- Community: An improved quality of life

Juggling these, often competing, demands places a huge stress on buyers and it is not surprising that ethical lapses occur, especially where there are no appropriate support mechanisms in place. For example a buyer who is under pressure to achieve margin targets as a result of shareholder pressure for greater returns on their investment, may be disinclined to check too thoroughly the working conditions of the actual producers of the product or the impact that the production of those products may be having on the local community. Likewise a buyer may not be prompted to ask a supplier if the low prices they are offering are financially responsible from the supplier's perspective if it means that the buyer may affect their chance of achieving their financial targets.

Even in companies that present a strong moral stance, such as Costco, there will be boundaries to where that moral stance is applied. According to the Costco CFO, Richard Galanti, "Costco is not going to make money at the expense of what's right" (Cascio, 2006), yet shareholders could argue, and Wall Street analysts *do* argue, that Costco is conducting their business at the expense of what is right for the shareholders. Likewise Costco does not hesitate to lean on its suppliers to ensure that it is getting as good a deal as any other retailer, even if those other retailers are acting unethically in the way they relate to the supplier. Is this behaviour towards suppliers, in itself, unethical?

What needs to be put in place?

There has been a push towards Socially Responsible Buying but it is important to note that this is not 'ethical buying', it simply means that buyers will *try* not to source product made by child labour or sweat shops in developing nations. The main deterrent against using this sort of labour is the bad publicity that could be generated if the public becomes aware of unethical manufacturing processes. Even socially responsible buying creates a tension for buyers because at the end of the day it increases cost prices. As a result it is in direct conflict with the almost universal buyer KPI of Gross Margin. Research conducted in the British apparel industry by Pretorius and Love (2006) highlights this dilemma as buyers try to balance the drive for margin and the risk of getting caught out. Fear is not a good long term motivator though and there is a real danger that Socially Responsible Buying practices will just lead to a more complex supplier chain so that buyers can distance themselves from the exploitation. Ethical buying involves a

much broader range of issues including intentionally factoring into the discussions with suppliers the power relationship that is present.

Many major corporations have adopted a Corporate Social Responsibility (CSR) statement, which has become part of their annual reporting process. Porter and Kramer (2006) from the Harvard Business Review, see this development as a demonstration of the extent to which “external stakeholders are seeking to hold companies accountable for social issues and [to] highlight the potentially large financial risks for any firm whose conduct is deemed unacceptable”. They also see social responsibility as a means of achieving competitive advantage, with customers now willing to factor social issues into their buying decisions. However, most of these CSR statements “rarely offer a coherent framework for CSR activities, let alone a strategic one. Instead they aggregate anecdotes about uncoordinated initiatives to demonstrate a company’s social sensitivity”. In other words they are a relatively undisguised public relations exercise. Others have implemented a Corporate Code of Conduct, signed by all employees. An abundance of research has demonstrated that while these are positive measures, by themselves they are insufficient in changing the ethical climate.

What also needs to be present for the ethical climate to be improved is peer based support for those clearly communicated written standards (Park & Stoel, 2005) and clear role modelling by senior management (Valentine & Johnson, 2005). Failure to support written statements in this way will result in ‘evasion behaviour’ where employee energy will be directed towards devising ways to circumvent the rules. As Archie Carroll, former professor at the University of Georgia, highlights, competitive pressure is often at the root of ethical lapses. If a realistic target is only half of what a buyer has to achieve in terms of sales or profit, the other half represents an incentive to “cheat”. He sees codes of conduct as being similar to “training wheels on bicycles” (Clark, 2006). In a competitive market, “individuals are encouraged to be achievement oriented and are judged according to tangible output. The greater the pressure, the more likely ... that the range between acceptable and unacceptable shrinks to reflect the organisational culture” (Smith-Hillman, 2007).

The public are ruthless in how they assess corporate motivation in this area. Companies, retail or otherwise, need to ensure that their CSR statements ‘fit’ with their business. If consumers see the actions of organisations as being incongruent with their core activities (e.g. a hardware retailer engaging with a breast cancer campaign), or they see the response of the organisation as being reactive rather than proactive, then CSR statements are more

likely to have a *negative* impact on consumer attitudes towards that retailer. An exception regarding reactivity is where companies respond to significant disasters such as Hurricane Katrina in the US or Cyclone Larry in Queensland. In these situations suppliers are able to build their reputation with the public by providing a socially acceptable response to those in need (Becker-Olsen, Cudmore & Hill, 2006).

Building a framework

An ethical framework is built by making the right choices in the little things. It is in the day to day choices that a category manager or buyer establishes their ethical framework. It is crucial that employees observe management practicing these ethical values (Mujtaba & Sims, 2006). In addition, appropriate ethical decisions should be rewarded (Mitchell, Schaeffer & Nelson, 2005) as ethical standards do not come from the indoctrination of abstract principles or rules. There is a spectrum of ethical positions that can be adopted ranging from “the end justifies the means” (a teleological position) to “doing what is right” (a deontological position) and existentialism which suggests that there is no need to have *any* ethical position. Other alternatives are:

- **Egoism** – Maximum benefit to the individual (preferred by most dictators)
- **Utilitarianism** – Maximum benefit to the most people (most governments)
- **Relativism** – Behaviour is acceptable to the group (most companies)
- **Justice Ethics** – Fairness in process, distribution & interaction (most lobbyists)
- **Virtue Ethics** – Absolute standards based on a predetermined rule or rules eg First, do no harm; Do to others as you would have them do to you; 10 commandments (most fanatics).

Most retailers tend to adopt a position in the middle and tend to gravitate toward Relativism. However, it is not enough to simply adopt a position. If organisations want to change their ethical climate they must be intentional about how they address this issue. There must be a conscious decision to include a person’s moral/ethical makeup as well as their psychological background and skills set. Employing people, particularly for senior positions, simply because they have a successful track record (despite the cost of ‘winning’) can do untold damage to the long term health of the business. Change must start with senior management because unless there are large numbers of new people introduced into the organisation at lower levels with strong ethical frameworks, then new employees will simply adjust their moral framework to the existing company position and the organisation will be no better off.

People have an evolving situational approach to ethical dilemmas, they will decide what they think is right in this instance (Buchholz & Rosenthal, 2005). Individuals will also become desensitised over time if they continue to compromise their personal standards (Fassin, 2005). It is for this reason that role modelling and positive peer support are important as they will help buyers determine the most appropriate behaviour. This inconsistency can be confusing and contradictory but it is also perfectly normal (Wempe, 2005). Senior management must also be trained in the details of the ethical framework preferred by organisation so that they can coach others in what is appropriate behaviour. A clear ethical position needs to be supported and developed by the consistent presentation of both formal and informal training as well as rewards for making difficult ethical decisions.

Conclusion

For the long term health of Buyer/Supplier relationships, ethical considerations must become a conscious part of the decision making process. Failure to do so will see major questions being asked by both the public and regulators about the behaviour of 'partners' who wield significant market power. We must see the implementation of real ethical practice not just the adoption of an ethical decision-making vocabulary. It is not enough to simply address issues of corporate corruption after the fact; the die is cast long before that level of behaviour is manifested. The ethical use of market power in the negotiation process is just one example of where buyer/supplier relationships would benefit from a greater emphasis on ethics. Buyers must ask themselves - Are they getting co-operation or capitulation from their suppliers?

About the author

Andrew came to the ACRS after 20 years working for Coles Myer Ltd. In that time he gained experience in a wide-array of functions including buying. With a strong background in theology and interest in ethical business practices 'ethical buying' as a concept has always been of interest. Andrew's responsibilities at the ACRS include coordinating, designing and facilitating the Retail Buying and Finance Programs for both the in-company and public streams. With exposure to a large selection of retail organisations and their employees and his insight into retail buying practices he is well placed to discuss retail buying and ethical considerations.



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The ACRS builds skills, knowledge and understanding at all levels of management from first line appointees to CEOs; because of its unique retail focus the Centre offers advantages over other general management training providers.

Enquiries

Please contact us if you have any enquiries about Retail Therapy or the centre itself. Also if you would like further information about this paper or contributing please feel free to contact **Jeff Rogut**.

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