

## CHAPTER 2

### LITERATURE REVIEW

#### 2.1 Introduction

The Malaysian economy is at an important crossroads. Bold and imaginative measures are required to enable Malaysia to have smooth transition to a fully-developed nation with a knowledge-based and information driven economy that is resilient, robust and competitive.

In Malaysia, the issue of ethics gained momentum following the mismanagement of financial institutions. In the mid-80's, several financial institutions particularly finance companies and deposit taking Cooperatives were under-receivership. Several key directors of these institutions have been prosecuted for criminal breach of trust. By 1987, a code of ethics for bankers was advocated and on January 1, 1989, Bank Negara Malaysia formalized the code of ethics for bankers.

One of the issues gaining increasing prominence in business management is the question of ethics. Over the last three decades, only a few theoretical and empirical studies have been conducted in this area. Most of the research was carried out in the developed countries particularly in the west, while only few surveys have been done in the east, such as in Singapore, Hong Kong and Australia (Kam Hon Lee 1981; Mehta and Kau 1984; McDonald and Zepp 1987).

There were so many cases of mismanagement of funds, fraud and criminal breach of trust. This study is particularly important as it provides us with a better understanding of the ethical business practices in Malaysia and also the ethical climates in the Malaysia's financial system. This may provide important implication for the existing business executives as regards to the need to adopt appropriate measures to maintain ethical standards in business.

The finding of this study may also provide greater insights into the key issues to be addressed in an effort to develop a morally conscious business organization culture.

Qualitative and quantitative publication have attempted to identify various organization ethical issues. Examples includes social responsibility (Walton, 1967; Adizes and Weston, 1973; Shaklin, 1976; Zeusek, 1979; Stevens, 1984), conflict of interest (Snoeyebos et. al, 1983), payoff (Pastin and Hooker, 1980), financial results liability (Bevenson, 1972), Whistle-blowing (Nader et. al, 1978; Dizier and Miceli, 1985), organisation politics (Cavanagh et. al, 1978), ambivalence and reward systems (Jansen and Von Glinow, 1978).

Within the banking industry, additional issues have been raised: laundering drug money (Frank, 1986), insider trading (Magnet, 1986); conspiracy filing false documents and embezzlement (Clifford, 1986), improper loan and withdrawals (Crock and Jaben, 1985) and the political morality to lending to non-friendly nations (Siager, 1987).

However, the ethical perspective of executives particularly the executives in the financial institutions have not been done here before.

## **2.2 Definition of business ethics**

The present economic situation demands for a prudent and highly ethical and efficient management of financial institutions. Only transparent and highly ethical companies could withstand the down turn of the economy at the present moment. Therefore, financial institutions should make business as an ethical activity. In search for excellence, whatever else it may be, begins with ethics.

Yet business ethics is still a matter of controversy. Public opinion is clearly antagonistic to business. However, many writers and ethical thinkers have concluded based on their experience the followings:

- i. The more successful the company, the more attention it pays to its code of ethics. The higher one climbs in the corporate hierarchy, more emphasis is given to ethics.
- ii. Conversely, the cynical view that ethics is irrelevant to business and not concerned with the bottom line seems to prevail in businesses on the brink and among people who are locked into middle management jobs that no longer satisfy them.

The most successful people and companies are those that take ethics seriously. This is not surprising, since ethical attitudes largely determine how one treats employees, suppliers, stockholders, and consumers as well as how one treats competitors and other members of the community.

Business executives do not uniformly agree on how to define business ethics. De George (1987) states that the field of business ethics is defined by the interaction of ethics and business. From its object is the study of the morality and immorality as well as the possible justification of economic system.

Lewis (1985) attempted to reach a definition of business ethics by consulting literature, addressing the topic and collecting primary data from executives in order to make a selection. This resulted in the following definition: business ethics is rules, codes or principle, which provide guidelines for morally, right behavior and truthfulness in specific situation.

Despite the accuracy and usefulness of this definition, the term 'ethics' is used in a variety of ways by different people in different circumstances. Sometimes, ethics is synonymous with morality, for example an action that is morally right is called an ethical one. Codes of moral conduct adopted by professions are frequently called ethical codes.

Although, philosophically, business ethics is a branch of general ethics, some people interpret the phrase business ethics to mean business morality. They interpret this either descriptively that is, as the morality followed in the business or normatively, as the morality that ought to be followed.

Those engaged in ethics as a branch of philosophy perform analysis and synthesis. There are three related phases of ethical study, which are commonly known as descriptive ethics, normative ethics and metaethics.

Descriptive ethics is closely related to anthropology, sociology and psychology, and leans heavily on them. It insists in studying and describing the morality of people, culture or society. It also compares and contrasts different moral systems, codes, practices, belief, principles and values. Descriptive ethics provides basic materials that normative ethic must account for, and it provides a touchstone of considered morality of people or a society with which the normative theory must more or less coalesce. Although normative ethics is critical, it starts from an assumption that most of the moral rules, norms and values that a society holds, and are detailed in descriptive ethics are justifiable.

Normative ethics builds on the whole that descriptive ethics provides and attempts to supply and justify a coherent moral system based on it. Typically, it seeks to uncover, develop, and justify the basic moral principle or principles, or the basic moral values, of a moral system found in a society.

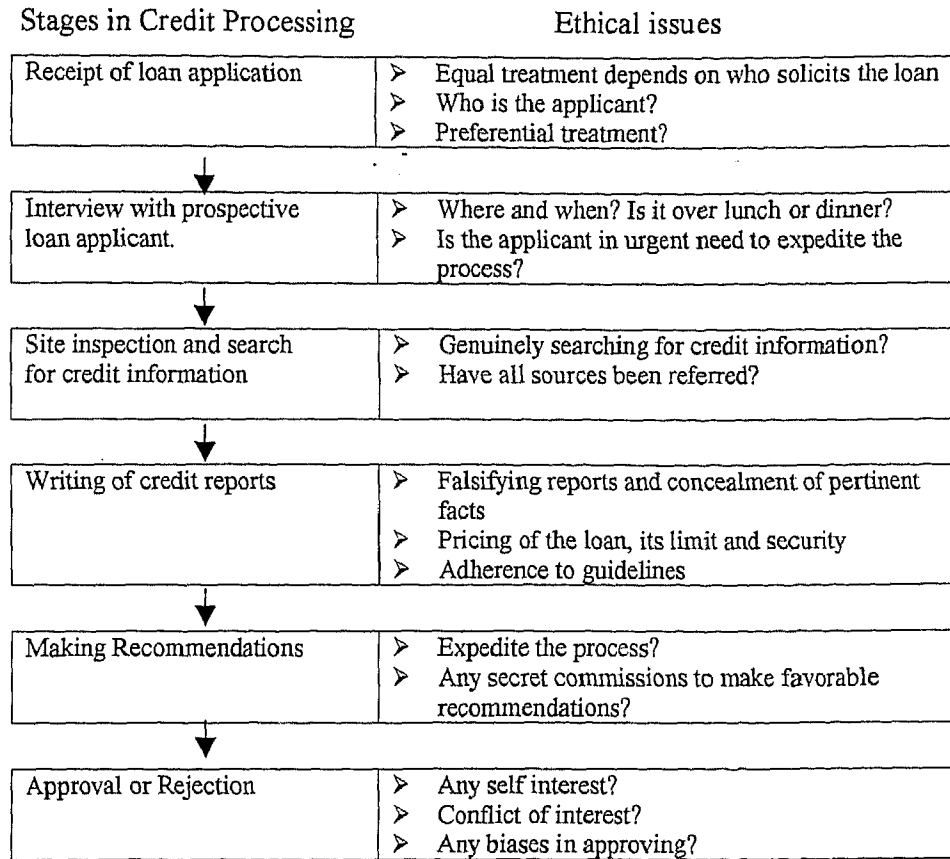
The task of normative ethics is threefold. First, it attempts to form into a related whole the various norms, rules, and values of a society's morality. It tries to render these as consistent and coherent as possible, with perhaps some hierarchical arrangement of norms. Second, it attempts to find the basic principles from which the particular norms can be derived. Third, it attempts, in a variety of ways, to justify the basic principle of morality. Because normative ethics is a systematic attempt to explain and justify the morality of a society, such attempts are called "ethical theories".

Metaethics, the third phase of general ethics, is closely related to normative ethics. Metaethics is the study of normative ethics, and, to some extent, both normative and descriptive ethics involve some metaethical activity. It is sometimes called analytical ethics because it is concerned with analysis. Metaethics deals with the meaning of moral terms and with the logic of moral reasoning. It asks, for instance, what the term *good* and *bad* mean in the moral sense and what *moral responsibility*, *moral obligation*, and other similar phrases mean.

Various ethical issues can be analyzed in the financial institutions. To make the study more readable and easily interpreted, various ethical issues that may be encountered by an executive in financial institutions are shown in the Figure 1 . It can be clearly seen in the stages of credit evaluation.

Figure 1

Ethical Issues during credit evaluation



### 2.3 Previous Researches

Only a handful of studies have been conducted on the subject of ethics in Malaysia. Md Zabid Abd Rashid (1989) conducted a survey on the perception of unethical practices among bank managers. Questionnaires developed by McDonald and Zepp (1987), Kam Hon Lee (1981) and Ferrel and Krugman (1981) were sent out to various commercial banks in Malaysia..

A total of 138 questionnaires were sent out to managers working in 20 commercial banks. The response rate was 72.5%. In the questionnaires, the managers were asked to rate thirteen unethical practices on a six point Likert scale. The reliability test for the thirteen items was conducted and the Cronbach alpha suggests an acceptable level of reliability.

The result shows that bank managers perceived bribery as most unethical. Using company time and falsifying reports were also rated as highly unethical. On the other hand, gaining competitor information was rated least unethical. The other items such as malpractice in sales, obtaining trade secrets, deceptive advertising, misleading instruction, taking credit for another's work, taking longer than necessary to do a job and padding out one's expense account were rated as quite unethical.

The findings suggest that the bank managers considered the practices less unethical when the action had greater impact on themselves (personal) than on the organization (bank). The managers also perceived certain practices to be more unethical than others did.

In comparing the perception between the small size banks and larger ones, the results show that managers in small and large banks perceived bribery as most unethical. However, managers in small banks perceived bribery as more unethical than managers in larger banks.

In concluding his finding, the authors suggest that locally owned banks need to review their unethical practices. Overall, there is a greater need to adhere to the code of ethics developed by Bank Negara.

In the west, many studies have been conducted on the ethical issues in the banking industry. Brian Harvey (1995) conducted a survey project as a case study on a Co-operative Bank. The research was aimed to present a significant British case on the application of an ethical approach to banking practice. A quantitative research project was undertaken with 30,000 consumers who revealed major support for the practical issues of greatest concern. The outcome was an ethical banking policy which communicated “what we are and what we stand for” and strict guidelines on who we will or will not do business with”.

The research confirmed that there was a growing public awareness of the wider social and environmental implication of consumer behavior. Taking a different perspective in ascertaining ethical value in banking, the study approached consumer view on how their bank should behave or play their role. And the results show that there was an increasing awareness among consumers on ethical banking.

William J. Mitchell, Phillip V. Lewis and NL Reinsch Jr (1982) conducted an exploratory study of ethical behaviors and perceptions in small, local banks. The study addresses five research questions: What specific behavior is described in the literature as ethical or unethical? What percentage of business people is believed to be guilty of unethical behaviors? What specific unethical behavior bank employees have observed? How serious are the behaviors? Are experiences and attitude affected by demographics?

The study suggests that there are 17 categories of behaviors and in what they are heavily skewed toward internal behavior. The result shows that younger employees have a higher level of ethical consciousness than older employees do.



The longer one works for a company, the more one may look at job security as a priority. This can lead to rationalizing or overlooking apparently unethical behaviors. More emphasis is needed on internal behaviors with particular attention on the impact that external behaviors have on ethical behavior.

The respondents were asked to estimate the percentage of business people who commit unethical acts. Factorial analysis of variance indicated that responses to this question were significantly related to respondents' age. A younger person perceived immoral acts as more common than did an older person. The results show similar findings of studies conducted by Brian Harvey (1995).

The literatures reviewed shows that no studies were conducted on ethical perception of executives in financial institution in Malaysia. The study conducted by Zahid (1992) was on bank Managers in the financial institution. This study may also be a comparison with the executive level and manager level in the financial institutions.

Although similar studies were conducted in the west, but the set-up of the financial system and the culture of own country may not lead us to use the similar results. Therefore, its more important to find out how executives in the financial institutions in our country behave and whether they have similar perspectives of the west. A comparison may also be done in the ethical perceptions by different cultural perspective.