

United Nations Global Compact Case Study

Massmart Limited A moral community

Willem Punt
Business Ethics Manager
Ethics Institute of South Africa

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Special thanks

- To Mr Mark Lamberti, CEO and Deputy Chairperson of Massmart for leading a company whose efforts is so satisfying to report on; and
- To Mr Brian Leroni, Director of Corporate Affairs at Massmart for supplying valuable source material in researching this article.

1. Background

1.1 Massmart profile

Massmart is a managed portfolio of 11 wholesale and retail chains, each focused on high-volume, low-margin, and low-cost distribution of branded consumer goods for cash. The group, which operates in 10 countries in Southern Africa, is the third largest distributor of consumer goods in Africa, the leading retailer of general merchandise, liquor and home improvement equipment and supplies, and the leading wholesaler of basic foods.

Massmart generated a trading profit in excess of ZAR 1 billion for the year ended June 2005. The group achieved sales of ZAR 26.6 billion and headline earnings of ZAR 679 million for the same period.

Massmart biographical data

Sector:	Private
Organisation type:	Publicly listed holding company on the Johannesburg Securities Exchange
Industry:	Retail
Population:	Approximately 15 500 employees in eleven divisions
Leadership:	Mr Mark Lamberti (CEO and Deputy Chairperson)
Governance:	Compliant with the Second King Committee Report on Corporate Governance (<i>King II</i>) best practice guidelines. Non-executive Chairperson governs a board predominantly populated with independent non-executive directors.
Scope:	Serves an extensive consumer base in a wide ranging series of retail business in ten African countries, with South Africa being the largest.
Turnover:	ZAR 26.6 billion (approximately \$4 billion)
Last audited results	
Profit:	ZAR 679 million headline earnings (approximately \$110 million)

Box 1: Massmart Biographical Data

1.2 Ethics Institute of South Africa and Massmart

Massmart is a founding subscription member of The Ethics Institute of South Africa (EthicSA).

EthicSA was responsible for the training of ethics officers (13 since 2004), the evaluation of the Massmart Code of Ethics (2004), providing advisory services on ethics management, and conducting an independent verification – the *Massmart Ethics Indicator* (2005) – of its ethics management programme, the Massmart culture and ethical risk indicators in the group.

Other service providers, working closely with EthicSA, were responsible for conducting further training and awareness initiatives throughout the group.

The standards governing our engagement with Massmart are in part derived from the King II Report, the United Nations Global Compact Principles and the South African Constitution.

It is especially in terms of the 10th Principle of the United Nations Global Compact – combating corruption – that EthicSA takes a holistic view to encouraging organizational adherence. We acknowledge that strengthening the forensic and investigative capacities of an organization is essential in order to combat corruption. However, to truly enable effective forensic and investigative work, it is important to enhance the capacity to detect such crimes within the organization as well.

This goal is at the heart of a corruption prevention programme and should be kept in mind when considering our evaluation of Massmart in this article.

What is the King II Report?

It has been likened to the Cadbury Report (1992) in the United Kingdom and the Winter Report (2002) in Western Europe, for attempting to provide a set of self-regulating guidelines commonly understood to encourage self governance as a counter argument limiting government regulatory influence in the private sector.

In response to a heightened awareness of the importance of responsible business conduct and the influence leadership can have in shaping good corporate behaviour, the King II Report was published in South Africa in March 2002. It originated from an earlier report, a more basic document, the First King Committee Report on Corporate Governance, published in 1994. Its convener, retired High Court judge Mervyn King, brought various experts in the field of corporate governance together to craft a series of best-practice guidelines, which, if followed with real leadership commitment, may result in lowered ethical and reputational risk for organizations, including more responsible stakeholder engagement, within and outside of organizations.

While not intended to be of relevance to any sector exclusively, it is often interpreted to apply to large private-sector concerns and not to small and medium-sized enterprises (SMSEs), civil society or the public sector. It is our experience that the South African public sector has been taking King II more seriously in recent times, but the challenge of interpreting King II in addressing the governance requirements of SMSEs and civil society organizations remains unresolved.

King II differs from King I in that the more generalized guidelines of the first report was significantly expanded, including what was first labeled “Non-financial Matters”, but later more appropriately titled Sustainability.

It is within the sustainability section (Section 4) of King II that the best-practice guidelines for ethics management governing our engagement with Massmart Limited are contained.

Box 2: The King II Report

1.3 The United Nations Global Compact and Massmart

At the time of writing, Massmart is not a signatory to the Global Compact, yet, as will be discussed it takes seriously the principles of the Global Compact in exercising its corporate citizenship.

Massmart, as a non-signatory, managed to comply with the Global Compact principles because it institutionalized similar values to those that support adherence to Global Compact, through its ethics management programme, into its business strategy and daily operations.

These values - such as honesty, respect and fairness, underpin both the Global Compact principles and a Massmart Ethics Management Programme designed to ensure responsible business conduct.

1.4 Method of analysis

An ongoing relationship with Massmart enabled EthicSA to develop good knowledge of Massmart, both through anecdotal evidence collected during training and advisory engagement, special research for this article, and through the *Massmart Ethics Indicator*.

1.4.1 The *Massmart Ethics Indicator*

While internal monitoring and reporting on ethics are beneficial, Massmart, following the recommendations of King II, undertook an independent verification of its ethics management process. This involves voluntarily opening the organisation to scrutiny by external organizations.

Such scrutiny included an Ethics Perceptions Survey that was conducted by another external consultant and a comprehensive ethics review conducted by EthicSA – the *Massmart Ethics Indicator*.

EthicSA had unfettered access to engage employees of all employment hierarchies, all of whom were free to provide feedback anonymously, depending on their preference.

The *Massmart Ethics Indicator* provided a scientifically sound benchmark against which to measure the performance of further interventions over time.

1.4.1.1 Statistical Integrity

The instrument used for the *Massmart Ethics Indicator* yielded excellent results from a statistical point of view:

- a. Reliability
 - i. Reliability refers to the extent to which a research instrument produces consistent results with repeated measurements.
 - ii. The international benchmark is 70.0%.
 - iii. The *Massmart Ethics Indicator* reliability score is 94.84%.
- b. Validity
 - i. Validity refers to the extent to which a research instrument measures what it intends to measure.
 - ii. The international benchmark is 60.0%.
 - iii. The *Massmart Ethics Indicator* validity score is 69.0%.

Employing the Global Compact performance model, we will provide further analysis and insight into the activities of Massmart. Where possible, results from the *Massmart Ethics Indicator* will support discussion of these points.

2. Evaluating Massmart's Corporate Citizenship

It is not often that one finds a company where financial success is matched by demonstrated ethical commitment. Massmart may be viewed as providing tangible evidence for the assertion that well-managed companies are motivated to act ethically.

From a financial perspective, the group has performed very well, achieving nine successive years of record turnover. In its five years as a listed company, the group has achieved compounded growth in headline earnings of 33.1%. This has been supported by compounded growth of 35.6% in trading cash flow and has led to an 81% compounded growth in dividends to shareholders.

Being a holding company that evolved rapidly through a vigorous acquisition programme, and not through long-term organic growth, leadership was faced with the challenge of retaining the organizational characteristics that made its divisions attractive acquisitions in the first place, while recognizing that Massmart is a publicly listed entity, needing to comply, at a minimum, with regulatory standards set by the Johannesburg Securities Exchange and national legislation.

However, as we shall see, Massmart leadership went beyond a minimalist compliance approach and aimed for ethical excellence in pursuit of its goal of becoming a highly profitable retail force, capable of returning sustainable value to its stakeholders.

The issue of sustainable value creation and the diversity of the various businesses led Massmart leadership to adopt a “soft hands” approach, avoiding unnecessary interference in the culture and practices of the divisions, while using an ethics management process to craft an overarching ethical framework guiding the conduct of its constituent divisions.

The main ingredients of Massmart’s success are, therefore, its leadership, in terms of strategic vision, business skill and ethical commitment, and its capacity, through an ethics management programme and other supporting systems, to encourage ethical behaviour throughout the group.

2.1 The Performance Model

2.1.1 Defining the vision – The organisation as moral community?

“While business is not democratic, the context of modern democracy demands transparency, accountability and stewardship from all entrusted with assets or power.”

Mr Mark J Lamberti
CEO and Deputy Chairperson

Mr Lamberti’s comment mirrors our experience of Massmart as an organization that is highly competitive in a very competitive industry, but with monetary gain being understood and realized in terms of value creation – in other words, in terms of the Massmart values, encompassing goals broader than the limited pursuit of headline earnings at any cost.

According to Collins and Porras, the authors of the acclaimed work, *Built to Last*, this is the characteristic that differentiates the good from the great, the short-lived from the lasting:

“Profit maximization does not rule, but visionary companies pursue their aims profitably. They do both.”
p 54, *Built to Last, Successful Habits of Visionary Companies*

In many respects this predisposed the company to develop a vision of itself not solely as a legal vehicle pursuing profit but as a moral entity pursuing sustainable value creation. As a holding company, the concept that springs to mind is that of a moral community. This is an interesting concept for it has wide ranging implications. Most generally it requires a high level of vision, leadership and organizational maturity. It is worth briefly exploring this concept by reverting to a bit of philosophy.

The American philosopher, John Rawls, contrasted the so-called private and social natures of humankind. The private nature tends to be, whether it encompasses individuals or associations, inclined to pursue its own selfish ends that are in themselves competing with other ends. A second aspect of this private nature is that since it possesses no inherent values other than immediate gratification governing its interaction with self and others, it experiences engagements with various stakeholders as a burden to be avoided. All social arrangements are therefore only perceived as means to private ends. Common sense indicates that this is not a premise upon which a sustainable or moral community can be built.

Who was John Rawls and why is he important?

Rawls is an American philosopher much involved in the development of an understanding of the ethical dimensions of communities. In his seminal work, *A Theory of Justice* (1971), he argues that the merging of individuals into larger communities, sharing a common purpose, is vital to the moral development of the community as an entity and therefore those that operate within it. The importance for business ethics and those interested in the theoretical foundations of the Global Compact's goals for enhancing responsible business conduct, is Rawls's insistence that a business, as a social unit, is a moral community, and therefore not just a legal construct with compliance imperatives projected upon it, but rather ethical obligations originating from within it.

Box 3: John Rawls and business as a moral community

In describing the social nature of humankind, it is best to quote Rawls directly:

“... The social nature of mankind is best seen by contrast with the conception of private society. Thus human beings have in fact shared final ends and they value their common institutions and activities as good in themselves. We need one another as partners in ways of life that are engaged in for their own sake and the successes and enjoyments of others are necessary for, and complimentary to, our own good”

A Theory of Justice, p422.

Rawls equates this development of a social nature, essentially of a caring society (or organization), as being critical to the attainment of justice. In order to do so, the society, Massmart, needs to encourage “justice” through the pursuit of what is good, right and fair, not so much because it understands good ethics to be good business, i.e. good for the bottom line, but because it is the correct thing to do – principally. Justice originates from the way you are, not so much from the way you act. The business spin-off is welcome, but incidental.

Massmart leadership, possibly without an academic interest in philosophy in general or Rawls in particular, have been growing the organization to be what Rawls describes as a moral community. Massmart is, in that sense, being actualized, to be more than a vehicle pursuing profit, while being profitable in the process. They have been doing so by merging competence with universal ethical principles as social glue welding the various members of the community (divisions, departments, employees) together into a recognizable Massmart whole, while recognizing the uniqueness and autonomy of those in the community.

This pragmatic but principle-orientated approach to ethics Collins and Porras describe as having a core ideology (p 73). It informs the organization's core values, guiding principles, and its purposes, its fundamental reasons for existence beyond just making money. Without it, they state, organizations flounder when faced with the constant tension between conformance and performance in entrepreneurial environments. It has nothing to guide its action beyond the peculiarities of specific circumstance explaining why so many others get lost along the way.

2.2 Evaluating leadership

“If I cannot get my stock off the ships without paying bribes, I will offload them myself. If I cannot get it out of the port for the same reason I will get out of the country.”

Mark J Lamberti
CEO and Deputy Chairperson

The above stated position of principle was espoused during a recent interview with the Massmart CEO, when he stated his refusal to adhere to different ethical standards when engaging in countries where officials commonly demand bribes.

Notwithstanding these positive sentiments by leadership, ethical leaders do not automatically lead ethical organizations.

Leaders need to work to be ethical role models. Statements alone, although important, will not sufficiently influence the behaviour of those being lead, especially in the lower echelons of the organization, far removed from head office and the board room.

The espoused commitment to responsible business conduct must be matched by a perceived commitment of leadership and senior management to walk the proverbial talk.

The *Massmart Ethics Indicator* provides interesting data, comparing the levels of communicated commitment to ethical conduct emanating from leadership (the espoused commitment) versus whether leadership will turn away business that does not meet these espoused standards (the perceived commitment).

While a full alignment in any organization is unlikely it is important that gap between these two indicators is not too great. Emerging from this comparison, 88% of employees reporting being aware of top management's exposed commitment to ethical values, with 76% believing top management to be sincere in this regard.

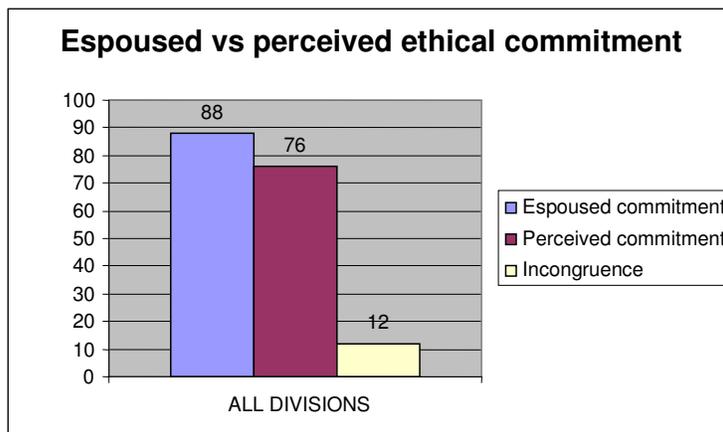


Figure 1: Espoused vs. perceived ethical commitment (a combination of Figures 3 and 4)

From the above analysis one may deduce that only 12% (see Figure 1, above) of top management is not perceived to be sincere. Inversely explained, with seven out of eight managers perceived to walk the talk, this is a positive confirmation that ethics in Massmart has developed beyond just talk emanating periodically from the boardroom.

In order to achieve such positive statistical results the vision of Massmart as a moral community required a vehicle to become a reality, a vehicle that needs to be steered by leadership and maintained by management.

Subsequently the Massmart Executive Committee undertook to implement a comprehensive ethics management programme during March 2004. According to Mr Brian Leroni, Director of Corporate Affairs, the decision was driven by an understanding that highly ethical conduct:

- Plays a significant role in good corporate risk management;
- Facilitates better and more consistent corporate decision making;
- Elicits more constructive responses from business partners and stakeholders; and
- Promotes employee happiness, effectiveness and workplace satisfaction.

The cornerstone of this programme was a practical vision for ethical practice. A key consideration in the collaborative formulation of this vision was that it had to have intuitive relevance for employees at all levels in the organization. An essential component of the vision involves the use of practical examples to describe the target ethics end state. The Massmart vision for ethics is described in *Figure 2*, below.

<p>Our Organization is Free of:</p> <p>Politics, Back Biting, Favouritism, Abuse of Power, Vindictiveness, Machoism, Theft, Fraud, Discrimination, Corruption, Intimidation, Sexual Harassment</p>	<p>Our Organization is Committed to:</p> <p>Transparency, Fairness, Personal Respect, Accountability, Employment Equity, Honesty, Individual Privacy at Work, Social Responsibility, Fair Remuneration, Respect for HIV Positive People, Natural Environment</p>
<p>Our Organization Facilitates and Ensures:</p> <p>Effective Ethics Education & Communication, Encouragement of Ethical Behaviour, Consistent Enforcement of Discipline, Immediate Reporting of Ethical Misconduct, Adherence to SHE Regulations, Integrity Considered in Promotions, Ethical Violations Addressed Openly, Responsiveness to Ethical Concerns, Employee Accessibility to Competent Ethics Officer, No Pressure to Behave Unethically</p>	

Figure 2: Massmart vision for ethics

Importantly, embarking on an ethics management process in Massmart was not preceded, as is often the case by some major critical event of an ethical nature. Commendably, leadership had the vision to embark on an organized process of trust enhancement among all stakeholders rather than post haste, post facto attempts at trust recovery.

Furthermore, very positively, an ethics management programme in Massmart has not been interpreted as an attempt to fix a defective business plan – something it can, in our experience, never do. As highly experienced retailers, Massmart is making money and its business plan is returning healthy bottom line numbers.

“Profitability is a necessary condition for existence and a means to more important ends, but it is not the end in itself for many of the visionary companies. Profit is like oxygen, food, water, and blood for the body; they are not the point of life, but without them, there is no life.”

James C. Collins and Jerry I. Porras, p 54

Built to Last, Successful Habits of Visionary Companies.

2.3 Driving empowerment – Making ethics a part of daily work life

Employees that do not have confidence in its employer’s ability to consistently apply its own policies, tend to resist making decisions, fearing some form of real or perceived backlash. Accordingly decisions are then made in a committee context, an often cumbersome vehicle that may be designed solely to deflect personal accountability in case of blame.

In our experience, organizations suffering from a lack of leadership vision and clear management guidelines, encourage inconsistent application of its policies and promote breeding a blame culture.

Such a blame culture inhibits organizational ability to innovate and quickly react to changing market conditions. This is because, in an ironic twist, a blame culture often originating from inconsistent application of policy encourages a flight to more policy. Without recognizing that the underlying cause may not be the policy itself but those utilizing it, an organizational response to a blame culture, is often more policies - policies that may very well just lead to further inconsistent application.

The result is the inevitable blossoming of organizational bureaucracy that a low margin, high volume business like Massmart could ill afford.

Subsequently, the desired manner of empowerment meant retaining the entrepreneurial qualities of successful shopkeepers, hard working, honest, straight forward and innovative – and exporting it into every aspect of its business.

Therefore its aim was to empower employees, and ultimately stakeholders beyond the group, to understand exactly what type of conduct would be supported by Massmart and what types it would not support. Good ethics facilitates good and defensible decision making, and subsequently increases general organizational effectiveness.

The *Massmart Ethics Indicator* provides compelling evidence that the organization is starting to reap the benefits derived from its leadership's vision. See *Figure 3*, below.

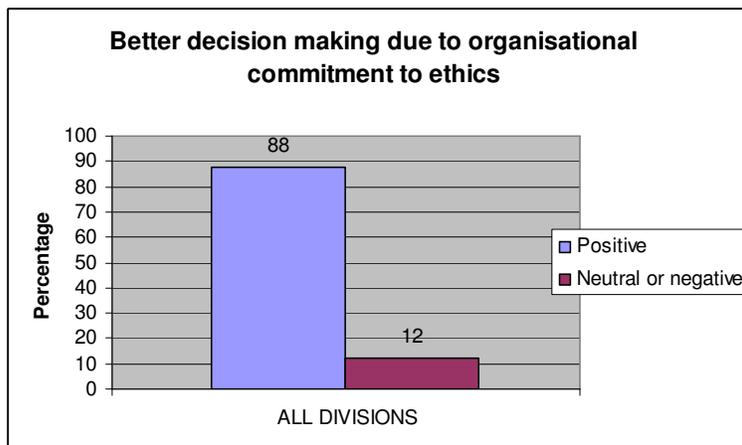


Figure 3: Better decision making due to organisational ethics commitment

In order to achieve such empowerment and in pursuit of its vision of a moral community, Massmart established a dedicated ethics management process to provide a decision making framework designed to integrate responsible conduct into the daily work lives of its employees.

This has been achieved by the combined effects of ethics advocacy by the CEO, ongoing training, a policy environment that is aligned to ethical good practice, and a robust process for encouraging, and enforcing good ethical practice. These elements are combined into a comprehensive programme that is integrated into all divisions and at all levels of the Massmart group. See *Figure 4* below.

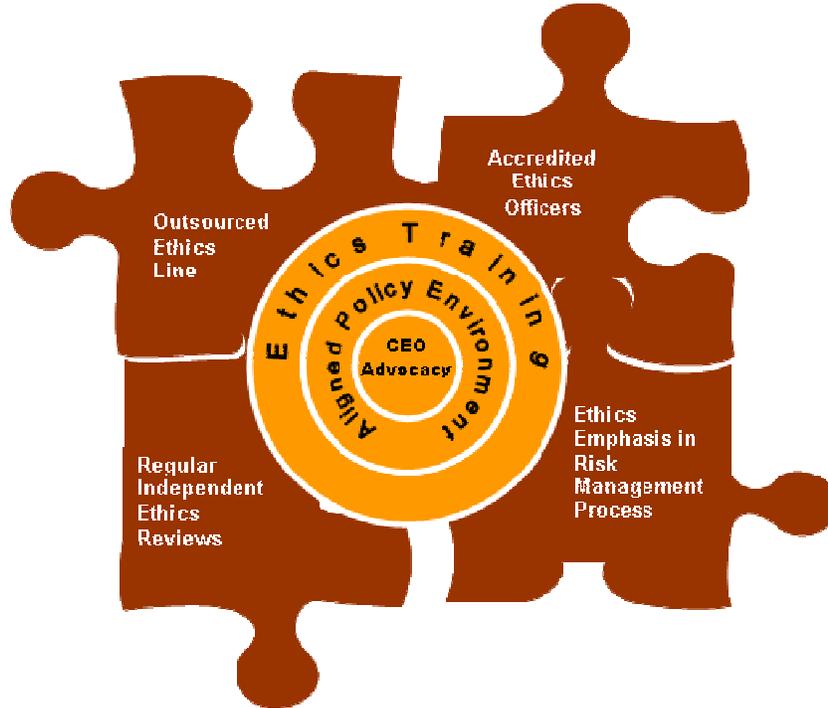


Figure 4: Massmart's ethics management programme

One of the special benefits of this empowerment programme is the creation of a culture of reporting unethical conduct.

An ethics management programme is designed to ensure the availability of safe and well managed reporting facilities, internal and external to the organization. It is the creation of this culture that ultimately ensures that every employee becomes a weapon in an organizational arsenal for combating corruption. This aspect is discussed at greater length in the next section.

2.4 Formulating policies and strategies

2.4.1 Codifying the values – Ethical principles for all stakeholders

“Our belief is that successful business is built on the foundations of good corporate citizenship, which we take to mean acting responsibly and with the highest standards of ethics and integrity in our dealings with all stakeholders.”

Mark J Lamberti
CEO and Deputy Chairperson

With the vision of Massmart as a moral community as the starting point, the organisation defined ethical principles that would have relevance for all its stakeholders. In keeping with good practice, Massmart established ethical standards that would apply to everyone in the chain of business – employee, customer or supplier.

The group defined eight stakeholder engagement principles, incorporating practical examples to facilitate understanding:

- We will always **abide by the spirit and the letter of the law** in the way that we conduct our business.
- We will always **maintain accurate and reliable records** that provide a fair representation of all business transactions and that are consistent with Generally Accepted Accounting Practices (GAAP), as well as our legal and financial reporting requirements.
- We will always strive to **create a stimulating and safe working environment** that is underpinned by respect for the rights of individuals and that is free of prejudice in all its guises.
- We will always **act in the best interests of our customers** paying particular regard to their expectations of product quality, product safety, competitive pricing and advertising that is not false or misleading.
- We will always compete fiercely in our chosen markets, but we will **not resort to dishonest tactics in order to gain advantage over our competitors.**
- We will **maintain strictly professional relationships with suppliers of goods and services.** We will specifically not engage in any activity, accept or offer gifts, favours or hospitality that may compromise our ability to deal with our suppliers objectively and without special favour.
- Our employees will always **perform their responsibilities professionally, honestly** and in a way that serves the legitimate interests of our stakeholders.
- We will always **act as a compassionate and responsible corporate citizen** that is in touch with the issues facing the communities in which we operate.

These principles serve as benchmarks against which Massmart evaluates its decision making, both in terms of its internal management and its corporate strategy.

2.4.2 Ongoing awareness – Scenario-based training

The decision to conduct interactive, scenario-based sessions was, in part, driven by awareness that it better facilitates learning, especially ethics learning, and, in part, by the diversity of operating cultures within the various division throughout the group.

The training is based on eliciting employee responses to topical public and work life scenarios. Participants in the training are required to debate ethical dilemmas such as the conflict between needs for punishment and compassion – being a typical dilemma managers constantly face

Furthermore, the training requires participants to evaluate their own, their managers' and the organization's ethics on a series of predefined ethics questionnaires. This offers the opportunity for introspection but also provides the company with important feedback about employee perceptions of the groups approach to ethics. During the first six months after renewing its ethics drive, Massmart exposed in excess of 14 000 employees to the group's ethics training process.

2.4.3 Establishing internal management capacity – Accredited Ethics Officers

Massmart took an early decision to appoint accredited Ethics Officers in all its chains. Trained by EthicSA and acting under the guidance of a Group Ethics Officer, they are the custodians of ethics in the organization.

The Ethics Officers are specifically tasked with ensuring that instances of alleged ethical misconduct are thoroughly investigated and properly resolved. As previously mentioned EthicSA to date has trained 13 Ethics Officers in the group.

Ethics Officers' independence is indicated by the fact that the Chief Ethics Officer reports to the Massmart Audit Committee, the chairperson of which is a non-executive director. This arrangement is also significant for another reason, in that it enables Massmart to integrate its ethics activities with the group's broader risk management process. Subsequently, internal ethics audits are conducted at regular intervals by the Massmart Internal Audit Department.

2.4.4 Independent ethics reviews – The *Massmart Ethics Indicator*

While internal monitoring of ethics practices is extremely beneficial, Massmart has voluntarily opened its ethics practices in the group to scrutiny by external organizations. Such scrutiny has included a comprehensive ethics review conducted by EthicSA – the *Massmart Ethics Indicator*.

EthicSA had unfettered access to engage employees of all employment hierarchies, all of whom were free to provide feedback anonymously, depending on their preference.

The *Massmart Ethics Indicator* provided a scientifically sound benchmark against which to measure the performance of further interventions.

Another advantage is, based on recommendations derived from the survey results, that Massmart may customize interventions to meet the specific requirements of each division.

2.4.5 Outsourced Ethics Line – The *Massmart Ethics Line*

Since the capacity to detect unethical conduct is central to a corruption prevention programme, Massmart established, in conjunction with confidential internal reporting paths, an anonymous *Massmart Ethics Line*, run by an independent private company.

This line is available to employees and suppliers as a mechanism of last resort for creating awareness about unethical conduct. The line features a 24/7 service and is staffed by operators who are proficient in five languages.

A total of 251 calls were made to the ethics line during the period June 2005 to May 2006. All calls are investigated followed by appropriate remedial action. Callers are able to track anonymously the investigative process and the group's response to the call through the use of a unique tracking number.

There is anecdotal evidence that the *Massmart Ethics Line* appears to be working. Mr Bryan Hacking, Ethics Officer within a major division of Massmart, recently told the author of a victimization case affecting a unionized worker. The case was reported via the *Massmart Ethics Line* by the employee's union representative, specifically to test whether the facility is effective. Being skeptical, the union representative was surprised when the report was dealt with, resulting in the transgressors being disciplined.

A similar case was reported by Mr John Hawksley, the Chief Ethics Officer, where the *Massmart Ethics Line* recently was instrumental in exposing a major fraud being conducted in the organization.

Such successes greatly enhance employee confidence in the line and are possibly more compelling indicators of an anonymous reporting line's success than survey data can ever offer.

However, again looking at the *Massmart Ethics Indicator*, survey results confirm that the *Massmart Ethics Line* appears to be working, although in certain divisions better than others.

In terms of combating unethical conduct such as corruption results drawn from the *Massmart Ethics Indicator*, management has objective data indicating the levels of observed misconduct, its frequencies, and the tendency to report such observed events.

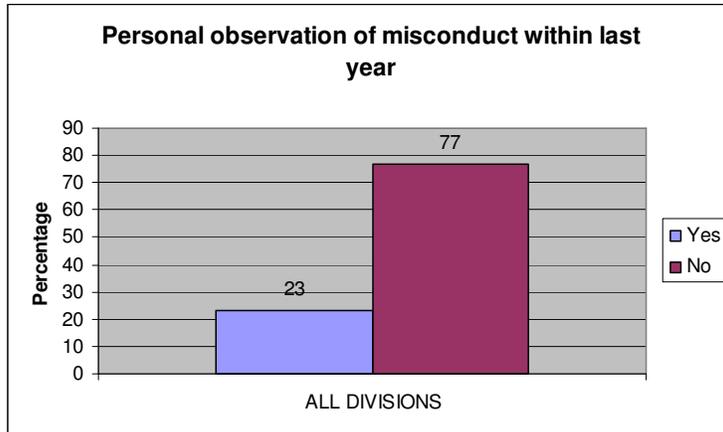


Figure 5: Observation of misconduct in past year

Judging from *Figure 5*, above, approximately every fourth employee in Massmart observes some form of unethical conduct in the group. From other data it emerged that in almost 60% of all cases this is at infrequent and very infrequent rates. Given the extent of the opportunities for unethical conduct present in a large organization retailing physical goods, this is overall positive, but certainly not a perfect finding.

Many of the types of observed misconduct that were reported during the *Massmart Ethics Indicator* survey were not theft, fraud or corruption, but issues falling within the traditional human resources domain (sexual harassment, intimidation et cetera). This was confirmed by the majority of reports to the *Massmart Ethics Line* being also of a human resources nature. This may indicate that in some divisions more attention needs to be given to establishing trust in traditional grievance procedures, usually administered by Human Resources departments.

The fact that over a third of employees do not report observed incidence of misconduct, is worrisome and reflects general cultural biases against using Ethic Lines, real concerns over safety and fear of victimization, and a general distrust in the effectiveness of the facilities (see *Figure 6*, below).

Massmart has, however, made progress in addressing these concerns and a future *Massmart Ethics Indicator* study may provide objective data confirming anecdotal evidence that a culture of reporting is taking hold in many of its divisions.

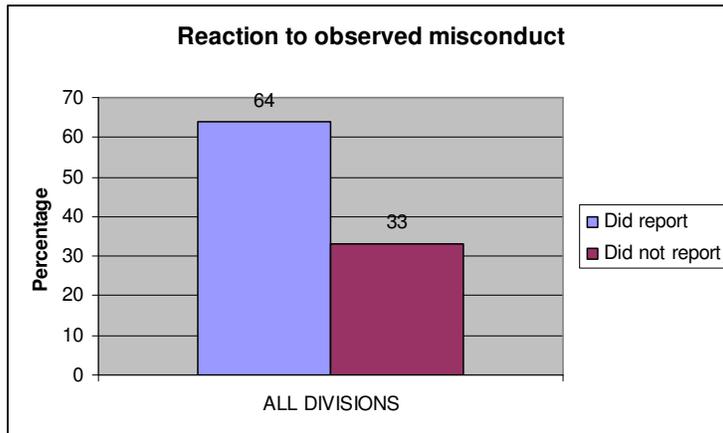


Figure 6: Reporting observed misconduct

2.5 Providing Resources – a sign of true commitment

EthicSA often encounters espoused commitments to responsible conduct from leaders when engaging with various organizations. However, in many cases such commitments are compromised by a lack of resources to get the job done. Sufficient resource allocation both in human and financial terms are signs of true commitment to any organizational initiative.

2.5.1 Human capital

Organizations without internal capacity cannot sustainably commit to any initiative, let alone an ethics management programme. External advisors cannot manage an organizational culture or the manner in which it endeavors to live its vision on behalf of management or leadership.

A sustainable commitment to an ethics management programme and good corporate citizenship requires the custodians of such initiatives, to be properly trained and supported. The custodians of these initiatives are often Ethics Officers, being members of management specifically tasked with managing ethics throughout organizations.

As mentioned under *Item 2.4.3, above*, EthicSA has trained to date 13 Ethics Officers throughout the group. They are tasked to daily interpret the ethics vision emanating from leadership. Under the coordination of a Chief Ethics Officer, located in head office, the various ethics officers operating in the divisions meet quarterly to pool experiences, provide feedback and plot future strategies.

None of the Massmart Ethics Officers fill their positions full-time and all have other roles within their respective divisions.

These Ethics Officers are in turn supported by other departments in the organization in terms of ongoing training and awareness, investigations and general counsel. The various Ethics Offices within the group are subject to internal audit procedures, conducted by internal auditors that received Ethics Officer training.

The biggest shortcoming in terms of the collective Massmart Ethics Office is an apparent lack of support in terms of what may be called an Ethics Champion network comprising members from all employment hierarchies.

Ethics Champions do not manage an ethics programme as Ethics Officers would do, but received special training in elements of the ethics management process, often the Code of Ethics, in order to be the first point of ethics advice for fellow employees.

In the case of Massmart, members of senior management in each division did receive additional special awareness training but being further removed from shop level employees it is unlikely that they will be approached by employees with the same level of candor than Ethics Champions taken from among their own peer group will.

A lack of easily accessible Ethics Champions and possible trust concerns with the grievance procedures under the custodianship of Human Resources may result in external reporting procedures being used to ask for advice or report on incidences best handled elsewhere.

When looking at the high levels of human resource related reports being reported to the *Massmart Ethics Line* this may very well be the case in some divisions.

2.5.2 Financial capital

In terms of the ethics management programme an initial establishment budget of approximately R1.6 million was allocated for specialist consultancy fees and training, both of Ethics Officers and wider among employees throughout the group. However since then, the daily running of the various Ethics Offices has been fully incorporated into normal business operations with no specific and separate budget allocate to it.

The running costs of the *Massmart Ethics Line* and the investments required for periodic *Massmart Ethics Indicator* surveys as well as specialist consultancy costs are bourn by head office.

Due to committed leadership support for ethics management resource allocations are generally good and commendable.

2.6 Innovation and process

2.6.1 Corruption prevention

The most effective detection tool in an organization is fellow employees. Yet, corrupt acts are often enveloped in a culture of silence, where employees are either too scared or too apathetic to report corruption.

An ethics management programme is partly designed to ensure the availability of safe and well managed reporting facilities, such as a hotline, to break the culture of silence in which corruption thrives.

However, it is important to note that Massmart did not attempt to specifically combat corruption when embarking on an ethics management process. Rather, the focus was to holistically develop a responsible business, committed to good corporate citizenship, the pursuit of which includes building an organizational culture that does not tolerate corrupt acts.

Therefore, the simple premise is that an organization committed to good corporate citizenship will be committed to protecting human rights, upholding proper labour standards, protect the environment and strengthen its capacity to prevent, detect and act upon corruption within its sphere of influence.

Importantly the combating of corruption, in a preventative sense, cannot always be distinguished from combating and resolving other issues of an ethics nature. Massmart managers reported cases of sexual harassment, religious factionalism, conflicts of interest and favouritism being surfaced through the various reporting paths within the organization. Successfully resolving these issues builds confidence in the organization, and its reporting procedures. This may result in the organization being better able and prepared, to detect and successfully managed cases of fraud and corruption.

2.6.2 Corporate Citizenship

Massmart understood that, to ensure the sustainability of its responsible corporate citizenship vision, it had to start with the promotion of responsible business conduct within its constituent businesses or divisions – hence the ethics management programme and, in particular, the Massmart Code of Ethics, informing the nature of its corporate social investments.

In this respect, Massmart avoided a common problem among many engaging in corporate social investments, namely that such initiatives, designed to enhance the sustainability of the organization, are built on unstable bases, with the promotion of ethical conduct not advanced or integrated into the operational fabric of the organisation.

We are of the opinion that without a strong ethical base, corporate social investments become mere investor relation exercises rather than sustainable initiatives flowing from an internal commitment to responsible business conduct.

Therefore, we argue that a good ethics management programme forms the heart of organizational attempts to protect human rights, adhere to internationally accepted labour standards, protect the environment, and combat corruption.

Simply, an organization not committed to responsible business conduct in its operations cannot sustainably commit to responsible business conduct in the communities in which it operates.

With the foundations of the Massmart Ethics Management Programme in place, the capacity to promote ethical conduct among employees increased. With a lowered internal risk profile, Massmart could thus pursue corporate social investment initiatives, not as isolated projects, but as coherent expressions of its vision and values.

2.7 Impact on people – taking ethics home

Probably the most fundamental impact among Massmart employees has been the ethics management programme's ability to increase organizational effectiveness, both through increasing the ability and confidence of employees in making decisions and taking responsibility (see *Item 2.3*, above) and the creation of a culture of reporting. The latter, as discussed under *Item 2.4.5*, above, has significantly increased Massmart's ability to detect corruption.

It is worth to quote directly from the general conclusion of the *Massmart Ethics Indicator*.

"In respect of all of these components of the survey, Massmart divisions show very positive results. Generally speaking, individuals across all employment levels are satisfied working in Massmart divisions and think highly of their integrity, not only as proclaimed, but, very significantly, also in respect of "walking the talk".

Interestingly, in various ways recent ethics initiatives at Massmart divisions are clearly known and positively appraised. Employees appear to have developed capacities and inclinations to make ethical distinctions, to reason about ethical issues they face in the workplace, to seek advice on ethical issues, and to report ethical misconduct.

Importantly, the data reveals that not all Massmart divisions are on a par in respect of their ethical performance. However, those that are lagging behind, for whatever reasons, appear to benefit significantly from these recent ethics management interventions, which is very positive and encouraging"

Massmart Ethics Indicator, p 29

For more background on the Massmart Ethics Indicator, please refer to *Item 3.3.4*, below.

In terms of its corporate citizenship initiatives, the most significant are its HIV/AIDS treatment programme and its black economic empowerment drive.

2.7.1 ARVs for staff and family

With over six million infected South Africans, HIV/AIDS is a major challenge in Southern Africa. The retail industry is particularly hard-hit, seeing both its employment and customer-bases eroded by the effects of the disease.

In 2001, the group launched an HIV/AIDS management programme incorporating prevalence testing, peer counseling, support, and widespread education initiatives. The next step was to provide for specific HIV/AIDS treatment.

However, the provision of antiretroviral treatment (ARVs), presented Massmart with a dilemma. Treatment of an infected employee alone, in many cases, did not suffice due to the employee's spouse also being infected.

An employee was faced with the terrible possibility of gaining access to ARV's that the government for numerous reasons did not supply, while watching a spouse waste away from the disease.

Therefore, Massmart had to make a strategic decision to extend its HIV/AIDS programme to include antiretrovirals (ARVs) for infected permanent employees *and* spouses, even though spouses may not be employees of Massmart.

This initiative forms part of Massmart's broader employee Health and HIV Management programme. Called *Impilo* – meaning health in the Xhosa language – this health programme incorporates a 24-hour, toll-free helpline that connects employees to healthcare professionals who provide medical emergency and healthcare advice.

2.7.2 Broad-based Black Economic Empowerment as an ethical imperative

The South African government has launched a socio-economic development programme aimed at uplifting black South Africans.

Referred to as Broad-based Black Economic Empowerment (BBBEE), it encourages organizations to commit to a set of socio-economic development principles. These principles include increasing investment in the development of black employees, implementation of affirmative action policies, opening business opportunities to black entrepreneurs, and assisting black people to increase their ownership stake in South African businesses.

In support of BBBEE Massmart placed 16 million Massmart shares, representing approximately R1 billion of Massmart's shareholding, into an Employee Empowerment Trust called *Thuthukani*.

Most significantly, however, is that share allocations were not made on the basis of seniority or value of remuneration since this would result in the BBBEE programme not being truly broad based. Instead, Massmart took the decision to allocate equity to staff based on one criterion – length of service.

2.8 Impact on the value chain

Considering that Massmart procures goods and services from thousands of suppliers it has the opportunity to export its commitment to responsible business conduct to those that it has daily regular business with. Given the variety of products, and the scope of concerns that may arise, this can be very challenging.

A classical example recently recounted to the author concerns the stocking of a condiment causing concern, for although the product is very popular with consumers and was passed by South African health authorities, international evidence started to emerge that the product contains significant amounts of very harmful chemicals. In such cases do you refrain from stocking your stores with the product in spite of consumer demand, or do you simply give the client what they appear to want? Where does the organization's responsibility begin, and more importantly, where does it end?

Another case is the stocking of a specific kind of braai (barbecue) equipment that appears to encroach on the patent rights of a famous high-quality South African brand. The product is made to intentionally look the same but is significantly cheaper and of inferior quality. In this particular case Massmart took the decision to not stock this particular product anymore.

We are of the opinion that Massmart could do more to set up clear guidelines, derived from their vision and Code of Ethics, in order to provide managers with the tools to resolve such dilemmas.

One often neglected aspect of the supply chain, that Massmart did pay detailed attention to, is mitigating the environmental impact of some of its suppliers.

2.8.1 Protecting the Environment - Ethical practice in the supply chain

While a common notion tends to exist that the retail industry has little environmental impact, this is misleading. Massmart embarked on a programme of encouraging suppliers to be more aware of their environmental impact. One example is the fishing industry with the popularity of seafood resulting in many marine species being over-fished. Subsequently Massmart identified its fish and shellfish suppliers as a priority focus area.

Over a five month period, it conducted a survey of supplier fishing practices, to verify that the group was applying responsible marine procurement practices. The survey served to highlight that:

- None of the fish species that Massmart stocks are listed on the 'No Sale Species' list of the World Wide Fund for Nature's Southern African Sustainable Seafood Initiative;
- The group only stocks dolphin-friendly tuna and does not sell bluefin tuna, which is severely over-fished; and
- Massmart's locally-caught hake is sourced from Marine Stewardship Council (MSC) certified fisheries. Gaining MSC approval requires that these fisheries adhere to stringent operating principles, verified by experts.

2.9 Gauging the impact on society

As an organization with a large employee population, procuring products and services from thousands of business, often from within the communities which it operates; Massmart has considerable influence on society. Good corporate citizenship requires of Massmart to match its position of influence by a commitment to act ethically and responsibly.

Massmart is using its Code of Ethics (*see Item 4.2.1, above*) as one of the vehicles guiding the group's internal and external responses to business imperatives. In this way, the group has brought to life, from within the organization, its commitment to highly ethical conduct in the broader community.

In keeping with the vision of Massmart as a moral community, this involved moving beyond a narrow interpretation of ethical practice that focuses solely on protecting the group's obvious commercial interests. Massmart has shown a commendable willingness to extend its ethical commitment beyond the realm of direct commercial self-interest and into the ambit of public interest.

It is worth mentioning some examples:

2.9.1 Participation in the Johannesburg Securities Exchange Socially Responsible Investment (SRI) Index

Massmart qualified for inclusion on the Johannesburg Securities Exchange Socially Responsible Investment Index each year since its launch in 2004. In its *2006 SRI Index* assessment, Massmart scored a total of 181 points, substantially exceeding the baseline qualification mark of 78 points.

2.9.2 Nurturing new businesses

Meeting the socio-economic needs of South Africa's poorest is a national concern that cannot be addressed by government alone. In South Africa this means providing assistance to marginalized groups such as unemployed youth and rural women. Massmart responded through a partnership with the *Umsobomvu Youth Development Fund* to create enterprise development opportunities for unemployed black youths. The project received a R1 million contribution from Massmart (and a matching contribution from *Umsobomvu*) that is being used to establish unemployed youths in micro or entry-level franchise businesses.

Massmart has also provided a R1 million interest-free loan to Women's Development Businesses (WDB), which runs a micro-finance programme for rural women. The programme provides small loans – of between R5,000 and R15,000 – to very poor rural women, so that they can develop micro-enterprises to generate household income. In order to participate, women need to be part of a team of at least ten members, who are able learn from and vouch for each other. Massmart pays the salaries of two WDB field workers who provide the participating women with ongoing advice and support.

2.9.3 Investing in communities

Following from the Massmart's Code of Ethics commitment to "act as a compassionate and responsible corporate citizen" the group's overarching corporate social investment (CSI) objective is to support education of previously disadvantaged individuals.

Each trading entity is required to spend 1% of after-tax profits on educationally-focused CSI initiatives. This is in addition to the group's focus on unemployed youth and rural women.

2.10 Reporting and communication on progress

In our experience large organizations tend to suffer from poor communication, both internally and externally to various stakeholders. While we have no particular knowledge about how well Massmart communicates on subjects other than ethics, one may deduce that if you are proficient at one you may very well be proficient in communicating other subjects pertinent to its business.

When reporting on various corporate citizenship initiatives, be it internal or external to the organization, a fine balance between making known worthy accomplishments and engaging in what may be considered inappropriate traditional marketing, is required.

2.10.1 External communication

Especially in the case of Massmart it is important for investors and other stakeholders to know what the organization is doing, but in a manner that underlines a commitment to doing the right thing, primarily out of principle and only secondarily, out of a desire to affect favourable outcomes for the business.

The most logical vehicle is the annual report and ideally a special corporate citizenship report. It is in this respect that Massmart has shown significant improvement. Still a special corporate citizenship report, independently verified by an appropriate assessor is lacking and would be highly beneficial.

Massmart on a regular basis also employs specialists to manage press releases on its corporate citizenship initiatives.

Further, the Massmart website (www.massmart.co.za) has an extensive section on ethics and governance, including a web based version of the Code of Ethics.

A copy of the *Massmart Ethics Indicator* is also published on the website.

2.10.2 Internal communication

Generally the *Massmart Ethics Indicator* paints a positive picture of employees enjoying high levels of ethics awareness.

Some data from the survey supports this view with the following:

- 98.8% of respondents were aware of Massmart's ethical standards;
- 90.5% of respondents find the ethical standards useful;
- 89.4% of respondents are aware of avenues for reporting ethical misconduct;
- 81.3% of respondents indicate that they can report misconduct without fear of retaliation; and
- 81.3% of respondents indicate that line managers are held accountable if they are caught violating the organisation's ethical standards.

This dataset vindicates the time, money and energy spent on driving a programme of responsible business conduct through the organization.

Massmart also circulates a regular internal magazine, addressing various topics. At the time of writing, the current copy in circulation contains an article on ethics and ethics management by the Mr Lamberti, the CEO.

3. Conclusion – the way forward

Massmart achieved a lot in a short period of time. In many respects the organization implemented a model ethics management programme. Its outreach programmes in the community also makes a positive difference in the lives of those touched.

Organisations can however always do more, with probably one of greatest areas requiring attention being in the environmental field and the corruption prevention fields.

In environmental terms this would include decreasing Massmart operation's own environmental footprint, especially in terms of energy use, and launching programmes, similar to the above mentioned responsible fisheries project, to encourage good environmental practices among various suppliers.

In terms of corruption prevention, its efforts to create a safe reporting culture has been very successful in certain divisions but less so in others. Organisational culture change does not happen overnight and requires sustained effort of up to 5 years in order to make a culture of reporting, of effective corruption prevention, evident in all divisions.

Strategically, from a risk perspective, the greatest risk may well be an aspect that counts so much in favour of Massmart, namely its profitability. In the current climate of robust economic growth and high consumer demand, some may argue that Massmart's management is yet to pay a significant price for its principled commitment to good ethics.

Yet there are already worrying signs that South African economic growth is driven, not by increased remuneration, but by increased credit extension. As household debt levels escalate any change in the interest rate environment may very well have an adverse effect on consumer demand. This may result in performance to ethical conformance pressures being felt at intensities not previously experienced.

Also, in the light of the continued need to unlock new markets, especially in Africa, where corruption is often ingrained in the operating cultures of those economies, the need to maintain ethical conformance may be further outweighed by the need to perform financially. The risk remains as a mergers and acquisitions environment is often a graveyard for many espoused ethical ideals.

This is not a challenge unique to Massmart but it does underline the necessity of values-based leadership and proper succession planning. The current CEO, an integral force behind the development of Massmart as a moral community, is due to retire at the end of 2006. The incumbent has an obligation to maintain the “moral community” that is Massmart.

4. Bibliography

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