

# The Corporate Social Responsibility Orientation of Chinese SMEs

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## Abstract

*This paper examines the Corporate Social Responsibility (CSR) orientation of Chinese Small and Medium Enterprises (SMEs) based on their internal functions, including training, job creation, quality assurance and environmental sustainability. In addition, it also examines the relationship between their CSR orientation and firms' financial performance. Despite SMEs' participation and investment in training, job creation, and environmental sustainability, their involvement and action have not produced a statistically significant positive relationship with their financial performance (as measured by profitability and sales revenue). The only CSR-oriented activity that registered a statistically significant positive impact on financial performance was quality assurance.*

## Keywords

*Employee training; environmental sustainability; job creation; profitability; quality assurance; sales revenue*

## Introduction

Research on Corporate Social Responsibility (CSR) practice has been focused heavily on large corporations and is relatively scant on Small and Medium Enterprises (SMEs). This imbalance is due to the higher CSR profile of larger corporations, which have largely driven CSR activities (European Commission, 2001). Although the individual contribution of a SME to an economy may appear relatively insignificant, when compared to a large transnational corporation, the aggregate contribution of all SMEs can be sizeable. SMEs constitute more than 90% of enterprises and account for at least half of employment in developing countries (OECD, 1997; Luetkenhorst, 2003). SME engagement in CSR is of crucial importance to the economy because SMEs are a major contributor to employment, wages generation and overall economic activity. In fact, this business sector is gaining increasing recognition for its potential to reduce poverty and contribute to equitable distribution of income (Storey, 1994; UNIDO, 2002). CSR in SMEs can also be very rewarding to a country when a CSR-oriented SME grows into a large enterprise and its continuing stance on local social issues may

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become increasingly influential. For example, large Chinese corporations such as Haier and Lenovo Group Ltd, which were initially SMEs, have now become internationally recognised large enterprises and active sponsors of community rebuilding, education promotion and poverty reduction projects. Although research on CSR of SMEs began to emerge in early 1990s, it has been particularly

scarce on SMEs in developing countries including China (Luken and Stares, 2005; Burton and Goldsby, 2007; Sweeney, 2007; Yu and Bell, 2007; Jamali, 2008; Mankelow, 2008; Morsing and Perrini, 2009; Hammann et al., 2009). It is important to gain a better understanding of the CSR orientation of SMEs located in China because they constitute a rapidly expanding group in the emerging Chinese market economy. There were about 8 million Chinese SMEs in the late 1990s and they have grown to more than 40 million entities in 2005, representing 99.6% of the total number of enterprises and accounting for more than 50% of the country's GDP. In 2008, they provided more than 75% of employment in the economy. Given appropriate incentives or encouragement for undertaking CSR, this growing sector can collectively generate significant and positive benefits for a range of stakeholders.

This paper aims to examine the relationships between CSR-oriented activities and financial performance in a sample of 208 SMEs in China. The underlying rationale of the study is that there are few conclusive empirical findings on the relationships between CSR activities and financial performance, particularly evidence from SMEs in developing countries. The data analysed in this paper was obtained from a survey on Chinese SMEs in 2004. Despite the consequent time lag in the publication of this paper, the authors strongly believe that their work contributes to the limited body of evidence on SMEs' CSR activities in China. This paper will firstly highlight the fluidity of a definition of CSRs for SMEs, before examining the CSR orientation of Chinese SMEs in terms of four factors: their engagement in support of labour skills development (as measured by training time spent by SME employees, and the proportion of SME employees attending training); as a source of employment opportunities (as measured by the number of equivalent full-time staff employed); the adoption of 'good practice' in their business management (as measured by the number of ISO9000 certifications or adoption of equivalent standards); and their investment in environmental sustainability (as measured by the proportion of sales revenue invested in environmental sustainability). The next section is devoted to a description of the methodology and variables utilised in the study and proposal of the research hypotheses on the relationships between SMEs' CSR orientation and their financial performance. This is followed by results and analyses of hypothesis testing. The last section presents an overall discussion including the effects of latest developments on SME's CSR orientations. The main conclusion is summarized in the last section.

## **There Is No "One-Size Fits All" Definition for CSR**

The literature reflects that there is no 'one-size fits all' definition of CSR. For example, van Marrewijk (2003) concluded in his study that there is no standard definition of CSR based on historical perspectives or philosophical analyses. Similarly, Whitehouse (2003) found no consensus among researchers, not only on the specific meanings of CSR but also on the practical methods for implementing CSR. Gond and Herrbach (2006) explained that despite considerable research efforts, determining and assessing CSR's contribution to business is not a clear-cut process, because of the absence of a reliable theoretical definition of CSR. While it has been a challenge to identify specific elements in a definition of CSR, it has been no less difficult to determine the breadth and scope of the obligations associated with CSR (Smith, 2003). The difficulty in precisely defining CSR has also been reinforced by Fassin (2008, p.367) who argues that CSR has evolved to a confused notion. Sweeney (2007, p.516) noted that some of the researchers who tried to determine the meaning of CSR have described it as "ambiguous", "subjective", "unclear", "amorphous", "highly intangible", and "fuzzy". Some studies (UNIDO, 2002; Van Marrewijk and Werre, 2003; Hill et al., 2007; Jamali, 2008; Welford et al., 2008) suggest that the meaning of CSR may vary according to the context (for example, location and industry) and the value systems of different organisations. For example, Welford's (2004) research highlights considerable differences in CSR among Asian countries, which vary according to national norms, values, economic development and culture. The attempt to obtain a clearer definition of CSR for SMEs has also been complicated by the fact that CSR evolves over time (Ullmann, 1985; Luetkenhorst, 2003; Gond and Herrbach, 2006; Welford et al., 2008). For example, a company's impact on society through its CSR can change as social standards evolve and science progresses to the extent that firms are expected to respond to the changing beliefs and values of society, which may ultimately be transformed into ethical and moral obligations for these firms. Fast

food companies, for instance, are increasingly subjected to unprecedented pressure to offer nutritious and low cholesterol alternatives in their menu.

Although there is no standard definition of the concept, the existing literature offers a very general description of what constitutes CSR. CSR is largely understood as a range of voluntary initiatives, beyond legal and contractual requirements, which, if undertaken effectively, should eventually benefit the workforce, their families and the local community, and ultimately improve the overall welfare of the community and contribute to economic development (Davis, 1973; Jones, 1980; European Commission, 2001; McWilliams and Siegel, 2001). In China, employee training, job creation, product and service quality, and environmental sustainability have been commonly associated with CSR. These activities were confirmed as primary CSR engagement in a survey conducted in 2008 involving 1593 respondents (Qiao, 2009). Forty percent of these respondents were senior managers of large enterprises, 30% were senior managers of SMEs, 10% were academics, 10% government officials, and 10% CSR experts. "Environmental protection and resource conservation" attracts the most votes (97%) from these respondents as an important CSR activity, followed by "high product and service quality" (95%), "employee training" (85%), "job creation" (85%). These activities are related to the internal functions of an enterprise and can lead to strong commitments if they generate positive benefits because if profit-oriented SMEs can see specific practices that benefit profitability and business improvement, they tend to be more likely to become involved since these are stronger reasons or incentives for firms to justify their CSR investments. In this way, CSR is integrated into the way companies manage their business processes and may produce benefits for stakeholders. For example, a sound business system can benefit both society and a company's own competitiveness through quality product offering and may generate intangible benefits for the company such as improved reputation for quality or reliability, allowing the company to generate and maintain its profit growth (Castka et al. 2004). It is believed that a firm that has a strong CSR orientation will invest in creating continual superior value for its customers (Porter and Kramer, 2006). However, a negative correlation with a firm's financial performance can become a serious cause for concern as managers will be cautious in supporting CSR.

## Methodology and Variables

This paper focuses on the CSR orientation of Chinese SMEs in the areas of employee empowerment, societal impact, environmental impact, and quality compliance. Median values will be used as descriptive statistics for profiling the CSR orientation of the 208 SMEs. More detail re the sample, selection, and responses required. The median is used instead of the mean because the variables are not distributed normally due to extreme values in the data set. The median is the middle value in a set of data, where 50% of the values are less than or equal to the median, and 50% of the values are more than or equal to the median. The median, unlike the mean, is not affected by extreme values, and is a fairer representation of a set of numbers. Pearson correlation analysis is used to address the hypotheses and investigate the relationships between CSR-oriented activities in SMEs and their financial performance. Profitability and sales revenue are used as measures of financial performance to determine whether financial performance has a positive relationship with CSR-oriented activities. The presumption is that CSR can improve a firm's competitiveness, resulting in increased profitability and/or sales.

### 1. Employee training

In China, labour quality and skills are still relatively low, and the underdevelopment of its human resources is the biggest restraint on Chinese economic development. For example, a study on Chinese enterprises by Venter (2003) found skill shortage to be a pressing issue in this emerging market economy. Her survey revealed that 46% of organisations found it difficult to fill managerial positions and 30% had the same problem with technical positions. The Chinese education system is still incapable of supplying the vital skills and talents required by businesses to keep up with a dynamic market environment. China's move to privatize and reform its various state run businesses since the early 1980s have introduced changes to the lifetime employment system that were operating for decades. Workers in the post-reform competitive Chinese labour market now regard their own career

growth and development as an important element in their work life, which they see it as employers' responsibility in developing and improving their job skills (Huo and Si, 2001). Good labour practices undertaken by Chinese SME owner-managers, such as providing training and development opportunities to their workforce, is considered as evidence of CSR because these can lead to improvement in labour standards, not only of the labour-intensive enterprise, but also of the national workforce. If all enterprises were to contribute in this way, the nation's skills base would be significantly enhanced, with the responsibility being shared equitably across all types of enterprises. In addition, the core business activities of a business can have a positive impact on poverty through the creation of employment. Training is all the more important, given that SMEs represent at least 99% of all businesses operating in China. Their aggregate impact on employment has been assessed by Zhou (2005) to be profound, in the ratio of 14 SME employees to each employee hired by a large corporation (14:1). Although it has been generally assumed that human resources training can help firms develop new competencies and capabilities, and improve competitiveness, this assumption has been largely based on qualitative studies (Patton et al., 2000; De Kok, 2002; Bryan, 2006). Empirical evidence on the relationship between training and company performance has been inconclusive. For example, the Wyncarczyk et al. (1993) study on SMEs in the UK found an insignificant relationship between training and company performance. Cosh, et al. (1998), on the other hand, found a positive but insignificant relationship between training and firm survival. However, Jones' (2004) identified a statistically significant positive relationship between training and performance in Australian Manufacturing. Overall, previous studies, including the aforementioned studies on the effectiveness of training programmes for SMEs, have focused mainly on Western nations (Huang, 2001). This paper will test two research hypotheses relating to the relationships between training as a CSR orientation and company financial performance on the chosen sample of 208 Chinese SMEs:

*H1: Training time spent by a SME employee has a significant positive relationship with company financial performance.*

*H2: The proportion of SME employees attending training has a significant positive relationship with company financial performance.*

## **2. Job Creation**

SMEs constitute an important source of job creation because they historically provide the majority of new job growth in a community, which itself constitutes a significant contribution to economic development (Burton and Goldsby, 2007). The SMEs have a great potential to play a key role in national and social development because the job opportunities they create can reduce or alleviate poverty. This CSR role in job creation can also create goodwill and improve relations with local governments and other stakeholders, potentially improving the image of an organization and demonstrating its social commitment to stakeholders (Davis, 1973). The Chinese government has been paying close attention to the issue of employment in recent years. For example, on 1<sup>st</sup> January 2008 the government enacted the 'People's Republic of China Employment Promotion Law', which encourages financial institutions to provide monetary support and local governments to provide tax concessions to SMEs, because these enterprises can become significant sources of job creation. However, the relationship between this job creation role and company financial performance remains unknown, and this paper examines whether this role has generated positive financial outcomes for the SMEs included in the 2004 sample. Therefore, we propose to test the third hypothesis:

*H3: The number of full-time jobs created by SMEs has a significant positive relationship with company financial performance.*

## **3. ISO9000**

It has been argued that a sound business system can benefit not only society but also a company's own competitiveness through quality product offering, because being socially responsible has been associated with positional advantage (Porter and Kramer, 2006). ISO9000 is an international quality assurance standard, and is one of the most well-known and widely implemented set of criteria voluntarily adopted by quality-oriented companies to achieve a sound business system. It has become

an important indicator of voluntary business commitment to quality assurance. In the main, ISO9000 standards appear to provide a baseline and an improvement mechanism for organisations aiming to improve company performance by way of improving product, service and organisational quality (Wilson, 1997). There may be economies of scope in the provision of CSR, or cost savings that arise for CSR incorporated systems and procedures such as ISO (International Standard Organisation) accreditation. However, there has been limited literature and research concerning quality standards in the context of SMEs because research on the use of ISO9000 tends to focus on larger companies (Boulter and Bendell, 2002; Mulhaney et al., 2004). Because ISO9000 is one of the most popular voluntarily adopted basic standards, the survey tracks the certification of this standard, or an equivalent, as a proxy for socially responsible commitment to quality from SMEs. Hence, the fourth hypothesis postulated in this paper is:

*H4: The implementation of accredited international standard ISO9000, or an equivalent, has a significant positive relationship with company financial performance.*

#### **4. Investing for Environmental Sustainability**

Although SMEs play an important role in the Chinese economy, collectively they are responsible for much of the nation's industrial pollution. For example, it was reported in 2003 that SMEs discharged about 50% of total emissions of industrial pollutants (CCICED, 2003). According to the report by CCICED (2003), the inability of SMEs to respond to the increasingly important environmental issues in the market has been due to their general lack of available financial and time resources. This has been a common constraint among SMEs in their efforts to develop and implement environmental management practices (Seidel et al., 2008). However, the dominance of these SMEs makes them significant potential contributors to global environmental sustainability, and potential adopters, if given proper incentives, of business system frameworks that incorporate proactive environmental practices. Spicer (1978) found that better pollution performance was associated with higher profitability and lower risk, but this is more obvious in larger firms. This positive attribute is also echoed by The Government Office for London (2009) which advocated that sound environmental management practices will deliver financial benefits (such as profitability) and competitive advantage for businesses, as well as benefiting society. This is encouraging because presumably SMEs will voluntarily adopt environmental activities if such engagements add value to their core business (Studer et al., 2006).

ISO14000 was developed under the same philosophy of ISO9000 and is widely regarded as an example of best practice in environmental management. However, the incidence of ISO14000 certification obtained by Chinese SMEs has been considerably lower than the certification rate for ISO9000. In 2004, the certification rate for ISO14000 in all types of enterprises was less than 10% of the ISO9000 certification rate in China (ISO, 2007). Although ISO14000 certification had increased by 2007, it was still below the ISO9000 certification rate (14.5% of the latter). In addition, this standard tends to be adopted primarily by larger enterprises. SMEs have commented that these environmental management standards are costly and time-consuming to implement and of questionable effectiveness. However, some of these companies may have adopted inhouse environment management systems which are not necessarily ISO14000 certified. In this context, the survey obtained data from SMEs on the percentage of revenue invested in integrating environmental sustainability, rather than the adoption of ISO14000 per se, because the key indicator is whether an organisation internalises environmental considerations into its operations and has mechanisms in place to prevent and control environmental impacts. The percentage of revenue invested in integrating environmental sustainability in company systems (such as implementing environmentally friendly business practices, or producing environmentally friendly products or services) is used as a proxy to measure the uptake of environmental practices in SMEs. Hence, this paper's fifth hypothesis relating to environmental sustainability and financial performance is:

*H5: Environmental sustainability investment has a significant positive relationship with company financial performance.*

## CSR Orientation of SMEs

Table 1, below, presents the median as a measure of central tendency of CSR-oriented activities in a sample of 208 SMEs in regard to training time spent by an SME employee (number of days), percentage of SME employees attending training, employment provided by company ( number of full-time equivalent employees), and percentage of sales revenues invested for environmental sustainability. Figures 1, 2, 3 and 4 show that the distribution of the data is skewed or not normally distributed, which justifies the use of the median instead of the mean for profiling CSR-oriented activities in these SMEs.

**Table 1: Descriptive Statistics.**

CSR-oriented activities in SMEs	Median
Training time spent by each SME employee (days)	30 days
Proportion of employees attending training (percentage)	75%
Employment provided by SMEs (number of full-time equivalent employees per SME)	26 employees
Proportion of sales revenues invested for environmental sustainability (percentage)	3%

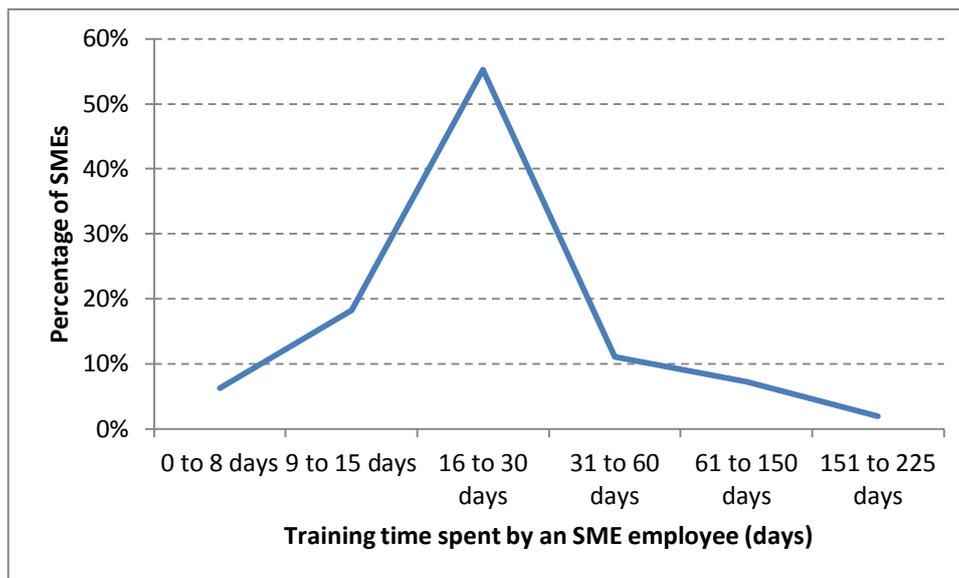
### 1. Employee training

According to Table 1, the median training time spent by an SME employee in 2004 was 1 month. In addition, the frequently occurring training time duration (mode) in this sample is 1 month. This training duration spent by an SME employee is significantly higher than enterprises, including large enterprises, in other countries. For example, the average training time spent by employees in all types of enterprises in Australia was 5.1 days in 2002-2003; 3.7 days in 2003-2004; 4.8 days in 2004-2005; and 6.2 days in 2005-2006 (ABS, 2003; 2004; 2005). In Ireland, the average number of days of training per employee was 5.61 days in 2001 and 5.35 days in 2003 (Heraty and Collins, 2006). De Kok's (2002) study on Dutch firms with 40 to 150 employees in Netherlands found an average of 2.5 and 2.7 training days respectively in 1990 and 1993<sup>1</sup>. Chinese SMEs' median training time in 2004 is significantly higher than these developed countries, possibly because of the latter's comparatively more skilled labour force. The higher average training time suggests that Chinese SMEs are taking a positive stance by investing for a skilled labour base.

Of the 208 SMEs surveyed, two companies (1%) did not provide or support any training for their employees. Although slightly more than half of SMEs (55.3%) were found to provide or support an average of 30 days or less in training time for each employee, there was a general gradual decrease in the number of SMEs willing to provide or support more than 2 months of training time (refer to Table 2 and Figure 1).

**Table 2: Training Time Spent by an SME' Employee (Days)**

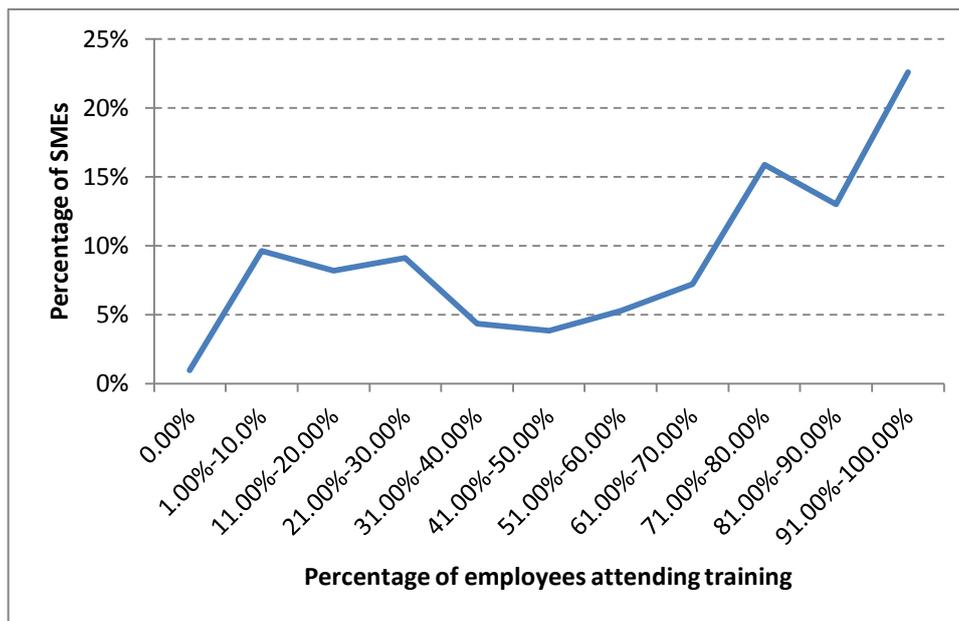
Training time (days)	Frequency	Relative frequency	Cumulative frequency
0 to 8 days	13	6.25%	6.25%
9 to 15 days	38	18.27%	24.52%
16 to 30 days	115	55.29%	79.81%
31 to 60 days	23	11.06%	90.87%
61 to 150 days	15	7.21%	98.08%
151 to 225 days	4	1.92%	100.00%
	208	100.00%	

**Figure 1: Training Time Spent by an SME Employee (Days).**

According to Table 1, the median proportion of employees in SMEs who attended training in 2004 was 75%. From the survey, approximately 14% of SMEs responded that all their staff had gone through a training programme at some point of time during the year. Table 3 and Figure 2 also reflect a general increase in the number of SMEs with more than 50% of employees who underwent training in 2004. These data indicate that although SMEs increasingly provide or support training for more than 50% of their employees, a training duration of more than two months is seldom supported by these companies.

**Table 3: Proportion of Employees Attending Training**

Proportion of employee attending training (percentage)	Frequency	Relative frequency	Cumulative frequency
0.00%	2	0.96%	0.96%
1.00%-10.0%	20	9.62%	10.58%
11.00%-20.00%	17	8.17%	18.75%
21.00%-30.00%	19	9.13%	27.88%
31.00%-40.00%	9	4.33%	32.21%
41.00%-50.00%	8	3.85%	36.06%
51.00%-60.00%	11	5.29%	41.35%
61.00%-70.00%	15	7.21%	48.56%
71.00%-80.00%	33	15.87%	64.42%
81.00%-90.00%	27	12.98%	77.40%
91.00%-100.00%	47	22.60%	100.00%
	208	100.00%	

**Figure 2: Proportion of Employees in SMEs Attending Training**

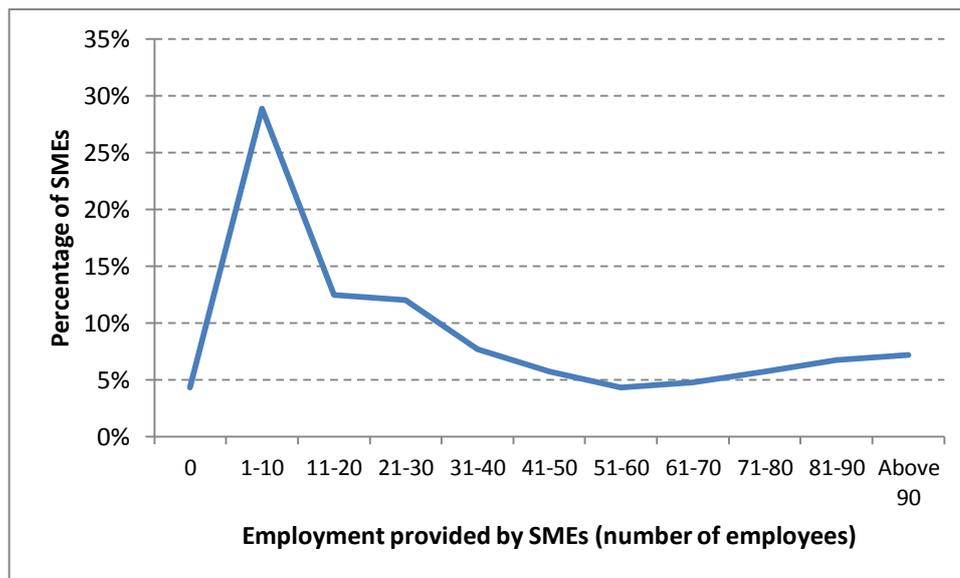
## 2. Job Creation

Table 1 shows that the median number of new full-time jobs or equivalent positions created by SMEs in 2004 was 26. About 29% of SMEs employed between one and ten new full-time or equivalent staff in 2004 (refer to Table 4 and Figure 3). However, 4.3% did not employ any new staff in 2004, while 7.2% employed more than 90 new staff in the same year. Slightly more than half of SMEs surveyed (57.7%) employed 30 or less full-time employees or equivalent in 2004.

**Table 4: Employment Provided by SMEs (Number of Employees)**

Employment provided by SMEs (number of employees)	Frequency	Relative frequency	Cumulative frequency
0	9	4.33%	4.33%
1-10	60	28.85%	33.17%
11-20	26	12.50%	45.67%
21-30	25	12.02%	57.69%
31-40	16	7.69%	65.38%
41-50	12	5.77%	71.15%
51-60	9	4.33%	75.48%
61-70	10	4.81%	80.29%
71-80	12	5.77%	86.06%
81-90	14	6.73%	92.79%
Above 90	15	7.21%	100.00%
	208	100.00%	

**Figure 3: Employment Provided by SMEs (Number of Full-Time Equivalent Employees)**



### 3. ISO9000

As mentioned earlier, SME survey respondents were asked whether their organisations had obtained accredited international standards certification for systems improvement initiatives such as the basic ISO9000. The rationale was to determine whether these Chinese businesses had integrated the CSR concept of ‘good practice’ into their business management. Table 5 shows that 29.3% of Chinese SMEs had adopted ISO9000 while 70.7% had not.

**Table 5: Proportion of SMEs With and Without ISO9000 Certification**

	Frequency	Relative frequency	Cumulative frequency
SMEs with ISO9000 certification	61	29.3%	29.3%
SMEs without ISO9000 certification	147	70.7%	100.0%
Total	208	100.0%	

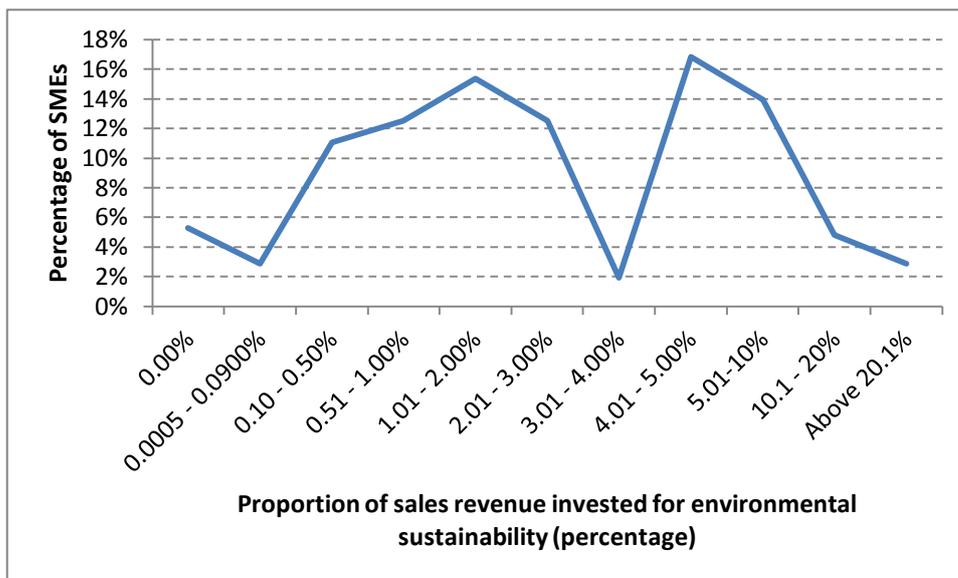
### 4. Investing for Environmental Sustainability

Table 1 shows that the median proportion of sales revenues invested for environmental sustainability was 3%. The highest investment was 33% from an SME in the construction industry. As shown in Table 6 and Figure 4, 68% of SMEs contributed more than 1% of their sales revenues towards the cause of environmental sustainability, while 7.69% contributed more than 5%. These measures are significantly higher than the aggregate contribution from Australian manufacturing industry, which was 0.26% of sales revenue in 2001-2002 (ABS, 2003; 2005). There were differences in the propensity towards environmental sustainability among the different industrial sectors. The rate of investment from the hotel and restaurant industry was 10%, while construction’s was 6.93%, manufacturing 4.42%, and information transmission, computer services and software 2.3%.

**Table 6: Proportion of Sales Revenue Invested for Environmental Sustainability (Percentage)**

Proportion of sales revenue invested for environmental sustainability (percentage)	Frequency	Relative frequency	Cumulative frequency
0.00%	11	5.29%	5.29%
0.0005 - 0.0900%	6	2.88%	8.17%
0.10 - 0.50%	23	11.06%	19.23%
0.51 - 1.00%	26	12.50%	31.73%
1.01 - 2.00%	32	15.38%	47.12%
2.01 - 3.00%	26	12.50%	59.62%
3.01 - 4.00%	4	1.92%	61.54%
4.01 - 5.00%	35	16.83%	78.37%
5.01-10%	29	13.94%	92.31%
10.1 - 20%	10	4.81%	97.12%
Above 20.1%	6	2.88%	100.00%
	208	100.00%	

**Figure 4: Proportion of Sales Revenue (Percentage) Invested for Environmental Sustainability.**



## Results of Hypothesis Tests

This section shows the hypothesis test results on the relationships between SMEs' CSR orientation and their financial performance.

**Table 7: Pearson's Correlation Results**

CSR orientation	Sales revenue	Profit
Training time spent by an SME employee (days)	0.031	0.013
Proportion of employees attending training (percentage)	-0.047	0.034
Employment provided by SMEs (number of full-time equivalent employees)	0.05	-0.063
Proportion of sales revenues invested for environmental sustainability (percentage)	0.05	0.016
SMEs with ISO9000 certification	0.203***	0.193***

\*\*\*1% significance, \*\*5% significance, \*10% significance

### 1. Employee training

*H1: Training time spent by an SME employee has a significant positive relationship with company financial performance.*

*H2: The proportion of SME employees attending training has a significant positive relationship with company financial performance.*

Overall, the sample of 208 Chinese SMEs did not suggest a significant positive relationship between either training duration or proportion of SME employees attending training and the respective SMEs' financial performance measures (profitability and sales revenue), as indicated in Table 7. Although the Chinese SMEs supported a higher training duration per employee than enterprises in Australia, Ireland and Netherland, as reported earlier in this paper, these Chinese SMEs have lamented the pressure in having to maintain a balance between their firm's sustainability in an increasingly fiercely competitive market, and their expenditure on training programs for staff development. Because training programs tend not to generate immediate benefits, these enterprises find it difficult to justify such expenditure at the expense of profit. In addition, these SMEs are also fearful that their trained staff will be poached by competitors in markets where skilled labour is in short supply. Based on the above comments from Chinese SMEs, it appears that these enterprises are not investing training resources sufficiently to create a significant positive impact on company financial performance, despite a high training duration. If this is the case, the average training duration of SME employees or the proportion of SME employees undergoing training would be even higher if these enterprises had more resources and adopted a longer term and broader view of training benefits for their future operations and the overall economy. As such, this aspect of the findings suggests the possibility of hypothesis test H1 revealing a different relationship between the training variable and the company financial performance, if these SMEs were able to afford the optimal investment.

### 2. Job Creation

*H3: The number of full-time jobs created by SMEs has a significant positive relationship with company financial performance.*

The survey of 208 Chinese SMEs did not exhibit a statistically significant relationship between the number of jobs created by SMEs, and the performance indicators of profitability and sales revenue. Chinese SMEs are generally labour-intensive enterprises and hire low-cost labour for their production processes. They also possess antiquated production methods with low technology intensity and have little financial strength. Despite SMEs being a major employment force in the economy, their viability as long term employers and stable engines of job creation in China is dubious. Moreover, their financial predicament during the current global financial crisis has revealed their vulnerability. For example, it has been reported that 40% of Chinese SMEs have already closed down their businesses, with another 40% struggling to stay afloat financially during this period (China Commercial

Intelligence Network, 2009). Only 20% of the SMEs were reported to be unaffected by this crisis. One of the reasons behind their financial weakness is that Chinese SMEs are generally faced with high borrowing barriers when seeking financial support from lending institutions. This is because Chinese SMEs tend to have few or no quality assets for collateral and a bad history of defaulting on loan repayments. For example, a summary of loan performance obtained at the end of 2008 revealed that 11.6% of loans granted to small enterprises in China had degenerated into bad debts, which far exceeded the national average bad debt of 2% of loans awarded to all types of enterprises (Yi, 2009). In some regions, the rate of bad debts incurred by SMEs runs as high as 20%. Financing difficulties have been an age-old issue for Chinese SMEs, despite the incentives given by government to lending institutions to encourage financial support for SMEs. Statistical data compiled from major banking institutions in the first quarter of 2008 revealed financial bottlenecks in SMEs which had serious ramifications for the future viability of these enterprises. The proportion of loans granted by the commercial banks to SMEs in the first quarter of 2008 constituted only 1.5% of all loans granted and was 10% less than in the same period of the previous year, due to the tightening of credit during the global financial crisis (news.163.com, 2008). This means that the Chinese SMEs are facing a tougher financial challenge than ever before, and that their viability as long-term employers of the country's population is being put at stake.

### 3. ISO9000

*H4: The implementation of accredited international standard ISO9000 or equivalent has a significant positive relationship with company financial performance.*

Overall, the sample of 208 Chinese SMEs evinced significant positive relationships (at 1% significance) between the implementation of accredited international standard ISO9000 (or equivalent standards) and both profitability and sales revenue. SMEs in China accounted for 68% of all Chinese exports in 2004 and their exports are twice that of their US counterparts and five times their European counterparts (Hall, 2007). The Chinese SMEs have become acutely aware of the importance of producing quality products and services for the international marketplace, as a result of their active trading with developed countries over the years (Wang, 2001; Hung and Gong, 2007; An, 2008; Liang, 2009). Their main export markets are the USA, European Union, Japan and North America, all of which maintain stringent quality requirements on imported products. As a result, the adoption of quality assurance standards in the SMEs' production processes has been driven by importers from these developed countries.

### 4. Investing for Environmental Sustainability

*H5: Environmental sustainability investment has a significant positive relationship on company financial performance.*

There is no statistically significant positive relationship between environmental sustainability investment and SMEs' financial performance at the aggregate level. Although 68% of SMEs in the sample invested at least 1% of their sales revenue on environmental sustainability, this appears to be not enough to make a significant impact on their financial performance. Overall, China is not operating at an environmentally efficient level. Its energy utilization rate is 33%, its industrial water recycling rate 55%, and its mineral conservation rate (a measure of the reduction of loss and waste of non-renewable resources) 30%, which are 10%, 25% and 20% lower respectively than the standards achieved by the developed countries (Yao, 2008). Although the median proportion of sales revenues (3%) invested by the Chinese SMEs is higher than the counterpart contribution from Australian manufacturing industry (0.26%), the impact of the Chinese investment appears to be inadequate for China to close its environmental sustainability gap with the developed countries.

SMEs in China generally rely on pricing strategy to attract demand for their products and services, rather than non-pricing strategies which emphasise innovative and quality products and services to engage customers. They lack the ability to be innovative because of their inexperience, and because of the limited availability of resources for research and development activities. In a survey conducted by UPS Asia Business Monitor (2009), 81% of Chinese SMEs admitted that the lack of innovation is the

major obstacle to their competitiveness in the marketplace. In addition, 78% of SMEs indicated that the lack of access to business financing hinders their business growth. Due to a persistent lack of financial support, these enterprises have to compete on pricing. However, their attempts to achieve a production cost that supports a low pricing strategy frequently means that they are unable to afford the integration of certain voluntary 'ancillary' processes into their operations. For example, integrating environmental sustainability processes is considered an ancillary activity and an unnecessary cost burden by struggling Chinese businesses (Ren and Yan, 2008).

If SMEs bring down their implicit costs by acting in an environmentally irresponsible manner by reducing the cost of pollution and protection, they will experience higher explicit costs and their competitive platform will be eroded. For example, Cheng et al. (2007) found that Chinese enterprises have to bear an extra export certification cost of between 1 million and 2 million yuan in order to comply with the new European Union (EU) Regulation on the Registration, Evaluation, Authorisation and Restriction of Chemicals (known as REACH) which was introduced by the EU to ensure a high level of protection for human health and the environment. If proper environmental protection measures are in place in the Chinese economy, the savings of this superfluous cost would alleviate the financial pressure on exporting enterprises, particularly the financially strapped SMEs.

## Discussion

The hypothesis test results reveal no significant relationship between SMEs' profitability and training time per SME employee, or the proportion of SME employees attended training. The same insignificant relationships exist between sales revenue and each of these training variables. While the descriptive measures in Table 1 reveal a healthy picture of training support (in terms of long training duration and high proportion of employees undertaking training) in SMEs, there is however no statistically significant positive link between either training variable and the posited financial performance measures. The authors caution against an immediate conclusion of a null relationship between these variables, because failure to provide adequate training can retard the development of SMEs. Information on the training duration and the proportion of staff undertaking training is useful for understanding the CSR profile of SMEs' commitment to training and development. However, further research needs to be conducted on the manner, approach and content of the training, and the applicable relevance of training for determining impact on the financial performance of SMEs.

There is also no significant relationship between profitability or sales revenue and job creation by SMEs, and likewise between financial performance and environmental sustainability investment by these firms. Overall, the relevant Pearson correlation coefficients suggest insignificant relationships between the three aforementioned CSR-oriented attributes and financial performance for the sample of 208 Chinese SMEs. However, there is a significant positive relationship between implementation of accredited international standard ISO9000, or equivalent standards, and financial performance in SMEs. The implementation of quality assurance standards in SMEs' production processes was mainly driven by importers from developed countries, which tend to impose stringent quality requirements on imported products. Informal feedback and comments obtained during the survey period suggest that the Chinese SMEs' roles in training, employment, quality assurance standards and environmental responsibility were primarily carried out as part of their core business function rather than for any CSR purposes. With the exception of quality assurance standards (represented by the implementation of accredited international standard ISO9000 or equivalent standards), the insignificant relationships between the 3 variables and financial performance may be due either to an insufficient level of commitment to these activities or to the fact that the benefits associated with these activities have yet to come to fruition.

The statistically significant positive relationship between the implementation of accredited international standard ISO9000, or equivalent standards, and the financial performance of the Chinese SMEs implies that CSR-oriented activities can be driven by market forces or customer demand. This relationship indicates that Chinese SMEs are becoming increasingly integrated into the global economy and will find social and environmental standards increasingly becoming a precondition for doing business with companies in developed countries. Although the Chinese SMEs initially adopted ISO9000 certification primarily for economic reasons rather than those of CSR, the authors still regard this

as a positive start towards socially responsible behaviour. The influence generated by customers within the value chain can be a powerful tool in developing the SMEs' perspective on quality assurance. The attitude towards product and service quality has now developed to a broader level that embraces supply chain efficiency. For example, a survey reported by the UPS Asia Business Monitor (2009) reveals that 93% of Chinese SMEs regarded supply chain efficiency as a critical success factor for their businesses. One quarter of these enterprises believe that supply chain efficiency can bring about reductions in capital outlay, while 23% believe it can help improve quality assurance for their products and 18% believe it can be used to forecast demand. This demonstrates that market conditions and competition pressure can lead to a change in attitude among SMEs in their quest to become viable suppliers in global trading.

Overall, Chinese SMEs tend to have a lower level of aggregate commitment to CSR in their core functions and business activities because of financial and resources constraints. Like many of their counterparts in emerging economies, the Chinese SMEs have undergone a relatively short and brisk period of development and are still experiencing rapid changes and demands from the market. For instance, their management philosophy, style, industrial structure, product mix and market orientation are still grappling with the demands of market competition and reform (Chen, 2006). Generally, they face challenges in the form of an unskilled labour force, low levels of management skills, weak innovative ability and difficulties in obtaining finance (Ren 2003; Dong, 2007; UNDP, 2005; Wang, 2008). These challenges can impede SMEs' ability to undertake CSR-oriented activities to a level where a positive impact on financial performance could be generated. Their commitment is expected to weaken if financial and resources constraints become tighter. A worldwide survey conducted by UPS Asia Business Monitor (2009) on 150 Chinese SMEs found that 64% of them plan to diversify their business or develop new revenue sources to combat challenges generated by the global financial crisis. Fifty-nine per cent of enterprises in the same group responded that they will reduce expenditure spending while 55% will tighten their cash management. Given the financial challenges, the lack of expertise and the skilled labour shortage in SMEs, achieving competitive advantage through innovation in products and services as well as developing new markets and building new business models can be very difficult. Cost-cutting strategies are a more accessible option for these enterprises and are likely to involve reduced spending on activities that may generate socio-economic externalities in the economy but not immediate economic impact for the businesses. It will be no surprise if profits prevail over social responsibility. A commonly targeted area for cost-cutting would be environment protection and control measures, because they are not generally viewed by Chinese SMEs as profit-enhancing processes. This view is also reinforced by the fact that SMEs lack the experience and functional expertise to integrate environmental aspects into their operations in order to enhance financial performance. However, if SMEs do not address environmental issues in their production and management operations, the cost repercussions are likely to be magnified in the long run.

CSR issues generally tend to be of low priority for SMEs if they are not required to comply with legislation, particularly if they view such undertakings as costly to integrate and unlikely to generate immediate or foreseeable returns. If public pressure is strong enough, it can replace regulatory imposition on businesses in the uptake of CSR and the extent of CSR engagement. However, this requires businesses to be at a mature level of development for the actualisation of socially responsible behaviour, and also financially empowered to move towards integrating social values into their decision-making processes.

Williamson et al. (2006) advocated the development and imposition of regulatory structures to generate pressure on SMEs to increase their uptake of environmental and social practices. In this way, environmental and social responsibility can be shared equitably across all types of enterprises. However, imposing regulatory compliance needs careful cost-benefit analysis because it can increase firms' non-productive overheads (Kapstein, 2001). In addition, regulation is costly to business and restricts the flexibility of decision-making. If CSR legislation is to shape the activities of Chinese SMEs, a consultative process involving interaction and negotiation between policy makers and these firms will be essential. Ideally, such a policy initiative would be more likely to yield mutually agreed socially and environmentally beneficial outcomes which have taken into account the difficulties of SMEs in taking on CSR. However, it will be difficult to mandatorily impose CSR on Chinese SMEs.

Legislative power has recently been used to influence CSR uptake in Chinese enterprises but its effect has been largely confined to persuasion and encouragement. For example, the guidelines issued by the State-owned Assets Supervision and Administration Commission of the State Council (SASAC) in early 2008 encouraged its large, state-owned enterprises to actively take on CSR. On January 1, 2006, the Company Law incorporated a CSR edict for the first time in its legislative history but it merely encouraged Chinese enterprises to undertake social responsibility as part of their duty.

## Conclusion

This paper has examined the CSR orientation of Chinese SMEs based on their internal functions, including training, job creation, quality assurance and environmental sustainability. Despite SMEs' participation and investment in training, job creation, and environmental sustainability, their involvement and action have not produced a statistically significant positive relationship with their financial performance (as measured by profitability and sales revenue). The only CSR-oriented activity that registered a statistically significant positive impact on financial performance was quality assurance (as measured by the implementation of accredited international standard ISO9000 or equivalent standards). The uptake of quality assurance by these SMEs was largely attributed to their involvement in global trade, whereby market and competition conditions pressurised these businesses to gain certification for their internal processes and participation in the international supply chain.

The obstacles faced by the Chinese SMEs (which include a lack of access to business financing, a lack of innovative capability, and an inexperienced and unskilled management and labour force) have resulted in these CSR-oriented activities being undertaken primarily for economic reasons rather than for their social value. There is a risk that the statistically significant positive relationship between quality assurance and financial performance may be eroded if these obstacles are not resolved. The lag in CSR uptake in the Chinese economy may aggravate the costs involved in the monitoring and certification of quality standards, so that it becomes a major burden to struggling SMEs and eventually erodes their share of the international market. This paper has also suggested that using legislative powers to enforce the uptake of CSR-oriented activities in enterprises must take into consideration the inherent difficulties faced by SMEs.

## Endnote

1. Some of these Dutch firms are not considered SMEs because SMEs in Netherlands are defined as enterprises with less than 100 employees.

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