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# Relationship between ethical leadership and value creation

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**The theme of value creation, being the source of this research, has received increased interest in the field of management science, and hence has become the new creed of managers. We have proposed that ethical behavior of managers influences the policy of value creation. In particular, we test the four cardinal virtues of the manager (justice, prudence, strength and moderation) that influence development and growth of the company. This paper attempts to make an inventory of ethical problems in a country's development and clarifies their role in the development of firms. We used a sample of Tunisian companies for a period of 2003 to 2011.**

**Key words:** Ethics, managers, behavior, creation of value.

## INTRODUCTION

In companies, value creation is the best protection against various threats from global markets. It is the first objective of the finance function. This necessity has led managers and business leaders to feel an urgent need to develop a sustainable leadership excellence, combining business and ethics. It includes developing the overall efficiency of leaders to generate more "results with less effort, more quality with less stress ..." Ways out of the dynamics of short-term to move towards a business strategy firmly focus on innovation and value creation

To find these results, we will focus on questioning the ethics of leadership in creating value. Note that ethics emerge from the Greek word "ethos" which means customs, ways of acting; "morality" comes from the Latin "mores" which means character. In this etymological point of view, Gauthier (2000) indicates that there is no difference between ethics and morality, that the two concepts refer the relationship of the individual with law, according to his own tradition, cultural references and compliance with the institutions of the society in which he lives.

As part of verification of this question, we first try to understand the causes of such behavior of leaders. We then show that the managerial ethic is a true corporate social responsibility, and why it will become increasingly important in the context of the emergence of the new "knowledge economy". Finally, we will make some suggestions to help improve the "quality ethic" of managerial practices in the business to achieve the overall development of the company.

### Theoretical development

Deregulation of the banking sector, the financial crisis of 2008 to 2009, the emergence of new financial and

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accounting techniques aim to hide the actual level of indebtedness to the various stakeholders, the explosion of managers' salaries and some easing ethics. All these deviations become crises of confidence of investors, creditors, employees, and corporate bankruptcies. Out of this scandal, it is necessary to focus on business and government practices, in particular, ethical behavior.

Managers are considered as one of the essential foundations of corporate success (Gohen, 2006). Indeed, they are knowledgeable, skilled and have an overall view on the enterprise market, which they share with all the owners and staff of the company in order to stimulate and encourage them to focus their efforts for the benefit of the company, globally. The manager is always present when questions or problems arise within the company. He adopts appropriate strategies, in terms of communication and explanation, to reduce conflicts and problems of uncertainty. The manager plays an important role in creating value through his ability to join the teams on a project to create value. Specifically, he knows how to convey his core values to all parts of the business and examines ethical standards in their decision making.

Only the ethic of responsibility has a place in the management of the company. It is the "understanding of the consequence of an act on all the actors and factors related to the act, and the will to direct his actions towards the goals of the partners in these same actors and factors." More specifically, it brings certain values forming a structural framework mode of action.

The choice of ethical leadership and vision in this field must be set in the sense that the latter feels that it opens a collective goal and a common vision. The sense of direction will only be a source of pride and personal gain. It will therefore be obliged to publish a code of ethics that aims to facilitate understanding and equality for employees, partners, suppliers and shareholders. This will lead to a liability at all levels, to share individual and collective demands and to support and reward efforts. In fact, ethic involves behavior, socially inclusive, which must lead to the realization of profit, whatever the conditions, forgetting morality; but with the inclusion of a responsibility vis-à-vis employees, customers and the environment through a long-term commitment which aims to achieve a new social responsibility (SR).

The concept of social responsibility (CSR) integrates business to its stakeholders and social, environmental and economic activity. Practically, CSR can cover the overall quality of supply chains and outsourcing, research and cooperative long-term relationships with suppliers, taking into account the expectations of customers (via quality procedures, hotlines, information services and customer satisfaction surveys), the welfare of employees, management quality, work environment; it encourages autonomy, training, remuneration and the ecological footprint of the company. SRC appears as the declination of the company for sustainable development concepts that integrate the three pillars of environmental, social and economic activities:

1. It contributes directly to economic development through investment,
2. Through the working conditions offered to employees, it helps to create or reduce social inequalities,
3. By consuming natural resources, producing waste and generating pollution, its activities more or less deeply affect the environment.

Management skills and the emergence of a knowledge economy are two key sources of value. Specifically, the real assets and sources of value added business skills are the talents and energies. Specifically, the process of value creation depends on quality leaders. But it is itself related to ethical practices. It is embodied in the means and conditions to promote new visions of leadership and organization.

Ethics form the concern of various governments and professional organizations. It has gained a great importance in the private and public companies for achieving the best results. The social responsibility has influence in terms of value creation and performance (Garric et al., 2007; Valentine and Fleischman, 2008). These authors focus on the ethical behavior of managers in the process of value. We know that the determinants of ethical behavior are social norms, personal goals, business, law and values of other individuals with whom we interact.

However, unethical behavior of leaders is largely related to the pressure of competition. This is the stress caused by the quota, the pay system or the competition that attacks morality. Thus, if the leadership has a strong ethical sensitivity, it will encourage the formalization of an ethics policy. The introduction of ethics in business depends, in large part, to the commitment of the leader and his value system. Samuel (1999) shows that the factors that influence leaders in their decision to formalize ethics are personal philosophy, career and training (Figure 1).

In total, ethical behavior is required today, a key factor of survival and development of the company. It is a competitive advantage and an important factor in value creation. That occupies a prominent place in contemporary management in the company. It is both a tangible sign of success and development. Note that the term of value creation has generated much debate and controversy because of its multiplicity of styles.

This concept is expanded to include various stakeholders, which is not only the result of contributions from shareholders, but the effort of all partners of the firm. The model of value creation is necessarily an integral model of organizational value, economic and social.

It has internal and external measures: the Return On Equity (ROE), the Market Value Added (MVA), the total shareholder return (TSR), the Weighted Average Cost of

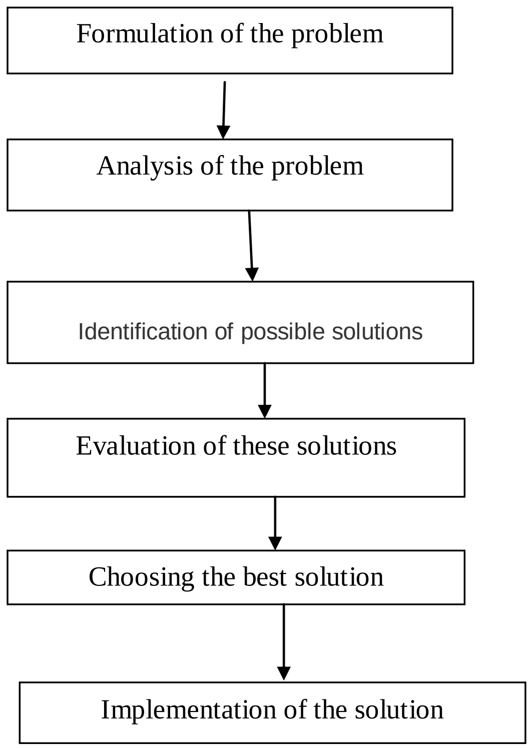


**Figure 1.** Decision making in the company.

Capital (WACC), the Total Business Return (TBR), the Return on Investment (ROI) and the Economic Value Added (EVA).

## An empirical study: case of Tunisia

This paper analyzes the effect of ethical behavior in creating value. The main hypothesis is that behavior can be an indicator of value creation. This hypothesis will be addressed in a sample consisting of Tunisian listed companies.

## METHODOLOGY

### Data

Our study covers major Tunisian groups that have particular characteristics management. Specifically, we selected cases where companies have begun to formalize and integrate ethics in their policy. The teams of these companies are characterized by greater moral values: the presence of rules of ethical conduct dictated by the public, educating business leaders and the presence of legislation reprehensive (Hung, 2007). There are is forty companies listed during the period, 2003 to 2011. We collected data by two methods:

1.The use of the database of the Central Bank of Tunisia (BCT).
2.The method of semi-directive interviews with managers.

The use of this method of interviews is justified by the qualitative character of the ethical variable.

### Measurement of variables and methodology

Our interrogation is to verify the influence of ethical behavior in creation of value. To verify this impact, we use the following variables.

### The dependent variable (Yi)

MVA: this is a measure of external performance, patented by the firm, Stern Stewart in 1991. It is the difference between market value and total assets book value.

MVA = VM-VC

where VM is the market value of the company (shares * price), VC is the book value of equity.

### The independent variables (Xi)

The ethical behavior of leaders: this variable is determined from a semi-directive interview with business leaders about how they can translate ethical behavior. This behavior is expressed by four sub built: Justice, Prudence, Strength, and Moderation.

We use these variables as dummy variables. The leaders respect the principles of rights and justice (Rawls 1971) and are characterized by rationality in decision making, taking into account feelings without exacerbating them and setting an example so that the image we give of ourselves is consistent with the message that we want to communicate.

In summary, the variable, Xi called ethic included justice, prudence, strength, and moderation.

Size (T): This variable is calculated from the logarithm of total assets.
Financial structure (Lev): It is determined from the financial leverage.
The investment opportunity (OP): the ratio of book value (VC) and market value (MV).
Earnings capacity (VACA): the ratio of value added (VA) and turnover (CA).
Labour productivity (WI): it is equal to the value added, less the cost of capital and reported number of employees.
Variation of turnover (var CA).

All the variables described below and the relationships that connect them; and will be subsequently validated empirically. They are summarized in the following model:

MVA (i,t) = a0 + a1Ethic (i,t) + a2T(i,t) + a3Lev(i,t) + a4OP(i,t) + a5VACA(i,t) + a6varCA (i,t) + a7WI(i,t) + $\varepsilon$ i,t

With $\alpha 1$, $\alpha 2$, $\alpha 3$, $\alpha 4$, $\alpha 5$ are the coefficients of independent variables which are to be determined. $\alpha$ 0: constant of the model. $\varepsilon$ it: the error term. Ethics contain the variables: justice, prudence, strength and moderation.

## RESULTS

### Descriptive statistics

For the analysis of the data, first, a descriptive statics and

**Table 1.** Descriptive statistics.

| Variable | Numbers of observation | Mean (Std. Dev) |
|---|---|---|
| MVA | 180 | 0.55 (0.704) |
| MODERATION | 180 | 0.44 (0.498) |
| PRUDENCE | 180 | 0.55 (0.49) |
| JUSTICE | 180 | 0.8 (0.4) |
| FORCE | 180 | 0.4 (0.501) |
| T | 180 | 11.61 (1.23) |
| Lev | 180 | 3.8 (5.95) |
| Op | 180 | -0.014 (0.85) |
| VACA | 180 | 1.52 (18.12) |
| Var CA | 180 | 0.74 (0.1) |
| WI | 180 | 0.0001 (0.00018) |

**Table 2.** Spearman correlation.

| | MOD | PRUD | FORC | JUSTI | WI | MVA | OP | Var CA | T | LEV | VACA |
|---|---|---|---|---|---|---|---|---|---|---|---|
| MODR | 1 | | | | | | | | | | |
| PRUD | 0 | 1 | | | | | | | | | |
| FORC | 0.3* | -0.31* | | | | | | | | | |
| JUSTI | -0.05 | 0.05 | -0.005 | 1. | | | | | | | |
| WI | 0.36* | 0.07 | -0.02 | 0.18* | 1 | | | | | | |
| MVA | -0.22* | -0.28* | -0.18* | 0.21* | -0.2* | 1 | | | | | |
| OP | 0.07 | 0.018 | 0.008 | -0.063 | 0.037 | -0.022 | 1 | | | | |
| Var CA | -0.09 | 0.09 | 0.11 | 0.05 | -0.08 | -0.003 | -0.05 | 1. | | | |
| T | -0.51* | -0.27* | 0.07 | -0.11 | -0.8* | 0.305* | -0.01 | 0.14* | 1 | | |
| LEV | -0.37* | -0.073 | -0.17* | -0.35* | -0.3* | -0.14* | 0.041 | -0.012 | 0.39* | 1 | |
| VACA | -0.07 | -0.077 | -0.076 | 0.039 | -0.06 | -0.039 | 0.052 | -0.0113 | 0.13* | 0.03 | 1 |

Spearman correlation will be realized.

Table 1 indicates the descriptive statistics of variables used in our empirical analysis. We find that the dependent variable (MVA) has an average value of 0.55 with a standard deviation of 0.7. And that our sample is characterized by negative growth opportunities. They have an average value (-0014).

The variables of ethical behavior of leaders have average values that vary between 0.8 and 0.4. Justice in managerial policies better explains the increase in turnover achieved.

We exhibit, then, the Spearman correlations between the indicators selected as part of our empirical study. We note from Table 2 that the determinants of value creation are the ethical behavior of leaders and different measures, the productivity of employers, the size of the business and financial policy of the company. And that these determinants are weakly correlated. Measurements of variables of size and leverage are negatively correlated.

### Method of panel

Following these initial descriptive results, we will adopt technical panel to analyze the data collected and assess the variables assumed to have influence.

Two estimation methods were then compared: the approach to the fixed effect and random-effects. According to the Hausman test and the Breush – Pagan, we specified the manner of estimate. But we will first perform the test for the presence of an individual effect (Chow test).

### Testing for the presence of individual effect

The results of this test concluded about the presence of individual effects in our sample (Table 3).

### Hausman test

We performed Hausman test to specify the model or by

**Table 3.** Chow test.

| | Chow test |
|---|---|
| Fisher test | 15.26*** |
| Prob > F | (0.000) |

*** Significant at 1%.

**Table 4.** Hausman test.

| | Hausman test |
|---|---|
| Chi-2 test | 2.50 |
| Prob>chi2 | (0.475) |

the inclusion of a fixed or random individual effect (Table 4). The Hausman test is insignificant; we will apply the random effects specification.

## Breusch – Pagan test

The probability of the Breusch-Pagan statistic shows that the random effects are significant at 1%; we use the appropriate statistical treatment by estimating random effect (Table 5).

Table 6 provides the estimated coefficients of the variables of our model for our sample. The results show that prudence and justice positively influence the value creation at the 1% and the feeling of superiority is negatively on value creation (significant at 5%). They are seen as competitive strategies of the business that have led to its survival and development.

The first objective is the satisfaction of all economic partners- financial and social "stakeholders". A behavior characterized by anticipating risks, listening to the various stakeholders, alignment of interests, regulatory transparency and having full understanding of the roles of each accompanied by an overview of the work environment should be put in place.

The specific strategies and financial management from the ethics of leaders influence the operation and business development. However, injustice between different parts of the business or the deterioration of relations between different parts of the company assigns the value of the company. This is the result of unethical behavior for the company, employees and investors. The behavior of leaders is considered a full-fledged social responsibility of business. It forms a major lever for sustainable performance and overall business.

Besides this behavior created value, there are four determinants of economic value of Tunisian companies:

(1) Leverage: the coefficient for leverage is negatively significant at 5%. Debt affects the performance of companies and is an incentive for executives to maximize their investment decisions.

(2) Earnings capacity (VACA): this variable is negatively significant at 1%. This implies that companies do not have the ability to achieve the average productivity level achieved by the sector.

(3) Dynamics: it being positive and significant at 10% shows the importance of increased turnover in improving business operations. Indeed, the increase of sales improves the ability of companies to increase value added, to achieve more growth and control the market.

(4) Size (T): the positive and significant coefficient of the variable size shows that large firms have superior performance to those of small ones.

**Table 5.** Breusch-Pagan test.

| | Breusch-Pagan |
|---|---|
| Chi-2 test | 91.75*** |
| Prob > chi2 | (0.000) |

*** Significant at 1%.

**Table 6.** Estimated coefficients on the source of value creation.

| Variable | MVA<br>Coefficients (probability) |
|---|---|
| MODERATION | -0.987(-0.1) |
| PRUDENCE | 0.24** (0.02) |
| JUSTICE | 0.18** (0.038) |
| FORCE | -0.78* (0.01) |
| T | 0.67*(0.08) |
| Lev | -0.64** (0.028) |
| Op | 0.295(0.14) |
| VACA | -0.98*(0.006) |
| Var CA | 0.01*** (0.088) |
| WI | -0.67 (0.79) |
| Numbers of observation | 177 |
| Wald chi2 | 46.00* |
| *Prob > Chi-2* | (0.0000) |

*** ;** ;* Significant at 1, 5, 10%.

## Conclusion

The main interest of this work lies in its contribution to the analysis of the ethical behavior of leaders in creating value in the strategies deployed by companies' management.

Faced with different mutations and crises, attitudes and ethical behavior are considered as necessary condition for business operation and development. The ethics of leadership appear increasingly as a new corporate social responsibility. This is a responsibility of any person holding a position of hierarchical supervision and direction. This behavior is an essential lever for overall performance and sustainable business. Responsibilities and leadership skills will significantly improve and evolve to incorporate this new managerial practice. This is related to the size, growth opportunity, the ability of employers and funding arrangements adopted.

Particular, the emergence and generalization of management practices for a better quality ethic will certainly pave the way for a new "organizational humanism." It will prove indispensable for the survival of economic and social system, resulting from the market economy.

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