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Perceived Enforcement of Informal Buyer-Supplier Contractual Arrangements in Ugandan Small and Medium Enterprises (SMES)

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Abstract - SME buyers tend to avoid formal binding contractual arrangements with suppliers of resources, a situation which creates operational and technical difficulties and increases transactional costs. Ntayi et al., 2010a using data from Ugandan SMEs have revealed that majority of buyers (83.4%) use oral agreements in their business transactions with suppliers. Only a few (16.6%) were observed to have used written contracts. Whereas informal and oral contracts are enforceable in the Uganda's commercial court, the process of assembling evidence is tedious and takes long (Kiryabwire, 2010). In such circumstances parties privy to the contract end up losing genuine cases unfairly. Even where they are successful, the assessment of damages to be awarded to the victor is a nightmare as business records are non-existent to properly establish the impact of the breach of contract on the business (Kiryabwire, 2010). This happens in SME business relationships which are meant to generate intangible and tangible benefits in short or long terms through the firm's social capital. The purpose of this study is to examine the effects of social capital, organizational amnesia, and moral reasoning on the enforcement behaviors of informal contracts in Ugandan SMEs. This study adopts a triangulation approach and collects data from a sample of 2,228 SMEs.

Results reveal that social capital and organizational amnesia have a significant negative effect on the enforcement behavior of Ugandan buyer-supplier informal contracts. However, the interactive effects of: social capital and moral reasoning; and organizational amnesia and moral reasoning has a positive effect on the enforcement behavior of Ugandan buyer-supplier informal contracts. This has policy and managerial implications which we present and discuss in our paper.

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1. BACKGROUND

Small and Medium Enterprises (SME's) continue to be constrained by resources despite consensus from organization theory that resources are of critical importance to the survival and competitiveness of firms (Lee et al., 1999). Resource constraints could be attributed to size; a concentration of power in the owner and the informal nature of doing business that characterize SMEs in Uganda (Ntayi et al., 2011a). Due to their nature and size, SMEs use social interactions of human capital to acquire needed resources from supplying firms. Additionally, conditions of competition and the quest for survival and growth, have forced SMEs to seek for resources embedded in their social relations. These social relations with both internal and external stakeholders provide buyer and supplier information related to their credibility, reliability, honesty and integrity. It is against this background that SMEs base their judgments and decisions to obtain supplies and other resources which are required in providing value to their customers. They establish relationships purposefully and employ them to generate intangible and tangible benefits in short or long terms. At the firm's level, the effectiveness of socialization process depends on the firm's social capital.

Social capital refers to "the resources embedded within, available through and derived from the network of relationships possessed by an individual and social group" (Nahapiet, 2000) through its structural and density cognitive aspects (Jansen et al., 2005). Social capital exists between individuals and resides in relations among the nodes to facilitate productive

activity (Coleman, 1988b, p 101; White, 2002). The creation of social capital in SMEs can be particularly beneficial in creating organizational knowledge and attitudes. Extant literature has revealed that social capital has both positive and negative consequences. It facilitates or inhibits innovative and risk-taking behavior, shapes relational business behaviour, provides networks, supplier information, supplier assessments and other resources that are of value to cooperate members (Westlund and Bolton, 2003). Indeed Othman and Hashim (2004) have noted that social capital resources are mobilized in purposive actions. In procurement related transactions, where research on social capital is sparse, the concept of social capital has been observed to facilitate inter-unit and inter-firm resource exchange (Hansen, 1998) and strengthen buyer-supplier relations (Baker, 1990; Gerlach, 1992; Uzzi, 1997). Findings in social capital research concerning "closed networks," reveal that norms and social relations conducive to getting work done are more easily developed in workplaces (Coleman, 1990). This idea is similar to Ntayi et al., (2010a)'s findings suggesting that the absence of proper contract records, proper book keeping and financial records in SMEs, despite their strategic importance in decision making process is partially calculated. These findings point towards a possible link between social capital and moral reasoning. The moral reasoning associated with this premeditated behaviour is that of insulating the resource constrained SME from losing resources, thereby facilitating business survival. Additionally, there is a general feeling that the self interests and aspirations of the owner managers must be protected. We suspect that the SME moral reasoning is based on conformity to social norms and expectations that exist in the workplace, although there is paucity of research to confirm this view.

Anecdotal evidence from the Ugandan SMEs reveals that, generally, there is low recognition of the ethical issues involved in a buyer-supplier informal contractual arrangement. This may be attributed to the fear of the aggressive tax collection methodology employed by the Uganda Revenue Authority (URA) and the current litigious environment creating an economic incentive for "organizational amnesia". Organizational amnesia refers to the systematic destruction of all unneeded personal notes and documents at regular intervals. The thinking behind this policy is that, in the event of litigation or criminal prosecution, no document should exist in writing that could be used against the SME buyers and/or sellers (Conklin, 2001). This is a tricky state of affairs for Ugandan SMEs, since a stream of organization theory research on contracts from organizational learning literature posits that the design, development, implementation, monitoring and enforcement of contractual provisions are a result of an

organizational learning process (Smith and King, 2006). Contracts are both inputs to learning processes and outcomes of learning. As inputs, contracts may assist organizations and courts of law in developing incremental changes in their structure. As outcomes, contracts are routines that are learned through experience with relational contracting and that contribute to organizational inertia (Smith and King, 2006, p. 33). Absence of relevant information on business transactions affects the quality of buyer-supplier contracts developed and may affect contract enforcement.

SME buyers tend to avoid formal binding contractual arrangements with suppliers of resources, a situation which creates operational and technical difficulties and increases transactional costs. Ntayi et al., (2010b) using data from Ugandan SMEs have revealed that majority of buyers (83.4%) use oral agreements in their business transactions with suppliers. Only a few (16.6%) use written contracts. Whereas informal and oral contracts are enforceable in the Ugandan commercial court, the process of assembling evidence is tedious and takes long (Kiryabwire, 2010). In such circumstances parties privy to the contract end up losing genuine cases unfairly. Even where they are successful, the assessment of damages to be awarded to the victor is a nightmare as business records are nonexistent to properly establish the impact of the breach of contract on the business (Kiryabwire, 2010). Othman and Hashim (2004) have revealed that research specifically examining the relationship between social capital and organizational amnesia is nonexistent. They aver that the creation of social capital will be an important element in overcoming organizational amnesia. The purpose of this study is to examine the levels of social capital, organizational amnesia, and moral reasoning of SMEs in Uganda. Additionally we examine the relative effect of these variables on the enforcement behaviors of informal contracts in Ugandan SMEs. This study adopts a conceptualization presented in figure 1.

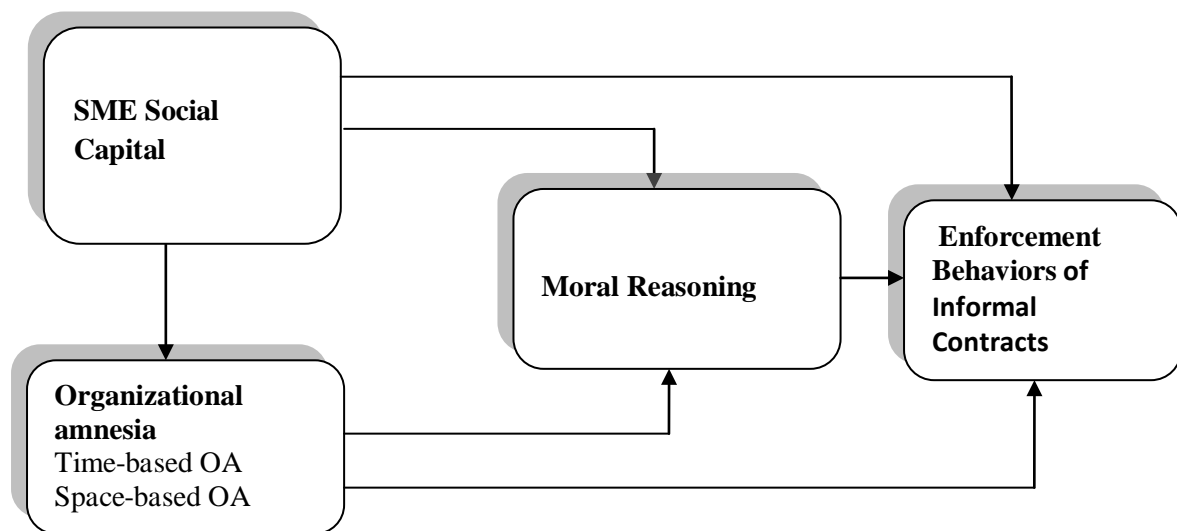
II. CONCEPTUALIZATION

Since most SMEs are family businesses, scholars suggest that high levels of family influence could have a negative effect on the social capital of the firm, and in turn on its performance (Adler and Kwon, 2002; Arregle et al., 2007; Leana and Van Buren, 1999). Some scholars argue that in an effort to maintain family ties, family members could reduce their ability of maintaining strong social ties outside the family (Barney et al., 2003), and that high firm social capital could lead to the problems associated with lack of innovation as individuals get rooted in time honored practices, thereby overlooking potential sources of useful information (Leana et al., 1999). This situation is potentially

dangerous for moral reasoning, organizational learning, organizational memory and organizational amnesia. Contract enforcement-managers with moral values would tend to apply reason and fulfill their contractual obligations. This suggests that in the event of any contractual disagreements, use of formal dispute

resolution mechanism will be pursued. The purpose of this study is to examine the levels and interrelationships of social capital, organizational amnesia, and moral reasoning and enforcement behaviors of informal contracts in Ugandan SMEs. This study adopts a conceptualization presented in figure 1.

Figure 1 : Relationship between social capital, organizational amnesia, personal values, emotions, moral reasoning, and enforcement behaviors of informal contracts within SMEs



III. LITERATURE REVIEW AND THE DEVELOPMENT OF THE CONCEPTUAL MODEL

a) Social capital, moral reasoning and enforcement behavior of contracts

Social capital is a multidimensional construct composed of structural, relational and cognitive aspects which allow the exchange of resources among individuals (Nahapiet and Ghoshal, 1998). The structural dimension of social capital, concerns the existence of connections among individuals and the structure of the social network in which relationships are embedded. Relationships occur between collaborating partners like buyers and suppliers. The relational dimension of social capital refers to the quality of those connections. It addresses the levels of mutual trust and reciprocity that exist among relationships. The cognitive dimension of social capital is related to attributes that facilitate the common understanding of the social context and reflects the levels of shared understanding and goals. A review of extant literature reveals that there is a connection between social capital and moral reasoning. Moral reasoning is the cognitive process of having moral sensitivity to a situation (interpretation of the situation, being aware of how various actions would affect parties concerned, imagining cause-effect relationships, and being aware of a moral problem) and having moral

judgment to a situation (judging which action would be most justifiable in a moral sense) (Rest et al., (1999), page 101). Kohlberg (1981) argued that moral reasoning is a function of a person's level of moral development, which is an enduring component of a person's cognitive makeup which may influence attitudes and behaviors. Piaget (1973) revealed that behavior reflects a conscious state of mind and thinking through a dilemma or a problem. Moral reasoning forms the basis for ethical behavior and decision making (Candee and Kohlberg, 1987; Kohlberg, 1987). From the ongoing we hypothesize that, H1: Social capital and moral reasoning are significantly positively correlated; H2: Moral reasoning affects SME buyer-supplier informal contract enforcement behaviors positively; H3: Social capital affects SME buyer-supplier informal contract enforcement behavior; H4: Social capital interacts with moral reasoning to affect SME buyer-supplier informal contract enforcement behavior.

Moral reasoning refers to the reasoning process by which human behaviors, institutions, or policies are judged to be in accordance with or in violation of moral standards. Moral reasoning is characterized by moving along a pre-conventional to a post-conventional level of thinking. At the pre-conventional level of thinking, SME employees and employers would ordinarily obey and respect rules and norms for a solution. Individuals, who are dominated by the post-conventional thinking, tend to

weigh and consider abstract principles and also take more perspectives into consideration. As noted by Rest et al., (1999) the development of moral reasoning is a shifting distribution in which more primitive ways of thinking are gradually replaced by more complex ways of thinking. This primitive or complex form of thinking has been conceptualized by Rest et al., (1999) as moral schemas. These schemas or frameworks are a result of accumulated socio-moral experiences. Drawing from the works of Kohlberg (1967), we identify three moral schemas of personal interest schema, the maintaining norms schema, and the post-conventional schema that forms a developmental hierarchy.

"The personal interest schema relies on an egocentric and interpersonal perspective in which the individual focuses on the personal stakes that the actor has in the dilemma and its consequences. It also emphasizes concern for others with which the person has a close relationship. The maintaining norms schema, usually emerging in adolescence, is characterized by perception of a need for a society-wide system of cooperation and the uniform application of laws and social norms, as well as a duty-based, authoritarian orientation. The post conventional schema, which is the most complex of the three schemas, is characterized by the core belief that moral obligations are to be based on shared ideals, which are reciprocal and are open to debate and tests of logical consistency, and on the experience of the community (Endicotta, Bockb and Narvaez, 2003, p.406)".

Ntayi et al., (2010b) have revealed signs of personal interest schema commonly displayed by buyers and suppliers in Uganda. For example in almost all transactions, payments to suppliers were delayed by the buyers for selfish or egoistic reasons. This resulted in the most frequent illegal actions of cutting corners on quality control, cover ups, inflated costs, outright deceit, dishonesty, cheating, shirking contractual obligations and violating an unwritten understanding with a supplier. Excessive pressure to deliver results without any down or timely payments from buyers was significantly correlated with willingness to compromise ethics to cushion SMEs from financial shocks. This was surprising in situations where parties to the contract have the duty to comply, duty to disclose, duty not to misrepresent and duty not to coerce.

Literature has revealed that sometimes parties to the contract act irrationally when under the influence of fear or emotional stress. When a seller takes advantage of the buyer's fear or emotional stress to extract consent to an agreement that the buyer would not make if the buyer were thinking rationally, the seller is using duress or undue influence to coerce, because contracts have to be entered into freely, the seller, has the duty to refrain from exploiting emotional states that

may induce the buyer to act irrationally against his or her own best interests. For similar reasons the seller also has the duty not to take advantage of the gullibility, immaturity, ignorance, or any other factors that reduce or eliminate the buyers ability to make free rational choices. It can be averred that the principles of buyer-supplier ethics as enshrined in the PPDA Act (2003) are interrelated to moral reasoning and guide in decision making (Beauchamp and Childress, 1989; Beauchamp, 2003). Moral reasoning of SME managers when confronted with moral dilemma has not been studied extensively in a developing world context. SME owner managers make decisions that can develop the economy. When confronted with ethical and unethical decisions, a moral dilemma arises. Several unethical events and failure to fulfill contractual obligations across the country have put business development in Uganda at a risk and jeopardize the investment climate. Research in moral reasoning of SME managers in Uganda is needed to understand and solve the growing problem of ethics. Extant literature has shown that the relationship between a business firm and its customers is essentially a contractual relationship and the firm's moral duties to the customer are those created by this contractual relationship. From the above discussion we hypothesize that, H5: Moral reasoning of SME buyers and suppliers is characterized by the personal interest schema.

b) Social capital, organizational amnesia and enforcement behavior of buyer-seller informal contracts

Literature has demonstrated that social interactions within an organization, provide a platform for passing on explicit (objectified) and tacit (collective) organizational knowledge (Spender, 1996). Organizational knowledge is embedded in the forms of social tacit experiences and collective (relation specific) institutional practices (Brown and Duguid, 1991). As articulated by Spender and Grant (1996, p. 8) "...knowledge which is embodied in individual and organizational practices cannot be readily articulated. Because of its uniqueness, tacit knowledge is created and shared through interactive conversation, shared experience, learning by doing, training or exercising (Herrgard, 2000). It is indigenous wisdom that could be transferred from our minds to other holders through social capital- continuous interactions and relationships'. Ghobadian and Gallear (1997) and Wong and Aspinwall (2004) have noted that SMEs employ individuals who are connected to networks and share common beliefs, norms, and values. Their thinking is not expected to vary from the thinking of owner managers. Should there be a variation in the philosophical mindset of the SME owner managers and employees, the SME employee is forced to exit leaving behind no retrievable records.

As revealed by Moran (1999), staff in SMEs need appropriate and up to date knowledge, need to know what their colleagues know and need ways of remembering what they know. In SMEs, this is partially done using social capital and/or other informal networks. It is on the basis of these informal networks that SMEs base their informal dealings and contracts. The construct of social capital has gained wide popularity and acceptance among researchers in organization studies due to its ability to explain individual network interactions within (Burt, 1992) and outside the organizations (Fukuyama, 1995; Putnam, 1995). These network interactions are inevitable in a competitive industry where firm's success depends on how well business transactions with stakeholders are managed. The creation of social capital in SMEs can result in social, psychological, emotional and economical benefits (Lin 1986;1999;2000). Socially, social capital represents the resources embedded in the social network between SME employees, managers and SME employees, and buyers and suppliers. For example establishing working relations with new suppliers or vendors may be facilitated if they are met through after-hours connections. This minimizes high transaction costs associated with managing business transactions in a less developed country like Uganda and solve difficulties of enforcing informal contracts. Based on the above discussion we hypothesize that; H6: Organizational amnesia affects SME buyer-supplier informal contract enforcement behavior. H7: Social capital interacts with organizational amnesia to affect SME buyer-supplier informal contract enforcement behavior.

IV. METHODOLOGY

a) Research design, sampling and data collection methods

This study adopted descriptive, quantitative and qualitative research designs. The qualitative research design was associated with interpretative approaches, from the informants' emic point of view, rather than relying on only etically measured discrete, observable behaviour (Maykut and Morehouse, 1994; Frechtling, and Sharp, 1997). This was deemed necessary in order to obtain explanations for enforcement behavior of informal buyer-seller contracts better. The corresponding results of the subjective inquiry are presented as vignettes, cases and causal networks used to explain and discuss the statistics obtained in the quantitative results section of this paper. The argument used was that quantitative methods measure human behaviour "from outside", without accessing the meanings that individuals give to their measurable behaviour. This is what the qualitative inquiry attempted to solve (Mishler, 1986; Punch, 1998; Sekaran, 1992). A qualitative research design allowed these

understandings to be investigated from the informants' point of view (Patton, 1982; Patton, 1990; Patton, 1997; Patton, 1999) by describing experiences and relating them to enforcement behavior of informal contracts. We selected a sample of 2,228 out of the total population of 45,832 SMEs using the average sample size of similar studies in Uganda (Ntayi et al., 2010b). This sample was proportionately distributed under small manufacturing, trade and agro-processing. A sampling frame of SMEs was obtained from Uganda Small Scale Industries Association (USSIA) and Uganda Manufacturers Association (UMA). The respondent firms were selected using stratified and simple random sampling methods. Stratified sampling was used because SMEs are categorized according to industrial grouping and we believe that there could be significant differences in the contractual practices in these three categories. From each stratum a sample representing the population was chosen using simple random sampling. Data was collected using an interviewer administered questionnaire which was made up of both closed and open ended questions to allow deeper understanding of the subject matter. This questionnaire was initially developed and pilot tested to ensure validity and reliability of the measurement scales. Results of the pilot test using a sample of 50 respondents drawn from buyers and suppliers engaged in formal contracts revealed a Cronbach Alpha coefficient of 0.6 and above which was considered satisfactory for this study. Respondents for the main study were only managers and/or individuals working with SMEs who participate in either buying goods and services for the organization or selling goods and services to other organizations and/or trade on a contractual arrangement. Due to the sensitivity of the subject matter under investigation, the researchers assured the respondents of their confidentiality and anonymity. A copy of an executive report was given to them during a dissemination workshop that was organized by the researchers.

b) Measurements

All item scales for the variables were derived from previous studies where they had been tested for validity and reliability.

Moral Reasoning - Moral reasoning construct was measured using a self-administered questionnaire developed using ideas from Rest's (1986) Defining Issues Test (DIT). This is one of the most well-known measures of moral reasoning in the field of moral psychology (Modgil and Modgil, 1988) which has been utilized in many published studies. The DIT provides a useful contribution to the understanding of an individual's moral reasoning abilities based on dilemmas derived from social issues and is an accurate measure of moral reasoning dealing with personal issues (Fraedrich et al., 1994). Unfortunately, when used in its original format the DIT does not accurately reflect

an individual's moral reasoning in a professional buyer-supplier contractual setting. This is because the DIT does not contain dilemmas which fairly represent business or professional environments (Ponemon, 1990, 1993; Weber, 1990; Trevino, 1992; Elm and Nichols, 1993; Elm and Weber, 1994; Welton et al., 1994). The dilemmas contained in the DIT comprise broad life moral issues, ranging from stealing a drug to saving the life of one's spouse to discontinuing a newspaper for its disturbing social influence. This prompted the researchers to develop a context-specific instrument to help tap and understand better an individual's moral reasoning in professional buyer-supplier settings (Welton et al., 1994). Consistent with Welton et al., (1994) this study applied a self-designed test which parallels the DIT in design, to tap issues related to moral reasoning levels of SMEs in Uganda. Realistic case dilemmas were preferred because of their ability to elicit representative reasoning processes. Fredrickson (1986) has observed that case dilemmas generate interest and create involvement in the respondent. The DIT consisted of moral dilemmas relating to main moral duties of buyers and sellers. In general, these included complying with the terms of the contract and the secondary duties of disclosure, avoiding misrepresentation and avoiding use of duress and undue influence. This instrument comprised of twelve business and buyer-supplier contractual dilemmas at the pretest level, which were reduced to six which were adopted for the main study. These were:

- (i) The "compliance" dilemma considers whether an SME manager of a buying firm should accept a liability for failure to live up to the promises made by his/her staff (the seller) to the buyer when the manager knows very well that the seller cannot deliver goods that conforms to the affirmation or promise made. The manager also knows that when he/she accepts, the penalty to the company is heavy and this may result into crippling the company that has not lived up to the express claims made about products.
- (ii) The "disclosure" dilemma considers whether an SME manager should keep records and performance of all transactions with the contracting party and keep such records in the proximity of regulatory bodies with a view of disclosing such information to regulatory bodies if need arises. But the SME manager is also aware that the company has not complied with any of the tax statutory requirements.
- (iii) The "misrepresentation" dilemma considers whether the SME manager should approve an act by his/her senior sales staff who has described a product as new or fit for consumption and has also displayed old/used/expired products with several new products with an intention to deceive the buyer into

thinking something about the product that the seller knows is false.

- (iv) The "coercive" dilemma considers whether an SME manager would approve a contract entered into by his/her staff who has taken advantage of a buyers ignorance, fear or emotional stress to extract consent to an agreement that the buyer would not make if the buyer were thinking rationally. Unscrupulous sales people may skillfully induce guilt-ridden and grief-stricken or unsuspecting buyers to buy a product expensively which they would otherwise have not bought.
- (v) The "due care" dilemma considers whether an SME manager should accept to take responsibility over a manufacturers product which he/she sold to a customer and the customer experienced a terrible incident with it. E.g a customer used a product he/she bought from your stores and while in use all of a sudden the user heard a terrible loud cracking noise. The product burnt producing a terrible smoke and fire that burnt the room where it had been installed.
- (vi) The "social costs" dilemma considers whether an SME manager (buyer/supplier) would extend his duties beyond those imposed by contractual relationships and beyond those imposed by the duty to exercise due care in preventing injury or harm
- (vii) The "faulty products" dilemma considers whether an SME manager - supplier should deliver expired products, knowing that he is delivering goods which are not fit for purpose and contrary to the terms and conditions of the contract;
- (viii) The "payments" dilemma considers whether an SME manager should approve a claim by his colleague to pay a supplier, knowing that the claim has been exaggerated, all the paperwork has been properly written and passed and no deliveries were made.
- (ix) The 'reimbursement' dilemma considers whether a finance officer should approve an expense reimbursement claim by his superior, knowing that the claim has been exaggerated;
- (x) The "power" dilemma considers whether a buying or supplying party which has more power than the other should dictate the terms of the agreement knowing the rights of each contracting party
- (xi) The "product adulteration" dilemma considers whether a supplier should go ahead and supply a product whose attributes has been tampered with (e.g label, package, trademark, weight etc) knowing that this product alteration would lead to serious consequences for the company
- (xii) 'The acceptance' dilemma considers whether a manager of a supplying company should accept a

qualified opinion report from the staff of the supplying company pointing out weaknesses in the client's products in the production process supplied by the same firm.

The DIT was composed of a series of moral dilemma vignettes and follow-up questions; after deciding what the character in the vignette should do, the participants were asked to identify which issues they felt were important in making a decision about the moral dilemma. Each DIT moral dilemmas had 12 follow-up questions, which resulted in a total of 72 items. These items were rated on a five-point Likert scale with 5=great importance to 1 = no importance. We checked for internal consistency of reliability using the "meaningless" score. The issue statements after each vignette have statements that sound meaningful and important, but do not match up with any stage of moral reasoning. Therefore, they are considered "meaningless" items (Rest, 1986). Participants who endorsed a large number of meaningless items were considered to have invalid protocols and were excluded from the study. Other reliability checks like consistency, missing ratings, missing rankings, non-differentiation – to eliminate respondents who have taken insufficient care in completing the test were applied. This scale yielded a Cronbach alpha coefficient of 0.774.

SME social capital- There are several measures for social capital and obtaining a single, true measure is probably not possible. Woolcock and Narayan (2000) have attributed this difficulty to the multidimensional nature of social capital and the different levels of analysis. Further, the forms of social capital change over time shifting between formal and informal organizations. despite this challenge, common measures in the studies have been identified as the membership in informal and formal associations and networks and the trust, norms, values that facilitate exchanges and lower transaction costs (Woolcock and Narayan, 2000; Schuller, 2001; Krishna and Schrader, 2002). This study adopted the definition given by Leana and Van Buren (1999) who define social capital at the organizational scale as "a resource reflecting the character of social relations within the organization, realized through members' level of collective goal orientation and shared trust." Organizational social capital was conceptualized as a multidimensional construct composed of Structural social capital (connections among actors), relational social capital (trust among actors), and cognitive social capital (shared goals among actors) (Nahapiet and Ghoshal, 1998). Structural social capital pertains to the opportunities for organizational members to gain access to relevant peers with desired sets of knowledge or expertise. Consistent with Andrews (2007, p.15), the structural dimension was gauged by asking informants about the extent to which "cross-departmental and cross-cutting working" was "important in driving contract

enforcement". Informants were asked whether "there is a high level of trust between top-management and staff" and if "there is a high level of trust between top-management and employees" in order to assess the relational dimension of social capital (p.16). Finally, the cognitive dimension was evaluated by enquiring about the extent to which the SME's "mission, values and objectives are clearly and widely owned and understood by all staff". Item scales for the trust, dimension of cognitive social capital were derived from the works of Munene and Isingoma (1994). These item scales were further adapted and broadly related to trust, reciprocity, mutual help, etc. we preferred to adapt these trust item scales because they have been previously applied to Ugandan organizations yielding an acceptable validity and reliability levels Zhang et al., 2006. All item scales were anchored on a 5 point likert-type scale with "1=strongly disagree to 5=strongly agree". All score items for structural capital, relational capital and cognitive capital were aggregated to form the social capital index. The Cronbach Alpha coefficient, which measures the internal consistency of a scale based on the average inter-item correlation was 0.838 and was considered adequate

Organizational amnesia - Measures for this construct were derived from a well documented body of knowledge on knowledge management and organizational memory. There are no standard universal measurement scales for organizational amnesia (OA). This may be attributed to conceptual differences. In this study, we attempt to contextualize previously developed item scale measures by relating them to SME buyer-supplier contractual arrangements. This study drew heavily from the works of Othman and Hashim (2004, p. 276) who have conceptualized organizational amnesia as a multidimensional construct composed of "time-based OA" that relates to the inability to benefit from past experience and "space-based OA" related to the inability to move or diffuse lessons learned at one point in the organization to other points in the organization. This preference was based on the ability of the Othman and Hashim's conceptualization to capture OA in its broad sense. Scholars like Kransdorff (1998) and Tiwana (2000) have tended to lean towards "time based OA" while Hughes-Wilson (1994), Snyder and Cummings (1998) and Robertson and Hammersley (2000) lean more towards "space-based OA". Despite these inclinations, this study captures both aspects of OA. All item scales were anchored on a 5 point Likert-type scale with "1= strongly disagree" to "5 = Strongly agree". Sample item scales adopted in this study included: "In this organization, we keep two sets of books of accounts one for management's use and the other for use by government regulatory bodies; In this organization, we don't keep up to date records on contracts with our business partners®; In this organization, quite often we experience loss of memory;

In this organization, we deliberately do not keep information that can easily be picked and used by detractors against us in future®; In this organization, we fear legal liability that could be traced back to the company "paper trails"; in this organization; In this organization, people who have the knowledge often leave and no retrievable record remains; Item measures for organizational amnesia yielded a cronbach alpha coefficient of 0.793.

Measures for contract enforcement behaviors were derived from the work of Fatchamps (1996) who developed a measurement scale which was used to collect data from case studies of manufacturing and trading firms in Ghana. The scales used in his paper document how commercial contracts are enforced in Ghana. Sample questions covered dimensions of compliance with contractual obligations, the desire to preserve personalized relationships based on mutual trust, harassment, court action, reputation effects, use of illegitimate force, contract renegotiation and reputation mechanism. Other items included: time elapsed since last case, in days, percentage of cases with full delivery, percentage of cases with partial payment, client faced technical or financial difficulties, client was unable to collect payment from own customer, client had to travel or left the business, client cheated. Other item scales were derived from the World Bank Group, Doing Business, (2003). Sample Items covered the efficiency of the judicial system on the enforcement of commercial contracts using: The number of procedures mandated by law or court regulation that demands interaction between the parties or between them and the judge or court officer, an estimate - in calendar days - of the duration of the dispute resolution, the cost- including court costs and attorney fees, as well as payments to other professionals like accountants and bailiffs. We compared these items against the ones developed by Ntayi et al., (2010b). All item scales were anchored on a seven point Likert type response scale ranging from "1 = strongly disagree to 7 = strongly agree". Item scales yielded a Cronbach Alpha Coefficients of 0.824.

c) Data analysis

To test our hypotheses, we conducted correlation, regression and interaction analyses. In order to test the hypotheses rigorously, we conducted hierarchical multiple regression analyses following the procedures recommended by Aiken and West (1991); Cohen et al., (2003). In the first step of the regression, we entered SME social capital variable. In the second and third step, we entered the organizational amnesia and moral reasoning variables respectively. In order to test the enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements containing the moderation and interaction effects, we used the procedure recommended by Aiken and west (1991) and Irwin and McClellan (2001). Aiken and West

(1991) have described the use of multiple regressions as a method for investigating interactions between continuous variables. Consistent with Aiken and West, (1991), the first thing we did was to center the independent variables by subtracting the mean from each value to prevent the interaction effect from causing unacceptable levels of collinearity.

V. RESULTS AND DISCUSSION

Response rate was 36%, which was slightly lower than the average 39% obtained from similar studies conducted in Uganda. This could be attributed to the sensitivity of the research topic. The trade sector had the highest number of respondents (38.4%), followed by agro-processing (34.1) and manufacturing sectors (27.5%) respectively. 56.7% of the respondent firms were small, employing between 5-49 people, while the remaining 43.3% were medium sized enterprises with 50-99 employees. Majority of the respondent firms (46%) had operated for 10 years and over. This was followed by firms that had been in business for a period between 5-9 years making up 30.2% of the surveyed firms. 23.8% of the remaining firms had been in operation for less than 5 years. The business relationship between buyers and suppliers had on average lasted for a period of 4 years.

Figure 2 displays the means, standard deviations and bivariate correlations among the study variables. Zero order correlations were all significant and moderate, ranging between 0.309 and 0.558. Variance inflation factors were below the 10.0 threshold (Hair et al., 1998) and the corresponding tolerance levels ranged from 1.00 to 1.12 (figure 4). This indicates that multicollinearity was not a major problem in the database. According to Rovny (2009, p.3), "multicollinearity exists when a predictor is a perfect linear combination of one or more of the remaining predictors". This situation creates high correlations which results in large standard error which leads to rejection of relationships which may be true. Specifically, figure 1 reveals that organizational social capital is significantly positively correlated with organizational amnesia ($r=0.309$, $P<0.01$), significantly negatively correlated with moral reasoning ($r=-0.364$, $P<0.01$) and enforcement behavior of informal buyer-supplier contracts ($r=-0.422$, $P<0.01$) supporting H1. Organizational amnesia was significantly and negatively correlated with moral reasoning ($r=-0.526$, $P<0.01$), and enforcement behavior of informal contracts ($r=-0.558$, $P<0.01$). The relationship between moral reasoning of procurement managers and enforcement behavior of informal buyer-supplier contracts was positive and statistically significant ($r=0.531$, $p<0.01$).

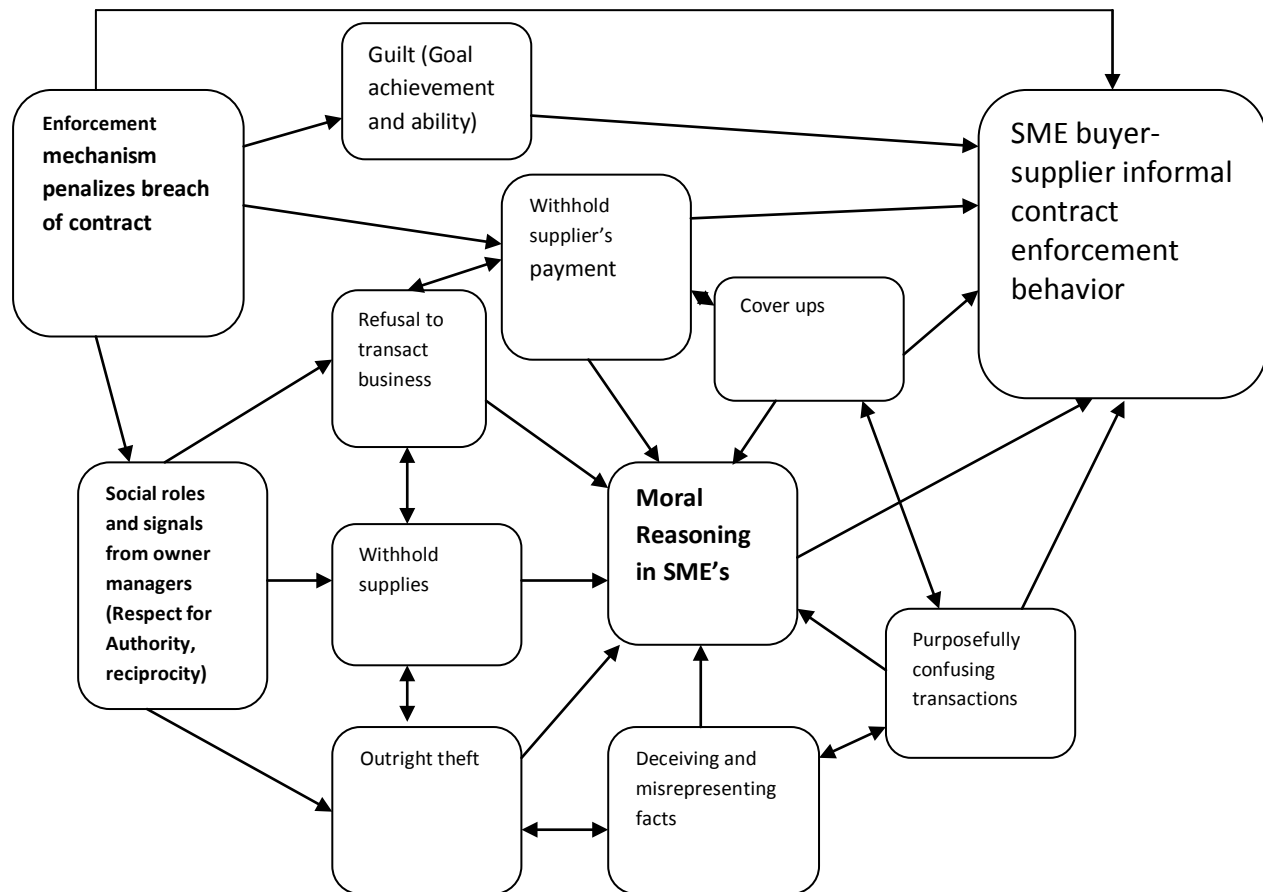
Figure 2 : Correlation Analysis Results

	Mean	Std. Deviation	1	2	3	4
SME Social Capital (1)	3.26	1.74	1.00			
Organizational Amnesia (2)	4.30	1.76	.309**	1.00		
Moral reasoning of procurement managers (DIT P%-score) (3)	0.25	2.27	-.364**	-.526**	1.00	
Enforcement Behavior of Informal buyer-supplier Contracts (4)	4.41	1.71	-.422**	-.558**	.531**	1.00
**Correlation is significant at 0.01 level of significance, *Correlation is significant at 0.05 level of significance, n=802						

Consistent with H5, descriptive statistics and results from qualitative interviews using the absolute P% values of moral reasoning scale, reveals that 93% of the respondents scored a dismal 25 or below, scores commonly associated with pre-conventional stage. This study further revealed that when SMEs procurement managers are faced with ethical dilemmas they more often than not exaggerate their offer, lie about certain things in order to protect their self-interests, alter facts, promise to do certain things and fail to do them. This finding is partially supported by the following representative case, V1 "...we have experienced many disappointing situations from our business partners which include but not limited to outright theft, cheating, breach of the gentleman's agreement, distorting data, purposefully confusing procurement related transactions, making false threats and promises, cutting corners, cover ups, deceiving and misrepresenting, inflating costs, dishonesty, shirking contractual obligations and violating unwritten understanding with buyers and suppliers" (see figure 3 for details). Additionally, late delivery, and deliveries of wrong quantities and poor quality items are a common feature among SME business partners. This self-interest could be attributed to the increased pressure on the SME resources and the demands of the buying or supplying organizations. For example, buyers testified that suppliers of agricultural produce typically supply goods which are high in moisture content, shriveled, diseased and discolored, insect damaged, mouldy and on several occasions foreign matter like sand, earth, dust, weeds, stones constitute a sizeable part of the supplies. These findings are consistent with observations of Kiryabwire (2010) who contends that increased business disputes in Uganda are associated with delivery of goods not fit for the purpose or not according to specifications or description; non delivery of goods and services paid for, nonpayment for goods and services given and failure to interpret terms and conditions of the contract. The following case displays a typical encounter between a buyer and supplier. "...In our daily transactions, we aim at developing a long term business relationships. When a supplier fails to supply as per the contractual obligations, we expect a genuine reason for non-

compliance." Unfortunately, our business partners are shrewd. Sometimes they display total ignorance of the contractual terms or completely deny their contractual obligations. We usually take it simple, because this seems to be the order of the day in Uganda." Surprisingly this study reveals that many SME managers try to weigh the physical consequences of an act before engaging in any manipulative trick. This is possible because most of the contracts entered into are informal and paperless. The SME procurement managers are interested in promoting self-interest and only consider others to the extent that they can help get what they want. This partially confirms H3 and also offers an explanation to the existence of negative social capital which leads to the practice of avoiding partners who are expected to be a hindrance to achieving procurement manager's self-interests. This depends on the perceived impact they would have on goal achievement and the level of guilt felt. Guilt is a cognitive or an emotional experience that occurs when a person realizes or believes—accurately or not—that he or she has violated a moral standard, and bears significant responsibility for that violation (Strickland, 2001; 2006; 2007). Guilt is a result of how close our social setting is closely knit to the SME business establishments and one's ability and desire to achieve goals as shown in figure 3. Unfortunately, this study finds that some buyers and suppliers lack any true sense of guilt or remorse for harm caused to others. Instead, buyers/suppliers rationalize their behavior, blame someone else, or deny it outright (Morten, Millon, Erik and Davis, 2002; Hare and Neumann, 2005). This can be seen as lack of moral reasoning and an inability to evaluate situations in a moral framework.

Figure 3 : Causal network relating moral reasoning and contract enforcement in Ugan



7% of SME respondents scored above 30 but less than 40 scores on the DIT, indicating that the moral reasoning for this category of respondents in the SME sample was at the "conventional" level. Consistent with Kohlberg's model, SME managers are very conscious with what people around them would think about a decision taken on an ethical dilemma. As a result SMEs try to gain acceptance in filling social roles by seeking approval from other people as it reflects society's accordance with the perceived role. This forces them to informally collaborate with external members like Uganda Revenue Authority (URA) staff, area Local Councils (LC's), district planners and development offices, to try and offer protection to the SME. What is interesting here is that morality of an action by the SME manager is judged in terms of a person's relationships with the immediate and distant members of the social system. The moral and social relationships forms a basis for a moral order on which SMEs in Uganda are built. The intentions of actions play a more significant role in moral reasoning at this stage. Social influences in Uganda discourage the use of a legal system and contract law.

Social relations within SMEs undermine moral judgment and connect organizational members through

negative interactions. These organizational members end up complying with unwritten rules within SMEs due to excessive pressure originating from peers and/or managers or collective social behaviors of both internal and external organizational members. This social influence has been responsible for the low level moral development among SME buyers and suppliers and thus conditioning SME employees to be morally mute. SME Employees have decided to keep quiet and not to speak out on moral behaviors of their buying or supplying organizations which act contrarily to the buyer-supplier contractual obligations. Social cohesion offers punishment to enforce contractual obligations by refusing to deal with a trading partner in the future and/or driving the partner out of a business network. This behavior can be referred to as social exclusion. Exclusion from business associational life is based on pressure to gain transactions that SMEs badly need in order to acquire resources that enable survival possible. This practice offers incentives to SMEs to comply with industry organizational amnesia practice of not filing tax returns, failing to keep and destroying business records, a practice that reinforces or perpetuates low moral reasoning.

Consistent with Flannery and May, (2000); May and Pauli (2002) and Singhapadki, Vitell, and Kraft, (1996), this study finds support for the relationship between work place social consensus and moral action in situations of ethical dilemmas. For example, social learning that result from continuous peer interactions among SME employees creates social identity which is related to moral behavior. In this study we demonstrate that employees in Ugandan SMEs worry more about social identity than professional identity. Respondents did not feel shy to defend and/or associate with SMEs that were known to be morally insensitive to their clients. Results from interviews revealed that many SMEs participated in some or a combination of these morally questionable actions : add sand to the grain at the time of sale to increase the weight, add stones to bulk the commodity, mix good quality with poor product, mix wet product with dry product, refuse to pay after delivery of goods and supplies, sell their produce to one buyer after having agreed on a price with another buyer, accept advance payment from one buyer and then sell the product to another buyer, adulterate the products of manufacturers and/or farmers. This finding is surprising and at variance with what transactional problems that contracts are meant to resolve. Under ideal situations, the buyer-supplier contracts provide assurance to the contracting parties that they do what they contract to do. It is only if they have such assurance will businesses feel able to trust each other's word and, on that basis, to

secure the benefits of the institution of contracts. Despite this contradiction, the study supports the works of Newell (2004), Edelman (2004) and Edelman et al., (2004) who reveal that social capital can be detrimental to value driven transactions. This paper has proved that social capital in SMEs has drawbacks and that these negative aspects of social capital result into opportunistic tendencies which the contract is supposed to address. Social capital has implications for decisions made when faced with ethical dilemmas since moral reasoning and social capital constructs were significantly correlated.

Furthermore as recommended, regression analysis was undertaken hierarchically to test for significant interaction effects over and above the main effects of the independent variables and the results are reported in figure 4 below. The control variables of organization age, ownership, and sales turnover were entered first to examine their simple additive effects on the enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements. Model 1 revealed SME ownership to have a significant negative main effect on the enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements ($R^2 = 0.015$, $p < 0.01$). The main effects of social capital, organizational amnesia and moral reasoning were entered second, third, fourth respectively and the interaction terms were entered in the fifth, sixth and seventh model.

Figure 4 : Hierarchical Regression Analysis with enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements as the dependent variable

Variables	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Co linearity statistics Tolerance	VIF
(Constant)	4.63**	3.13**	1.65**	1.29**	.527	.224	-.124	na	Na
Org. Age	0.067	.023	.009	.013	.007	.015	.013	.970	1.03
Ownership	-0.098**	-.087**	-.063*	-.046	-.048	-.049	-.047	.998	1.00
Sales turnover	0.028	.069*	.049	.031	.030	.024	.023	.969	1.03
Social Capital within SMEs		-.423**	-.279**	-.219**	-.514**	-.634**	-.552**	.982	1.02
Organizational amnesia (SMEs)			-.467**	-.349**	-.538**	-.461**	-.563**	.890	1.12
Moral Reasoning of SME procurement Managers				.261**	.260**	.413**	.580**	.899	1.11
SOCXOA					-.410**	-.264*	-.175	na	Na
SOCXMR						-.323**	.294**	na	Na
OAXMR							.290**	na	Na
R	.122	.437	.622	.657	.666	.670	.673	na	Na
R square	.015	.191	.387	.432	.444	.449	.453	na	Na
Adjusted R square	.011	.187	.383	.428	.439	.444	.447	na	Na
F – statistics	158.47	216.97	147.83	133.64	117.77	104.57	90.20	na	Na
Sig.	.007	.000	.000	.000	.000	.000	.000	na	Na
R Square Change	.015	.176	.196	.046	.011	.006	.003	na	Na
F change-statistics	4.04	173.46	253.94	63.87	16.39	8.06	5.04	na	Na
Sig F Change	.007	.000	.000	.000	.000	.005	.025	na	Na
Note: Standardized regression coefficients are reported, n=802, n/a = not applicable									
** Regression is significant at the 0.01 level, * Regression is significant at the 0.05 level.									

The results of model 2, shows a statistically significant and negative effect of social capital on the enforcement behaviors ($\beta = -0.423$, $P < 0.01$) with $R^2 = 0.191$ and $\Delta R^2 = 0.176$. This finding supports H3 which states that social capital affects SME buyer-supplier informal contract enforcement behavior. The negative sign indicates that higher levels of social capital within the buying and supplying SMEs are associated with greater levels of non-enforcing behaviors of informal contracts. Model 3, reveals that SME organizational amnesia significantly and negatively predicted enforcement behaviors of informal contracts ($\beta = -0.467$, $P < 0.01$) with $R^2 = 0.387$ and $\Delta R^2 = 0.196$. This finding supported H6. This result demonstrates that higher levels of organizational amnesia are associated with SME non-compliant contract enforcement behavior. Model 4 contained a simple additive effect of moral reasoning on enforcement behaviors of informal contracts which resulted in a statistically significant positive effect ($\beta = 0.261$, $P < 0.01$) and had a $\Delta R^2 = 0.046$ supporting H2. The statistically significant and positive effect demonstrates that increased levels of moral reasoning are associated with increased levels of enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements.

Model 5, reveals that the interactive term of social capital and organizational amnesia of SME Managers negatively predicted enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements ($\beta = -0.410$, $P < 0.01$) with R Square change statistic of 0.011). This finding support H7: social capital interacts with organizational amnesia to affect SME buyer-supplier informal contract enforcement behavior. Similarly, consistent with H4, model 6 reveals that the interactive term of social capital and moral reasoning significantly and negatively predicted enforcement behaviors of informal contracts in Ugandan buyer-supplier contractual arrangements ($\beta = -0.323$, $P < 0.01$) with R Square change statistic of 0.006). The negative sign of the interactive term means that higher levels of moral reasoning are associated with lower slope of enforcement behavior of informal contracts on social capital. In other words moral reasoning significantly moderates the social capital to enforcement behaviour relationship. The social capital to enforcement behaviour is strongest in the case of low moral reasoning and weakest in the case of high moral reasoning. Consistent with H6, model 7, demonstrate that the interactive term between organizational amnesia and moral reasoning is significant and negative ($\beta = -0.290$, $P < 0.01$) with R Square statistic of 0.453, $P < 0.01$) and $\Delta R^2 = 0.003$. The negative sign reveals that higher levels of moral reasoning are associated with lower slope of enforcement behavior on organizational amnesia.

VI. POLICY, MANAGERIAL AND RESEARCH IMPLICATIONS

Taken together our results offer strong support for the main and interaction effects of social capital, organizational amnesia and moral reasoning on the enforcement behaviors of informal contracts in Ugandan buyer-supplier business arrangements supporting H2, H3 and H6. A consistent body of research has tested and found a positive main effect of social capital on performance outcomes and behavior (e.g. Munene, 2004; Bourdieu, 1985; Coleman, 1990; Perry-Smith and Shalley, 2003; Podolny and Baron, 1997). However, in this study we obtain social capital effects which are exactly the opposite of what is commonly celebrated in literature. As social cohesion increases, social capital is made available to SME managers who use it to breach contractual obligations or defraud buyers/suppliers. The study has established that organizational social capital can be a liability to SME contracting partners. SMEs use social capital to engage in behaviors that compromise and/or frustrate the performance of informal buyer-supplier contracts. This finding lends credence to the research work of Ntayi et al., (2010d) who revealed a significant positive effect of work place social cohesion on unethical procurement behavior. This is supplemented by additional information from interviews which revealed that employees of the SME supplying firms collude to supply goods of questionable quality, delivery schedules are intentionally not adhered to, continuous and smooth supply from suppliers are almost non-existent. This business practice which result from the SME social capital has led to distrust among business partners. It is not uncommon today to hear terms like "kiwani" and "beleges" among the Ugandan business community, which literally means "a consistent lying culture" and "delivering fake products" respectively. The above coined words are reflective of the Ugandan SME ethical environment.

The findings of this study have policy, theoretical and research implications. First, a vast body of research emphasizing the positive effects of social capital has continued to dominate literature, largely ignoring its negative effects in business transactions. This has tended to create an impression that social capital is generally associated with positive effects. This study attempts to use data from SMEs in Uganda to demonstrate that social capital produces negative outcomes too. Further, the study points to the fact that there exists a form of negative social capital which operates to facilitate unethical business behavior associated with performance of contractual obligations. Despite this finding, the authors acknowledge that, there is inadequate conceptualization and empirical works under which social capital increases unethical business

behavior. Therefore, there is need to conduct more empirical studies to confirm the type of social capital and the conditions under which it promotes negative outcomes. One possible starting point would involve using theories from criminology literature to explain how social capital is generated and utilized in fostering unethical behavior in business transactions. This is supported by the Ugandan integrity survey reports which have revealed presence of widespread organized white collar crime. Secondly, the study reveals that as social capital increases, the effects of organizational amnesia and moral reasoning on enforcement of contracts is increasingly negative. This state of affairs increases transactional costs of SMEs as enforcement of informal contracts becomes a night mare. Another major implication of this study is that SME managers need to develop an ethical workplace culture and ethical rights which protect employees, buyers and suppliers from breach of contractual obligations (Barnard, 1950; Drucker, 1993). This is likely to promote productive social capital. Additionally, government through ministry of finance, planning and economic development, small business unit can design a strategy of developing small businesses through training and offering incentives to companies that keep records. Offering tax holidays to all new companies for a period of say five years may promote positive social capital, increase moral reasoning and reduce organizational amnesia. These initiatives can easily be interpreted as respecting SME owner managers, eventually resulting into improved and productive moral managers. A negative relation between URA and SMEs is a source of frustration, negative social capital and decreased moral reasoning of the SME managers. Respondents revealed that Uganda government does not offer any visible support to new SMEs. Government's selfish interest is to collect taxes from the resource constrained SMEs.

SMEs owner managers revealed that most of their businesses are established and financed using hard earned savings. This therefore means that, subjecting SMEs to taxation while in their infancy renders them operationally weak and unable to survive in the long run. This study establishes a link between government actions and the low moral development of SME buyers and suppliers. Government actions and/or policies are responsible for shaping an SME work environment that undermines moral development and judgment. The observed negative social capital, increased organizational amnesia and low moral reasoning, is a response mechanism by SMEs to balance government pressure directed at resource suffering SMEs to conform to statutory requirements. Over 89% of the respondents retorted that "it is unreasonable to expect government to reap and/or harvest from a newly started business". The government's requirement for all SMEs to register and pay their taxes electronically, comply with pay as you

earn regulations, and pay the compulsory SME worker contribution of 10% to national social security fund is unreasonable. This attitude explains the absence of business records in SMEs which has been previously attributed to a competence gap. Such a business culture burdens the process of assembling evidence, tedious and time consuming during contract enforcement process by courts of law. The inability to recall memory by SMEs is a characteristic of their history.

The study further revealed a dismal 25 or below, scores commonly associated with Kolberg's pre-conventional stage of moral reasoning characterized by a view that right behavior means acting in one's own best interests. This self-interest promotes non-compliance because of the belief that procurement officers will be much happier if they save their relatives/friends, even if they will have to serve a prison sentence. Results further revealed that 7% belonged to the third stage of conformity which encourages stealing/cheating and being engaged in all sorts of unethical conduct, because our friends/relatives expect it; if we want to be good to friends and relatives. This study has implications for SME managers and owners that want to develop their businesses through value driven interaction with suppliers. Those SMEs that want to avoid potential ethical problems may select those employees who are high in moral reasoning, as they are just as likely to be successful without compromising moral values. We need to improve the moral reasoning of SME employees. Secondly in order to achieve this goal, SME managers may want to use measures of moral reasoning as pre-screening criteria in situations regarding the hiring of new employees. And finally, managers and firm owners may want to investigate employing ethical training interventions designed to improve the ethical reasoning of their existing employees.

VII. CONCLUSION, LIMITATIONS OF THE STUDY AND DIRECTIONS FOR FUTURE RESEARCH

An important conclusion for this research is that SME social capital highlights negative aspects of social relations at work. Such behavior is consistent with Bartel and Saavedra (2000) and Godard (2001) who found social capital to be associated with abuse of managerial power. Results from critical incident analysis revealed that moral reasoning can be lost in the event of repeated resource constraints, social interactions and social learning. Intentional acts that harm or disadvantage one or more others like cheating are a reflection of low moral reasoning. Organizational socialization and acts of dishonesty, and discouragement which do not favour contract enforcement behaviours are linked to reduced moral reasoning. Similarly some pro-social behaviour of helping an SME business to successfully evade taxes,

not to follow business rules and regulations and encouraging are linked to low moral reasoning of SMEs.

This study has weaknesses that severely limit interpretation of results. The cross-sectional nature of the data limits inferring causal linkages between social capital, organizational amnesia, moral reasoning and enforcements of contracts. Additionally, this study concentrated on organizational social capital, ignoring buyer-supplier social capital which needs to be studied to get a balanced view of how the study constructs affect contractual arrangements.

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