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## IMPORTANCE OF IMPLEMENTING THE GREEN ECONOMY CONCEPT AND ITS IMPACT ON FINANCIAL PERFORMANCE OF AN ENTERPRISE

### Abstract

*In the modern business environment, sustainable development is largely achieved through the implementation of the concept of the green economy, both at the global and national as well as at the corporate level. The motive for the application of this concept at the level of enterprise can be found in the numerous benefits and positive business experiences of companies that have already decided to take that step. Although there are different opinions regarding the character and direction of the following relation, it is stated that the most important reason for implementation of this concept is possible positive correlation with achieving financial performances and competitive advantage of the enterprise-implementator. One way of understanding this influence is through monitoring the implementation of environmental strategy, or through monitoring the process of environmental performance and social responsibility performance management.*

**Keywords:** green economy concept, environmental performance, social responsibility performance, economic performance

**JEL Classification:** Q50, Q56, O44

## ЗНАЧАЈ ПРИМЕНЕ КОНЦЕПТА ЗЕЛЕНЕ ЕКОНОМИЈЕ И ЊЕГОВ УТИЦАЈ НА ПОСЛОВНЕ ПЕРФОРМАНСЕ ПРЕДУЗЕЋА

### Абстракт

*Концепт зелене економије је у савременим условима пословања виђен као врло значајан инструмент постизања одрживог развоја, како на глобалном и националном, тако и на корпоративном нивоу. Мотив за примену овог концепта на нивоу појединачног пословног субјекта може се тражити у бројним предностима и позитивним искуствима испољеним кроз пословање оних компанија које су се већ одлучиле на тај корак. И мада постоје различита мишљења на тему карактера и смера њиховог односа, ипак се као најзначајнији разлог примене овог концепта наводи његова могуће позитивна корелација са остваривањем осталих пословних перформанси, односно остваривањем значајних побољшања у погледу економских резултата и конкурентске предности предузећа имплементатора концепта. Један од начина за сагледавање тог утицаја је кроз праћење процеса остваривања еколошке стратегије, односно путем праћења резултата процеса управљања еколошким и перформансама друштвене одговорности предузећа.*

**Кључне речи:** концепт зелене економије, еколошке перформансе, перформансе друштвене одговорности, економски резултати пословања предузећа

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## **Introduction**

The survival of the modern business world can only be seen in drastic changes in the current way of doing business, by switching to the concept of sustainable development. The adoption of its idea at all, but especially on the level of individual enterprises, is greatly helped by an implementation process of a very similar concept - the green economy. Through accepting the basic principles and messages of both of these concepts in the everyday business activities, the enterprise achieves multiple uses and benefits, which is more than enough reason to continue to foster this new philosophy in the future trends of its business.

The green economy concept and environmentally responsible way of doing business mean understanding different relations between enterprise and the environment, as well as an altered view on the performances along achieved. Summarized, all of this can affect the final business results, which means that there is a need for a very detailed and precise examination of the very nature of these relations. Monitoring these relations can be made indirectly, through social responsibility performance, or directly, through environmental strategy implementation process. Since the functioning of the company is conditioned by some other factors as well, it is necessary to also include their impact in the entire analysis and to assess its possible consequences.

Therefore, in this paper, the focus will firstly be made on identifying all the relevant advantages and benefits that can be obtained by applying the green economy concept in an enterprise. Secondly, the paper captures the most important among them - the potential positive impact of such action on the financial performances of the company. This correlation is analysed through the business, so therefore also an environmental performance management process.

### **The advantages of using the green economy concept on the enterprise level**

As a concept, and by those who were promoting it, the green economy was being mostly explained through a number of its advantages and benefits that can be offered to the modern world. Thus, numerous publications and guides created by UNEP have characterized green economy in the following way:<sup>2</sup> green economy recognizes the value of natural capital and invests in this area; it is the key lever in poverty reduce; this concept creates a business with environmental elements that promotes social equity; thanks to green economy the use of fossil fuels is increasingly substituted by renewable energy and clean technologies use and finally, that this concept promotes resource and energy efficiency.

Similar is the view of green economy benefits in terms of its corporate implementation, through environmentally responsible way of doing business. The observance of sustainability principles and environmental responsibility introduction to everyday business actions of an enterprise can make savings on many levels, so that in a very short period of time, some former costs can slowly transform into cost savings and profit (e.g. waste as a source of income). This approach usually means higher interest of employees and other stakeholders, and their greater willingness to engage in the business of the company and create the best possible results from it. Eco-design of products and services contributes in attracting new customers, opening new markets and providing

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<sup>2</sup> UNEP (2011) *Towards a Green Economy: Pathways to Sustainable Development and Poverty Eradication - A Synthesis for Policy Makers*, <<http://www.unep.org/greeneconomy>>

greater visibility among other participants in the industry or on the market. Therefore, the process of “greening” means new challenges for the enterprise, the greater degree of its innovation and improvement of its flexibility, as well as a closer cooperation with all of its partners along the entire supply chain. All this inevitably leads to creating competitive advantage for an enterprise and to its better economic results.

Another list of potential green economy benefits can be found in the work experience of some experts in this field. According to one of them, Stefan Doering, the benefits of the green economy concept implementation for the enterprise are following:<sup>3</sup> increased volume of sales due to the increased demand for “green” products; less price sensitivity of these new products, which is why sales growth is also recorded in the future period of time; good business opportunities for the enterprises in the energy consumption field, the field of “green” technology use, training and consulting, environmental design, etc; greater publicity and competitiveness, greater customer loyalty and its impact on the business stability, strong support for the community and reduced impact on price changes. The named author is a founder and owner of BEST Coaches, a company that has been involved in providing advice and practical training for managers in the “green” companies management process since 1988.

So, green economy is an approach that can bring many benefits to the company that is implementing it, but only if done in the right way.<sup>4</sup> Therefore, following part deals with the analysis of all the possible effects of the green economy implementation in the company on its financial performances and its final business results, which is the most important benefit that this concept can give to one enterprise.

### **Impact of environmental performances on financial performances of an enterprise**

Probably the most important advantage and a great motive for an enterprise to choose environmentally responsible way of doing business and to implement the green economy concept, are potentially positive impacts of such actions on its business performances. This mainly refers to its financial performances, which can also retroactively affect the achieved level of environmental performances, as well as social responsibility and sustainable development performances in general. Since environmental responsibility is part of corporate social responsibility, relation between environmental and financial performances should first be considered through social responsibility performances, after which can the ecological-economic aspect of the business alone be separated and analyzed.

### **Understanding the relation between social responsibility performances and financial performances of an enterprise**

Namely, whether there is or not, and what kind of the relation between social responsibility performances and financial performances exists, were and continue to be many dilemmas and researches. Some authors<sup>5</sup> found that the social responsibility

<sup>3</sup> Doering, S., *It's UnReasonable to Be a Green Entrepreneur*, Best Coaches Inc, преузето 2012. године, <http://bestcoachesinc.com/>>

<sup>4</sup> Metz, B 2010, *Controlling Climate Change*, Cambridge University Press, England, pp. 5-7.

<sup>5</sup> Klassen, R. D. & Whybark, D. C (1999) 'The impact of environmental technologies on manufacturing performance', *Academy of Management Journal*, Vol. 42, No. 6, pp. 599-615.

performances negatively affect financial performances of a enterprise. This is because the enterprise that fosters socially responsible approach to its operations must also carry out a significant investment in the area, in order to strengthen its social responsibility performances. This in turn means pulling its resources back and turning management's attention from the key business areas. When because of this expected results fail, not only that the company will not achieve the expected competitiveness on the market, but it also won't be possible to have further realization of the social dimensions of the business. As a final result, the enterprise will be facing a drastic reduction of profits and growth of costs on the long term.

There are opinions that the relation between these performances does not exist,<sup>6</sup> or it is difficult to determine it due the complexity,<sup>7</sup> and the opinions that it depends on the size of the enterprise.<sup>8</sup> Thus, in case of larger companies and due to their greater involvement in the life and work of the community in which they operate, as well as due to higher level of their social responsibility, these companies achieve better economic performance. Smaller ones are concerned about the possible negative effects of investing in the social responsibility, which is why the positive economic effects, present in larger companies that do, are absent.

However, there are more and more of those who believe that socially responsible enterprises are making greater financial results, and that the social responsibility performances are actually their financial drivers. Positive effect is mutual, so the financial performances are drivers for social responsibility performances, but it is also possible to speak about their interactive relationship.<sup>9</sup> When these views are added to previous ones about their negative relationship, the following list of differentiated reviews is made:<sup>10</sup>

1. financial performances can be positively or negatively affected by the social responsibility performances;
2. social responsibility performances can be positively or negatively affected by the financial performances and
3. social responsibility performances can positively or negatively affect the financial performance of the company while the same time financial performances can positively or negatively affect the social responsibility performances.

The reason for so many different, often conflicting views regarding the above ratio is the fact that during the consideration of their relationship, different categories of financial performance are observed (profit margin, profitability of overall funds, profitability of own funds), but more importantly, but more important is the problem unique social responsibility performance inclusion. The main problem actually is, the

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<sup>6</sup> McWilliams, A. & Siegel, D. (2000) 'Corporate social responsibility and financial performance: correlation or misspecification?', *Strategic Management Journal*, Vol. 21, Issue 5, pp. 603-609.

<sup>7</sup> Margolis, J. D. & Walsh, J. P. (2003) 'Misery loves companies: rethinking social initiatives by business', *Administrative Science Quarterly*, Vol. 48, No. 2, pp. 268-305.

<sup>8</sup> Fauzi, H, Mahoney, L. & Rahman, A. A. (2007) 'The link between Corporate Social Performance and Financial Performance: Evidence from the Indonesian Companies', *Issues in Social and Environmental Accounting*, Vol. 1, No. 1, pp. 149-159.

<sup>9</sup> Carroll, A. & Buchholtz, A. K. (1996) *Business & Society – Ethics and Stakeholder Management*, South-Western College Publishing, Ohio, pp. 60-65.

<sup>10</sup> Oshika, T., Saka, C. & Oka, S. (2012) 'Why It Pays to Be Green? : An Empirical Investigation of Carbon SBSC', *Seeds of inovation*, American Accounting Association, Washington, pp. 4-11.

inability to quantify the aggregate performance of social responsibility in the form of a single performance measure of social responsibility.<sup>11</sup> The existence of such term would allow easier understanding the problem of relationship between these performances, so the unique opinion on the matter whether the impact is positive or negative and which is the direction of it, would be differentiated among most authors and researchers.

This paper adopted the viewpoint that there is a two-way correlation between the social responsibility performances, therefore environmental performances as well, and financial performances, which ultimately underscores the importance of the green economy concept implementation and the idea of sustainability on the corporate level. Sustainability performances of the company mean simultaneously achieving success with all of the mentioned goals: social, environmental and financial. The establishment and proper understanding of the links between sustainability performances, competitiveness and business success, makes possible having the insight about social role of an enterprise and helps the management to find adequate ways for managing corporate sustainability of their market and profit oriented enterprise.<sup>12</sup> This means that non-market dimensions, such as social or environmental ones, have a significant impact on competitiveness and business success (financial performances) of an enterprise.

In fact, willingly performing all the social and environmental activities aimed at improving the social and environmental performances, the company realizes its social responsibility performances. Managing these aspects of business, along with the key business activities management and appreciation of external and other factors, has its results in a form of certain level of competitiveness, which ultimately affects the financial performances of the company. Non-market business components may thereby have a direct impact (e.g. through production costs) or indirect, by realizing the overall sustainability performances and their impact on the competitive position of the company. The achieved level of financial performances, depending on the level of retained or accumulated profits and investments in environmental and social projects made from the accumulation, in turn influences the future level of social responsibility performances,<sup>13</sup> so it is very important to effectively manage both, market and non-market dimensions of the business. This is confirmed by the cases such as the one where the Shell company in 1995. wanted to sink its Brent Spar oil platform,<sup>14</sup> or when the Nike company in 2001. recorded the drop in its sales due to the pressure of non-governmental organizations regarding allegations that its suppliers use child labor in the manufacturing process.<sup>15</sup>

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<sup>11</sup> Krstić, B., Đorđević, S. (2011) 'Uticaj performansi društvene odgovornog poslovanja na finansijske performanse preduzeća', *ICDQM 2011 – Upravljanje kvalitetom i pouzdanošću*, DQM, Prijevor, str. 130-133.

<sup>12</sup> Schaltegger, S. & Wagner, M. (2006) *Managing and Measuring the Business Case for Sustainability - Capturing the Relationship between Sustainability Performance, Business Competitiveness and Economic Performance*, Greenleaf Publishing, Germany, pp. 3-7.

<sup>13</sup> Krstić, B., Vučić, S. (2004) 'Merenje ekoloških performansi preduzeća', *Ekonomске teme*, Vol. XLII, No. 4, str. 112-114.

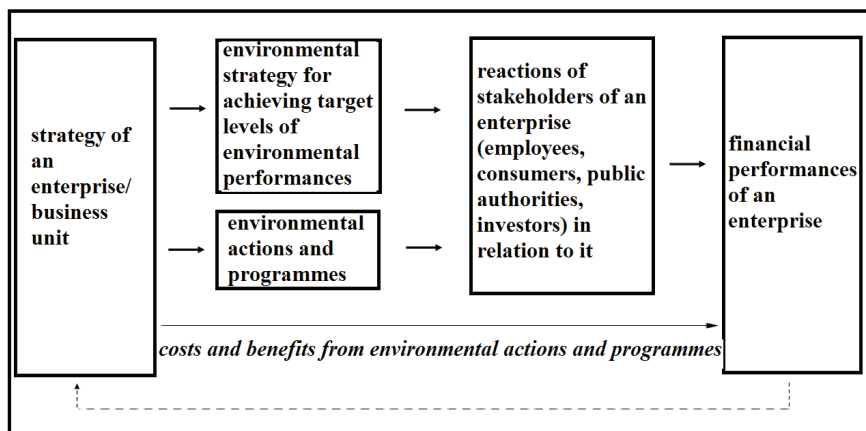
<sup>14</sup> Greenpeace (2011) *1995 - Shell reverses decision to dump the Brent Spar*, <<http://www.greenpeace.org/international/en/about/history/Victories-timeline/Brent-Spar>>

<sup>15</sup> Boggan, S. (2001) *Nike Admits to Mistakes Over Child Labor*, Common Dreams, <[www.commondreams.org/headlines01/1020-01.htm](http://www.commondreams.org/headlines01/1020-01.htm)>

## The impact of environmental strategy on financial performances of an enterprise

It has already been pointed out that an important element of strategy of the enterprise or business unit is environmental strategy, which accurately determines the ways and means of achieving the set of environmental objectives for the observed level (enterprise/business unit). This raises the question of economic viability and social feasibility of investing in the environmental aspects of business operations, or more precise, in the implementation of various environmental actions, programs and initiatives aimed to help the company achieve its planned environmental development (Figure 1).

Figure 1 - Environmental strategy, environmental performances and their impact on financial performances of an enterprise



Source: Krstić, B. (2012) 'Konceptualni okvir dizajniranja sistema merenja ekoloških performansi za kontrolu ekološke strategije preduzeća', Zbornik radova: *Nauka i svetska ekonomska kriza*, Ekonomski fakultet, Niš, str. 305-316.

Very often is operating in the ecological sphere in the enterprise associated with the costs or expenditures which are threat to current profits. This suggests a certain interdependence between environmental and financial performances of the company. First, it is necessary to emphasize that certain investments (spending, investments) in environmental programmes of the company are in the function of long-term, perspective growth of incomes, profit, business success and development.<sup>16</sup> Therefore, it is highlighted the importance of management actions in direction of proper routing of environmental actions, programmes and projects, and in a way that shows their company as environmentally responsible.

Through the accomplishment of dimensions of its environmental responsibility, the enterprise should also see its as well as the benefits therefore realized for all of the stakeholders, so because of that it is necessary that its management realizes how to manage actors and factors of environmental performances, how to identify measures and actions for their improvement and create supportive systems and structures for such improvement.

<sup>16</sup> Krstić, B. (2012) 'Konceptualni okvir dizajniranja sistema merenja ekoloških performansi za kontrolu ekološke strategije preduzeća', Zbornik radova: *Nauka i svetska ekonomska kriza*, Ekonomski fakultet, Niš, str. 305 – 316.



The involvement of businesses in the direction of preserving and improving the quality of the environment, results in increased motivation and productivity of employees, and the wider community is also pleased with enterprises with a higher level of environmental awareness. This is evident through their improved business reputation and increased corporate image, which, combined with the quality of products in the direction of their “greening” (healthy products, eco-friendly products, etc.) leads to increased satisfaction of its customers, their repeated purchases and profit growth for an enterprise on that basis. Finally, investors and financial analysts, as well as state authorities and its agencies are also interested in the environmental performances of the company. Thus, to the first mentioned group of stakeholders that information is needed in order to review the risks and justification of investing their assets in shares of the company, which in turn affects the reputation of the company and its market value. Satisfied investors and financial analysts mean lower overall risk and cost of capital for the company, and thus better chances in achieving enviable results in the future. And the state itself, on the other hand, highly values the efforts of company in the area of its environmental responsibility, which means better treatment for that business subject in terms when instruments of national environmental policy are acting. All of this means that by having its corporate actions in the environmental field, the company achieves an adequate response with its stakeholders, which in turn affects their cooperation, and the final business results as a product of that partnership.

Therefore, it is necessary that its management realizes the nature of the reaction that is produced by chosen environmental direction of an enterprise on time, and the possible effects of this situation on its overall business performances. This is the only way for enterprise to count on better integration of this important information in the daily process of business (including environmental) decision making, on the proper consideration of the possibilities of its further development, on creating environmental and business strategy for the next planning period, as well as on achieving positive feedback effect of financial on its future environmental performances in business.

However, no matter what the results of previous studies and confirmations of a number of authors in the issue of environmental and economic performances are, there are only few managers who actually succeeded to systematically analyze and manage these relationships through the end.<sup>17</sup> This is at the very least amazing, considering the fact that the very same environmental activities of an enterprise can be that crucial factor in achieving financial results in the contemporary courses of its business. However, validated practice examples of some of the world’s most successful companies, which have decided to “green” their own business and therefore have achieved remarkable, primarily financial results, speak in favor of the existence of these positive connections between the analyzed group of performances. Since this relationship is exactly what worries management the most, it is expected that such practical confirmation of its importance contribute to the increasing popularization of the green economy concept and to much greater corporate sector involvement in realizing the idea of sustainability in the future.

## Conclusion

Inclusion of the green economy concept in the daily operations of an enterprise, because of the numerous and serious environmental consequences of current business

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<sup>17</sup> Schaltegger, S. & Wagner, M. (2006) *Managing and Measuring the Business Case for Sustainability - Capturing the Relationship between Sustainability Performance, Business Competitiveness and Economic Performance*, Greenleaf Publishing, Germany, pp. 3-7.



system functioning, is increasingly taking on the character of precondition of its existence, the one that has no alternative. In addition to this inevitable, another reason can be found in all the other effects of environmentally responsible way of doing business, which depending on the success of the implementation of the concept, can bring multiple benefits to enterprise and the possibility of further progress in the business on all levels of the organization.

The essence and significance of implementation of this concept on the enterprise level just lies in the possibility of manifestation of all of the potential benefits of “greening” for an organization that is implementing it. Although there are very common opinions that the real connection between environmental and financial performances does not exist, analysed experiences of some companies that have decided to take this step showed that environmental responsibility can make significant improvements in the area of achieving financial results, all thanks to the fact that some cost savings or new sources of income can then appear, and generally the corporate image and market position for the company implementing the concept can be quite improved. However, the implementation of the green economy concept on the corporate level does not mean expressing the potential advantages of this concept by itself. This is due to many external and internal factors, as well as risk of incomplete or inadequate implementation of the concept.

Therefore, it is concluded that, between environmental and financial performances positive correlation does exist, and on all of the potential benefits of applying the green economy concept can count only those companies that approach this endeavor seriously and respecting the advice and experience from the field of its earlier implementation.

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