



Is sustainability a competitive advantage for small businesses? An empirical analysis of possible mediators in the sustainability–financial performance relationship

Silvia Cantele^{*}, Alessandro Zardini

Department of Business Administration, University of Verona, Verona, Italy

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ABSTRACT

The contribution of a single firm to sustainable development is largely dependent on the firm's perceptions of the advantages of sustainability strategies and consequent practices. The relationship between corporate social performance and corporate financial performance has been heavily debated, with mixed results.

Our research is aimed at defining a model in which sustainability practices affect firm financial performance via strategic drivers or antecedents of firm success. We used structural equation modeling on data collected via survey of 348 Italian manufacturing small and medium-sized enterprises. We included four constructs dedicated to sustainability, a construct dedicated to financial performance and four constructs measuring the possible mediators in the sustainability–financial performance relationship.

We found that the social, economic and formal practices dimensions of sustainability positively affect competitive advantage, mediated by corporate reputation, customer satisfaction and organisational commitment. We also found competitive advantage to be a second-stage mediator that positively contributes to financial performance.

The contribution of our study lies in having tested a new model of the sustainability–financial performance relationship, considering each dimension of sustainability and a path through different mediators in an under-explored context—that of manufacturing small businesses in a European country.

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1. Introduction

Stakeholder constituencies and global institutions are more and more requesting companies to be responsive and accountable, and this put increasing pressure to businesses to implement sustainability practices (SP), in order to contribute to sustainable development goals (United Nations, 2015). As a result, numerous opportunities have emerged to renovate business models towards sustainability (Bocken et al., 2013; Boons and Lüdeke-Freund, 2013; Rauter et al., 2015). These recent trends have been accompanied by long-lasting and lively debates in the literature about the meaning of corporate social responsibility and the motivations, pressures and effects of these practices on firms' performance.

Many studies have sought to demonstrate the 'business case for sustainability' (e.g. Dyllick and Hockerts, 2002; Schaltegger and Wagner, 2017) by testing the relationship between corporate

social performance (CSP) and corporate financial performance (CFP), with mixed results, yet a prevailing frequency of positive relationships is shown in meta-analysis (Margolis et al., 2007) or literature reviews (Lu et al., 2014). However, only a small number of previous studies were devoted to small and medium-sized enterprises (SMEs) (Hammann et al., 2009; Madueño et al., 2016). Sustaining the positive relationship hypothesis means arguing that the social responsibility of (small) business is not only an ethical vocation of enlightened entrepreneurs, but also a strategic decision leading to business success. This implies a need to rethink the sustainable development agenda, which could become a more widespread and desirable task—even for more sceptical, solely-profit-seeking organisations.

In light of relevant global, business and managerial implications, the challenge of this stream of research lies in answering questions such as: What kind of SP can really benefit firms and in which way? What operational and strategic intermediate goals enable a higher financial performance (FP) in sustainable business? This article presents a new model where the perceptions of sustainability and financial performance are put into relationship mediated by a two-

^{*} Corresponding author.

E-mail address: silvia.cantele@univr.it (S. Cantele).

level system of intermediate firm goals: customer satisfaction, reputation and organisational commitment (as measures of operational success), and competitive advantage that strategically leads firms to capitalise on FP. As previous studies have seldom introduced mediating factors between sustainability and financial performance, we decided to go deeper in the path of influence of SP on FP, considering that SP could first of all lead to enhanced operating conditions (customer satisfaction, reputation and organisational commitment – which are here called first-level intermediate goals), and then conduct to increased FP by the means of a second-level intermediate goal – which is competitive advantage – as an increase in profit could stem from higher revenues and/or lower costs resulting from cost or differentiation competitive strategies. We contribute to the extant literature by testing and validating this model in the context of small businesses, which are seldom considered in quantitative models of the effects of SP on FP. Our results indicate a positive influence of social, economic and formal practices of sustainability on competitive advantage and FP, through customer satisfaction, reputation and organisational commitment. This confirms the strategic relevance of sustainability in terms of competitiveness for small businesses.

The remainder of this paper is structured as follows. Section 2 is dedicated to the literature background, which is based on corporate social responsibility/sustainability streams, empirical studies on CSP-CFP relationships and sustainability in small businesses, and the consequent hypotheses definition. Section 3 is dedicated to the research design, with a description of the methods of data collection and analysis. Section 4 presents the analysis of the results and the discussion, while Section 5 is dedicated to conclusions and further research development.

2. Background

2.1. Corporate social responsibility and SP and their effects on firm performance

The term ‘corporate social responsibility’ (CSR) has been debated for many years, and there remains no real convergence on its meaning. From a literature review of CSR topics, Dahlsrud (2008) analysed 37 definitions of CSR and proposed a coding and relative frequency counting based on five dimensions relating to CSR: environmental, social, economic, stakeholder and voluntariness dimensions. These five dimensions are consistent with most of the theoretical frameworks in which CSR was developed, such as the corporate social performance (CSP) framework (Carroll, 1979), stakeholder theory (Freeman, 1984) and sustainable development concept (Brundtland Commission, 1987).

Carroll's model considers CSR a synthesis of different kinds of responsibilities—economic, legal, ethical and discretionary—while more general CSP studies have highlighted the need to consider the principles, processes and results of CSR (Wood, 1991). This managerial approach is consistent with the idea of CSR as a voluntary practice, rather than a moral obligation. The stakeholder theory contributes to the definition by clarifying to whom the firm is in fact responsible (Clarkson, 1995) and to highlight the instrumental and normative implications of the CSR approach (Donaldson and Preston, 1995). Finally, attention to the environmental, social and economic dimensions together recalls the sustainable development concept, which is traditionally defined as ‘Development that meets the needs of the present without compromising the ability of future generations to meet their own needs’ (Brundtland Commission, 1987). However, similar to CSR, the sustainable development term is a controversial concept that fosters debates and different interpretations. Hopwood et al. (2005) analysed three different approaches to sustainable development:

- ‘status quo’—whose promoters stress economic development as a solution to both social and environmental problems
- ‘reform’—which seeks changes to policy and regulation
- ‘transformation’—the most proactive approach, which promotes an active role of people who are outside of power centres (indigenous groups, people with low incomes, the working class and women).

All these approaches are coexisting, and perhaps the real challenge is not to convert all people to transformation, but to determine effective motivations for each approach in order to implement the sustainable development concept in practice. This raises a need to rethink sustainability in order to move beyond the traditional notions to include all emerging issues (Ramos, 2009).

In regard to businesses, sustainable development at the macro level should be transformed into sustainability management at the organisational level, beginning with the idea that firms should devote attention to all linked dimensions of sustainability (Lozano, 2008) and consequently measure their goals and performance with a triple bottom line (TBL) approach (Elkington, 1997), such as that proposed within the Global Reporting Initiative (Hussey et al., 2001). However, it is necessary to determine what could really push firms to embed sustainability in their practices at all relevant management levels, such as normative, strategic and operational management (Baumgartner, 2014). If the ethical driver proposed by traditional CSR and business ethics is not generally agreed upon—given its suspected contrast with traditional profit maximisation—the real challenge is to further demonstrate the business case for sustainability (Dyllick and Hockerts, 2002; Porter and Kramer, 2006) in order to persuade even the most sceptical supporters of the status quo.

Attempts to demonstrate the opportunities stemming from integrating sustainability into business have nurtured a long-standing stream of research devoted to studying the relationships between CSP and CFP. These studies began in the early 1970s (Bragdon and Marlin, 1972; Moskowitz, 1972) and have contributed to feeding a still lively debate that is synthesised in reviews (Griffin and Mahon, 1997; Margolis and Walsh, 2003; Wood, 2010; Wood and Jones, 1995) and meta-analyses (Margolis et al., 2007; Orlitzky et al., 2003). Recently, Lu et al. (2014) analysed 84 articles published between 2002 and 2011, and found that different results relating to CSP-CFP relationships might stem from different ideas and measurements of CSR. This highlights the need to use different ‘decomposition’ of CSP and CFP constructs, and that the enquiry should be linked to different institutional and business environments.

Previous reviews also highlight that the context of SMEs is under-investigated, as studies usually refer to large United States companies, and heavily used ready-made ratings (such as the old KLD rating) instead of measuring sustainability by the direct collection of firms' actual practices. Another relevant limitation is the lack of adequate investigations on the real path of influence, as possible mediator or moderator factors may have not been fully investigated yet (Cantele et al., 2015; Margolis and Walsh, 2003).

2.2. Sustainability in SMEs

SMEs are the prevailing form of business in Europe, where more than 99% of all companies are considered small (European Commission, 2016). The literature on CSR has usually depicted SMEs as organisations with peculiar features that differentiate them from large and multinational corporations (Jenkins, 2004). Among the relevant differences between SMEs and large companies, previous studies have cited the relevance of SMEs' entrepreneur/chief executive officer values (El Baz et al., 2016); SMEs'

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