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Business between Profitability and Sustainability



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Abstract

It has commonly been thought and said that the main goal of a company is to make profit and increase its value. If this is so, then the ways of achieving those goals are irrelevant. Are they really irrelevant?

We are witnesses of excessive depletion of natural resources, climate change and a loss of biodiversity. Water, air, soil, light and noise pollution is increasing. We are also faced with the ignorance of human rights and income inequality. At the end the quality of life is worsening as well. The need of paradigm change from profitability to sustainability is self-evident. Sustainability is an integrative, holistic and long-term approach that advocates balance between economic, social and ecological dimensions of business, making companies responsible not only for monetary, short-term goals, but also for people and the planet. It is a known fact that many companies are mightier than numerous countries. But let us not forget that the reverse side of might is responsibility. Companies which choose the path of responsible business publish sustainable reports that reflect their efforts in respecting social and ecological business dimensions.

Companies in Croatia accept this new understanding of business more and more. According to research results, they are aware of an increasing importance of social and ecological consequences of business, and the trend of sustainable reporting is on the rise. Top management has the most important function in implementing the sustainable company policy. Research shows that successful companies have a prominent role in pioneering the paradigm change.

The aim of the paper is to raise awareness of sustainability in business, to reaffirm everlasting values such as respect of human rights and nature, to share examples from a small country, and to stimulate benchmarking and cooperation between international researchers.

Key words

profit (ability), sustainability, economy of soul, Croatian companies, sustainable reporting

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1. Introduction

The present times are characterised by the search for harmony. The last century belongs to the era of quantity. The era of quantity is slowly being replaced by the era of quality. Harmony has three dimensions: harmony with ourselves, other people and with the environment.

Numerous pages have been written about profitability and different ways of achieving it. On the other hand, a lot of ink has been used to describe sustainability and its importance. Profitability encompasses a mono-dimensional perspective, monetary goals and a short term view, ignoring the consequences for society and the environment. Sustainability, on the other hand, is based on a holistic perspective, multi-dimensional goals and a long-term view, accepting the impacts of business activities on people and the planet. In this paper we want to explore the role of business between two opposite approaches, profitability and sustainability. With the results of empirical research we want to present the experience of companies in Croatia and stimulate wider research that could contribute to a shift in perspective from a mechanistic to a holistic paradigm.

2. Theoretical background

For decades profit has been, and often still is, accepted as the main business goal that has to be maximised. Profit is defined as "... the excess of the selling price of the article or service being sold over the cost of providing it" and profitability is defined as "...the capacity or potential of a project or an organisation to make a profit... It is the best known [measure](#) of [success](#) in an [enterprise](#)" (<http://www.businessdictionary.com/definition/profit.html#ixzz3SSg4XmTN>).

A strong influence on today's understanding of profitability was made by the American economist and Nobel Prize winner Milton Friedman (1970), who wrote that "The social responsibility of business is to increase its profits". Friedman argued that a company should have no 'social responsibility' to the public or society because its only concern is to increase profits for itself and for its shareholders and that the shareholders in their private capacity are the ones with social responsibility. Profit and profitability are still important and most common indicators of business success.

However, the most influential authors in the field do not agree on what business priorities are or should be. Michael Porter and his five forces analysis is a framework for industry analysis and business strategy development. He suggests industry-specific strategies for maximizing a competitive position and profitability. Jack Welch, one of the famous CEOs known as the youngest CEO at General Electric and author of several best-selling books, claimed that: "Productivity, efficiency, and profitability were the optimum words of the day." (<http://www.famousceos.com/profile-jack-welch-GE.php>) Still, it is worth noticing that neither author talks about the impacts that a business activity has on the environment.

In contrast, there are thinkers who are looking beyond profits. For example, Drucker (1993) says: "The first and easily the most common sin is the worship of high profit margins ...". Fredmung Malik (2007) argues that: "For business management the conception of profit maximization is completely unacceptable. The conception of profit minimization helps, the question how much we have to earn to stay in the business in the future?" Hermann Simon, a well-known author of the book *Hidden Champions* (1996) said: "The more successful you are, the more important it is to maintain humility and modesty... stay more a hidden champion." With his words Simon shifted away from profit and market share orientation, advocating human and ethical values. In *Corporate Social Responsibility* (2005), Philip Kotler, one of the world's foremost voices on business and marketing, and co-author Nancy Lee explain why charity is both good PR and good for business. Reinhard D. Sprenger as "Germany's most widely read management-author" (*Der Spiegel*) and "Germany's only management-guru, who really deserves this crown" (*Financial Times Deutschland*), pleaded in his book "Trust - The Best Way to Manage" (2004) that in business, nothing is more important than trust. No company can

prosper without trust between management and employees, among colleagues and partners, and between the organization and the outside world. Trust is the single most important issue in management today, and the basis for every truly successful company.

Klaus Schwab, Professor of Business Policy at the [University of Geneva](#) from 1972 to 2002 and Executive Chairman of World Economic Forum (WEF) said in his opening speech to WEF in Davos 2015: “We are here to improve the sustain of the world.“ In 1998, Schwab and his wife founded the [Schwab Foundation for Social Entrepreneurship](#), based in [Geneva, Switzerland](#). He is also the author of several books. Since 1979, he has published the [Global Competitiveness Report](#), measuring competitiveness not only in terms of productivity but also based on sustainability criteria. „More than ever, cooperative leadership among business, government and civil society is needed to re-establish sustainable growth and raise living standards throughout the world.“ (<http://www.weforum.org/reports/global-competitiveness-report-2014-2015>)

Global corporate power is constantly rising. One of the key ideas in the book *When corporations Rule the World* written by David C. Korten (2009) is that all political, economic and civil barriers to the free rein of corporate interests have been removed and the result of this unhealthy power in corporate hands is ecological destruction, the loss of civil freedoms, the erosion of democracy and community disintegration. In a research study released in December 2000 by Sarah Anderson and John Cavanagh of the world's 100 largest economic entities, 51 are now corporations and 49 are countries; according to their report from 1996 there were still 51 corporations out of the top 100 economies (<http://www.corporations.org/system/top100.html>)

With the process of globalisation came another important question: Who's more powerful – Governments or Corporations? According to Anderson and Cavanagh, “Two hundred giant corporations, most of them larger than many national economies, now control well over a quarter of the world's economic activity...Wal-Mart-the number 12 corporation-is bigger than 161 countries, including Israel, Poland, and Greece. Mitsubishi is larger than the fourth most populous nation on earth: Indonesia. General Motors is bigger than Denmark. Ford is bigger than South Africa. Toyota is bigger than Norway... The most alarming finding is that as corporate concentration has risen, corporate profits have soared, yet workers and communities are getting a shrinking piece of the growing pie. Figures from Business Week chronicle the explosion of corporate profits and CEO pay between 1990 and 1995 in the face of stagnating workers wages. The newest State of Working America by the Economic Policy Institute also reinforces our findings: median family income fell over 1 percent a year between 1989 and 1994 after four decades of expansion.” (<https://www.globalpolicy.org/component/content/article/221-transnational-corporations/47211.html>)

The rise of corporate power leads us to inequality and Thomas Piketty, Professor at the [Paris School of Economics](#), the author of the best-selling book *Capital in the Twenty-First Century* (2013). He addresses the problem of [wealth concentration](#) and [distribution](#), and [wealth inequality](#) which will increase in the future so he proposes redistribution through a [progressive global tax on wealth](#).

However, theorise of corporate power includes the rise of responsibility as a reverse side of business. The recent world economic crisis encouraged incentives to strengthen corporate social responsibility. Thus, in addition to profit as an (economic) value, the need for simultaneous compliance with legal and moral values, both at the individual and social level, is now emphasized more than ever before. Humans create value for each other, and “business” is the name we have given that process. (Freeman at al., 2008) Neither ethics nor regard for natural systems is typically central to the way we think about business. “In a similar way, environmental considerations are frequently viewed as barriers to profitability. They are viewed as necessary evils, costs to be minimized, or regulations with which to comply.... Models and theories of business traditionally have been silent on the subject of the environment. Silence, however, is no longer an option in the face of society's recognition of the potential environmental price of corporate profits.” (Freeman at al, 2008)

Maximizing profitability means at the same time ignorance of human rights and ignorance of the needs of future generations, thus reducing the quality of life and Life itself. There is already a discernible shift in popular attitude to favour improvements in the quality of life, opposed to amassing more quantities of assets, including money (Walter 1998). In fact; we are facing the change from economies of scale over economies of scope to economies of soul. Namely, a widespread idea of 'economies of scale', which includes increasing efficiency in the making of a product by producing more of it means that firms primarily focus on reductions in [average cost](#) (cost per unit) associated with increasing the scale of production for a *single product type*. Similarly, the concept of 'economies of scope' (Panzar & Willig 1981) refers to lowering [average costs](#) for a firm in producing *two or more* products. Nowadays, however, the business environment has undoubtedly changed. Therefore, the role of the companies has changed in that companies have become an indispensable part of social life. This has fostered the revitalisation of the concept of the 'economies of soul'. Actually, a soul economy is not a very new perspective. Tracing a seismic shift in American social thought, Jeffrey Sklansky (2002) wrote the book "Soul's Economy: Market Society and Selfhood in American Thought, 1820-1920" offering a new synthesis of the intellectual transformation entailed in the rise of industrial capitalism. As early as in 1922, Rudolf Steiner wrote the book "Soul Economy, Body, Soul, and Spirit in Waldorf Education", trying to integrate and to balance material and immaterial perspectives.

The Economy of the Soul means rational choice and moral decision-making. It means fair trade market and community. It means absence of child labour. It means respect for the people, animals, and Life in general. In short, it means balance between short- and long-term perspectives, balance between visible and invisible success. It is becoming obvious that a business does not have to damage the employee, the environment or nations. In addition, it is worth reminding ourselves that it is not business itself that is bad; it is an individual's greed. Business can be practiced with the heart and soul. Manfred A. Max-Neef, (2011) the winner of Right Livelihood Award in 1982 known as the Alternative Nobel Prize stresses: "And this entire crisis is the product of greed. Greed is the dominant value today in the world. And as long as that persists, well, we are done." Corporate ethics have been profoundly corrupted by the neoliberal cult of greed. In his provocative book "The Corporation - The Pathological Pursuit of Profit and Power" (and movie of the same title), Professor Joel Bakan (2005) argues that the corporation is like a psychopath. Bakan's book is a brilliantly argued account of the corporation's pathological pursuit of profit and power. He proposes a variety of reforms that he believes will restore the balance of power from corporations back to the people.

Looking at money and profitability as main business goals we are indeed facing the consequences of such mono-dimensional and very narrow view. Namely, there is a very high human and natural (environmental) price of corporate profit. The consequences of irresponsible business activities are shown in global warming, climate change, decrease in biodiversity, water, air, soil, light, noise, thermal and visual pollution (<http://www.sustainablebabysteps.com/kinds-of-environmental-pollution.html>) that we confront daily. It is therefore becoming obvious that we need a paradigm change. "Should a company aim at maximizing current profits? No! A company that is short-run profit-driven will not make long-run profits. The Navajo Indians are smarter. A Navajo chief does not make a decision unless he has considered its possible effects on seven generations hence." (Kotler, 2011)

As the opposite approach to the narrow-view of profit seeking and its broad consequences, there is sustainability as a holistic concept. Sustainable development has been defined in many ways, but the most frequently quoted definition is from Our Common Future, also known as the Brundtland Report (1987): "Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs. It contains within it two key concepts:

- the concept of needs, in particular the essential needs of the world's poor, to which overriding priority should be given; and

- the idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs."

Ensuring environmental sustainability is one of the eight Millennium Development Goals (MDGs) promoting integration, among other things, of the principles of sustainable development into country policies and programmes to reverse the loss of environmental resources (<http://www.un.org/millenniumgoals/>).

A sustainable development mindset includes a chain of new terms and activities: Ethical consumerism as the intentional purchase of products and services that the customer considers to be made [ethically](#), i.e. with minimal harm to or [exploitation](#) of humans, animals and/or the [natural environment](#). Ethical consumerism is practiced through 'positive buying' in that ethical products are favoured, or, 'moral boycott's negative purchasing and company-based purchasing, while green brands are products that identify themselves as ethical. Fair trade is an organized [social movement](#) and [market](#)-based approach that aims to help producers in [developing countries](#) to make better trading conditions and promote [sustainability](#). The movement advocates the payment of a higher price to producers, as well as higher social and environmental standards. Social Business and social enterprise are recent terms and fields, where Muhammad Yunus, deserves to be mentioned. He is a social entrepreneur, banker, economist and civil society leader who was awarded the Prize in 2006 for founding the [Grameen Bank](#) and pioneering the concepts of [microcredit](#) and [microfinance](#). These loans are given to entrepreneurs too poor to qualify for traditional bank loans. This shows us that there are alternative ways of finance. It is an example that not only profit counts, people are important too, especially poor people. Corporate social responsibility, corporate accountability, corporate citizenship, corporate sustainability, Triple Bottom Line, Global Reporting Initiative GRI, sustainable reporting, integrative reporting etc. are new terms within the framework of sustainable development.

The idea of sustainable development is becoming visible in sustainable reporting as well. For instance, P&L statement is a common obligatory company's report while a sustainable report is voluntary and focused on presenting the organization's performance in the wider context of sustainability. Sustainable reporting, integrative reporting, global reporting initiatives, triple bottom line and other similar reporting initiatives, principles and standards that integrate reports on financial, social and environmental business activities, have gained more and more attention recently and are becoming increasingly implemented as well.

It is obvious that social and environmental prices of business activities are very high. We have the right to require from companies to behave responsibly toward people, nature and planet as a whole. This brief theoretical background has illustrated the urgent need to shift the paradigm from profits as a mono-dimensional monetary business goal, to multi-dimensional and long-term business goals which ensure a balanced outlook and integrate economic, social and environmental aspects of business activities.

3. Business practice in Croatian companies

In our empirical research we have explored the orientation of Croatian companies, looking for the answer to the question where they are on the profit - sustainability scale. In this paper we are presenting institutional support to sustainability in Croatia and the results of several empirical studies, reflecting business priorities and sustainability.

Croatian Business Council for Sustainable Development, established in 1997 as a non-profit organisation, gathers 36 company members and collaborates with World Business Council for Sustainable Development – WBCSD. It promotes responsible and sustainable business through workshops, conferences and other events and activities. Together with the Faculty of Economics and Business Zagreb, and the Croatian Association for Sustainable Development (with 235 members) Croatian Business Council for Sustainable Development organised in 2014 the 6th National Conference on Social Responsible Business where eight companies of different sizes according to eight criteria got 'Index DOP' award for their sustainability activities and efforts.

Empirical research studies prove there is a shift in Croatian companies which apart from profitability, show social and environmental orientation as well (Osmanagic Bedenik et al, 2010). The sample of 900 companies (return rate 8.8%) showed that top business priorities in Croatia are reducing operative costs (74%), increasing sales (73%), remunerating claims (73%) and satisfied customer (72%), while environmental protection (41%) and society benefits (37%) are at the bottom of their priorities. The most frequent attitude can be described as follows: "We are focused on the economic aspect of business, even though we are aware of the social and environmental aspect" (33%). Companies in Croatia are aware of the benefits that the company obtains through promotion of corporate responsibility practices. That is why they gave the highest rate to brand strengthening (4.1 on the scale from 1-5) and strengthening company image and influence (4.1 on scale 1-5) as benefits arising from corporate responsibility practices. Croatian companies are mostly aware of the requirements of triple bottom line reporting and therefore adhere to it (47%) while 30% of companies in our sample are not familiar with triple bottom line reporting. Those results illustrate the slow process of reorientation of Croatian companies toward business responsibility and sustainability.

Applying the same methodology in the issue of how companies treat sustainability, we obtained results from companies in Austria, Greece and Poland, too. (Rausch et al, 2013) Satisfied customer (highest in Greece with 90%, lowest in Poland with 60%) and satisfied employee (highest in Greece 78% and lowest in Austria with 48%) are generally recognised as top priorities in companies. Similarly, in Croatian companies, the most frequent attitude toward CSR and sustainable development is the economic aspect of business, even though they are aware of the social and environmental aspects (in Austria it is 50%, and in Greece 23%). In all four countries the role of top management was recognized as the most important in implementing the sustainable company policy (rate for Croatia 4.9 as highest and 4.3 for Poland as lowest, on the scale 0-5).

The presented results reflect companies' focus on operational and financial business aspects, mainly short-term and monetary-oriented, although there is awareness of the need and importance of broadening the perspective toward its long-term, strategic and normative dimensions integrating social and environmental aspects. The top-management has the most important function in implementing the sustainable company policy.

In cooperation with International Performance Research Institute Stuttgart and other institutes from eleven European countries, we conducted research in Croatia in 2014 on sustainable reporting among top 50 companies selected according to the criterion of total revenue. Our aim was to explore the reality of sustainable reporting and to stimulate a wider use of it. According to our results for Croatia (Osmanagic Bedenik & Strugar, 2014) only 24% companies have a report on the social and environmental aspects of their business, and in 54% cases this information is available on the internet. Sustainable reports include on average 41.25 pages, ranging from 110 pages (INA) to 3 pages (Petrokemija). The most common sustainability-related topics, according to the volume of pages in reports, are employees (7.25 pages on average), followed by environmental aspects (6.5 pages). At the very bottom are human rights and anticorruption with only 1.83 pages on average. In the creation of sustainable reports five companies implement internationally accepted GRI standards, while the remaining even companies applied their own standards of sustainable reporting.

4. Conclusion

Current consumption and production levels are 25 percent higher than the earth's sustainable carrying capacity, according to the Ecological Footprint Sustainability Measure, an independent measure based on United Nations statistics. If everyone in the world were to live like an average person in the high-income countries, we would need 2.6 additional planets to support us all. (http://www.un.org/esa/sustdev/csd/csd15/media/backgrounder_brundtland.pdf)

Is business destroying our planet? With the primary orientation on profit and profitability, ignoring social damage to labour, human rights, product responsibility, local community and causing

environmental damage through energy, water, air, soil, biodiversity, effluents, emissions, etc. it seems that, yes, business does have a negative influence on people and the planet. Social and environmental prices for profitability are higher and higher. More and more authors and thinkers advocate humility, modesty, charity, trust, soul and spirit in business. We have seen that economies of soul are based on the reaffirmation of everlasting values. It seems that the biggest responsibility for that situation lies in international companies which are bigger and mightier than numerous national economies, so that they are the first ones to take adequate greater responsibility for our planet.

Companies in Croatia are focused on operational and financial business aspects, according to our empirical research, but they are slowly taking steps toward sustainability. They are aware of its importance, of its long-term goals, which is why they have started to implement sustainable reporting. Successful companies have a prominent role in pioneering the change in the quality of business and life as well. Top management is recognized to have the most important role in accepting and practicing principles of sustainability. The future of sustainable business and sustainable reporting therefore depends on the cooperation of enterprises, stakeholders and government bodies.

This paper contributes to the current debate on the role of companies, providing new insight into the responsibilities of companies and sustainable development. At the same time, it illustrates various aspects of sustainable reporting in Croatian companies. Our aim is to stimulate international cooperation between scientists toward a better world.

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