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RELATIONSHIP BETWEEN SUSTAINABLE ENVIRONMENTAL PRACTICES
AND SUSTAINABLE VALUE CREATION: A CONCEPTUAL STUDY ON READY-
MADE GARMENTS INDUSTRY OF BANGLADESH

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Abstract

Because of the increasing level of industrial contamination the demand for sustainable products and raw materials aligned with the ecological pollution has been on the rise in this horizon. This study theoretically explores the impact of sustainable environmental practices on financial performance of Ready-made Garment (RMG) companies of Bangladesh following the growing literature linking corporate sustainable environmental performance with revenue development and profitability. Various sustainable environmental practices have diverse effects on firm's performance, as the literature review suggests. From literature review this paper reports four key areas (community, employee, environment and governance) of sustainable practices for sustainable financial performance that would provide a useful and practical perspective on how companies can explore the sustainable agenda. Finally this paper concludes that companies should integrate environmental, social and governance issues to capture value in terms of revenue development and profitability for the companies. We recommend that the theoretical model that we have derived from literature review needs to validated and tested by future research.

Keywords: Community, Environment, Social, Governance, Financial performance, sustainable environment.

I. INTRODUCTION

Everything that is happening around us has an impact on environment. The same is true for our garments business and any other business as well. The traditional concept of doing



business “the activity of making, buying, or selling goods and services in exchange for money” no more exists, rather it encircles us with an obligation to do more for the society and environment in which we do and carry out our businesses. Business can no longer be viable without being responsible to the environment surrounding us. It is an indispensable part of any business that wants to maintain its existence in to-days global competitive business. This is also true for our readymade garment industry (coined as RMG in this paper), which has to embark on going green.

The RMG has achieved a strong footing in international market having 5% of the world apparel market share (Ahmed, 2015). This sector also has paved the way for women to come out of poverty as 3.6 million women are employed in RMG sector (Ahmed and Rahman 2015). The ready-made garment industry has been playing a significant role in the economic growth of Bangladesh. By providing direct employment to almost 4 million people –out of which over 80% are female workers, as is evidenced from 2014 report released by BGMEA (Bangladesh Garments Manufacturers and Exporters’ Association) This sector has, therefore, been instrumental in bringing women into labor force and has the potential lead in the social transformation of the country.

The number of factories increased almost 11 times from 1992 to 2014. As of 2014 there are in total 5615 units in 2012-2013 in the RMG sector of Bangladesh. (BGMEA, 2014). The sheer number of RMGs directly contributes to the increasing environmental impact caused by their activities. The pollution of air, soil and water is increasingly damaging the ecological system and this in turn may jeopardize the rate of financial growth of the companies.

In the past two decades the world has seen an increase in response to environmental factors as being part of a company’s strategy. In the RMG industry, the concern over sustainability is greater than ever. In addition to facing high-pressure competition, investors must increasingly pay attention to resource usage, waste treatment, air emissions, water pollution, employee welfare, and so on. Failing to manage these sustainability issues can substantially damage the image of the company and thus affect its performance.

Environmental sustainability in the RMG industry not only addresses environmental concerns about reducing the amount of energy and water used and minimizing the amount of waste produced, but also considers the financial benefits as cost savings and pays attention to social responsibility. We believe that in today’s dynamic and complex business environment, the environmental sustainability is likely to influence corporate value creation in terms of profitability and overall performance. It lays a foundation for preserving and enhancing value of firm. This paper takes into account the financial dimensions of the value creation. Thus, The purpose of this study is to examine the relationship between sustainable environmental practices and the firm’s financial performance in RMG industry sector of Bangladesh.

The study is justified for a number of reasons. First and foremost, since the independence of Bangladesh in 1971, there have been minimal efforts on the part of the previous governments



and the firms as well to address the environmental sustainability concerns such as water treatment, waste treatment, energy usage reducing the amount of energy and water used, minimizing the amount of waste produced, water pollution, air emissions, employee welfare, and so on. RMG industries face a major challenge on sustainability due to depleted energy, climate change, global warming, depleted natural resources, workers desiring better working conditions and better living. Secondly over decades the negligence of these concerns has left the RMG sector to capture and create value financially and socially. Finally the relationship between sustainable environmental practices and value creation is complex due to the intricate interplay between firm's performance dimensions and sustainable practices.

Not enough studies in the context of Bangladesh exist on the topic, so the present study, though theoretical in nature, will contribute to a better understanding of environmental factors that affect firm's financial performance dimensions in Bangladesh. Thus, this study constitutes an aid to the policy makers, researchers, and the government for improving various aspects of environment so companies can capture significant value by systematically focusing on sustainability.

II. LITERATURE REVIEW

The literature to environmental practices and its relationship to corporate value creation in regard to RMG industry is virtually non-existent. Even where it exists, a proper analysis of environmental issues impacting the financial performance of RMG is missing. We present a general literature review on sustainable environment and its impact on firm's value creation so we can derive a theoretical framework for RMG industry of Bangladesh.

The environment is a broad concept encompassing the whole range of diverse surroundings in which we perceive, experience and react to events and changes. It includes the land, water, flora, air and the whole gamut of the social order. It also includes the physical and ecological environment.

Arguably, without the environment there will be no society and without society, there will be no economy. The economy, therefore, depends on the environment, making environmental reservation and sustainability an obligation and a priority as well (Tullao et al, 2011)

In literature the concept of sustainability is described as "a development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (see WCED, 1987). Sustainability is a broad topic that can be viewed from many different perspectives, such as sustainable city, sustainable society, and so on. In this paper, the concept of environmental sustainability is referred to as Tripple Bottom Line (TBL), namely economic sustainability, environmental sustainability and social sustainability and seen as strongly connected to the concept of sustainable corporate value creation at the company level.

In his definition of TBL Elkington (1997) used the terms profit, people, and the planet as the three lines. The economic, social, and environmental lines are referred to as profit, people, and planet respectively, coined as 3 P's approach. However, different than TBL, some studies used



sustainability to primarily refer to the environmental line (Yan, Chen, & Chang, 2009).

The three P (planet, people, and profit) approach places an equal level of importance on each of the three lines; this brings more balance and coherence into the construct (Elkington, 1997; Epstein, 2008; Savitz & Weber, 2006). The 3P approach argues that a balancing act is needed between economic, social and environmental values. The relationship between these three aspects can be positive or negative. For instance, activities that create environmental values can have a negative or a positive influence on the financial sustainability of a firm. The subject of this paper is focused only on environmental sustainability practices in RMG industries and its relationship to company's value creation.

McKinsey Survey (2011) reports that if companies operationally assess sustainability along four major components such as employees, community, environment and governance, the companies would be able to create sustainable performance in terms of return on capital, risk management and growth, mounting to revenue development and profitability. Each of these components is discussed below:

a. Community:

A sustainable community is one that is economically, environmentally, and socially healthy and resilient. Ecologically environment must be able to re-generate, support bio-diversity and perform ecological functions that are essential to ecosystem health; Social equity means equitable rights for men and women, access to resources and participation in decision-making; economic aspects of sustainability allow people to sustain livelihood and meet basic needs. The interconnectedness of these three elements is stressed in the literature, especially the fact that environmental health and degradation are often directly connected to economic and social disparities (see Agyeman et al., 2002).

In the light of the above the Community Component consists of the company's commitment to the society in which it operates its business. This reflects company's citizenship, environmental social and economic impacts of company's products and services, product quality and safety and product sustainability.

b. Employee:

"sustainable workplace practices," means creating and maintaining a safe, healthy and functional workplace. Employees are the greatest assets of the company. It is widely accepted by both academics and practitioners that sustaining a safe, healthy and functional employee can become actively engaged in work and this employee engagement has a significant and positive impact on both the organization and the individual (Schaufeli and Bakker 2010).

Sustainable workforce practices may include employee carbon footprint, offering occupational wellness programs and stress-reducing strategies (e.g., nap rooms, on-site massages and stretch breaks), and providing wellness-related benefits such as on-site gyms. Maintaining a sustainable workplace also means minimizing external environmental impact—for example, by purchasing repurposed and recycled materials, minimizing unnecessary employee travel, and



reducing energy and water consumption, compliance with labor laws and regulation , respect for the workforce etc.

c. Environment:

Environmental sustainability is the rates of renewable resource harvest, pollution creation, and non-renewable resource depletion that can be continued indefinitely. If they cannot be continued indefinitely then they are not sustainable.

The environmental factors include environmental improvement, pollution prevention programs, resource management, waste management, climate change management, energy use , renewable energy, energy efficient operations, natural resource conservation etc. Our view is that environmental sustainability means corporate competitiveness and environmentally managed firms perform better financially. The thesis is that environmentally managed firms can attract more and more customers for them which, turn, results into more revenue leading to enhanced profits.

d. The Governance Component:

This component includes factors such as alignment of corporate policies and practices with sustainability goals; transparency to stakeholders, integration of sustainability principles from top down into day-to-day operations of company. Governance focuses on how management is committed to sustainability and corporate responsibility at all levels.

All the above components collectively are known as corporate social responsibility known as CSR. This refers to the accountability of company towards its effects on employee welfare, local community and environment and governance. Keeping the sustainability dimensions in view, we define sustainable performance as:

“The behaviors and actions of an organization toward community, employee, environmental practices and good governance across multiple financial dimensions such as return on capital, return on equity, revenue development, profitability in order to manage the risks and opportunities associated with economic, environmental and social developments” .

e. Sustainability and Firm's Performance:

Financial performance can be measured in terms of profitability, revenue development, growth in market share, and overall growth of the firms. Some measure profitability (return on investment, return on equity), some liquidity (quick ratio, current ratio), and still others solvency (gearing). Some measures are indicators of commercial success (growth, market share) while others are indicators of financial success (profitability).

Dow Jones (2010) defines corporate sustainability definition as a business approach that creates long-term shareholder value by embracing opportunities and managing risks deriving from economic, environmental and social developments. In its recently adopted Strategy 2020, Asian Development Bank (ADB) reaffirms financial sector development as one of its core areas of



operations in the coming years in support of inclusive and environmentally sustainable growth.

The focus on shareholder value relates to the impact of sustainable environmental practices on financial performance. Environmental management practices include cost reduction, revenue enhancement, reduction of liabilities, competitive edge, quality improvements, efficiency, more productive work force, and reducing business risks (Hart 2005; Orlitzky, et. al., 2003).

According to the McKinsey survey, companies should integrate environment, social and governance (ESG) issues into their business model to capture value in three key areas: Returns on Capital, Risk Management, and Growth. A relatively limited number of studies (for example, Wagner et al, 2001) found negative association between sustainable environmental practices and financial performances. They used return on sales, return on equity, and return on capital employed as financial indicators.

Baumol (1967) argues that the primary goal of many enterprises is some growth-related factor such as sales revenue, unit sales or market share. Similarly, many In this study financial performance will be measured by the firms are using profits a suitable indicator of financial performance as well.

Looking at the relationship between financial performance and environmental sustainability, one can argue that a firm, by being environmentally sustainable can differentiate its products and thus increase its revenue. Similarly, a firm can save costs on resources, regulatory costs, capital and labor and thus increase its profits. The increased societal attention towards environmental sustainability has resulted in an augmented consumer demand for products with a relatively low impact on the ecological environment.

There is a growing recognition that financial performance is strongly linked to sustainable business practices. Environmental, social and governance issues (ESG) are now an important consideration for investors and corporate managers. The reason is simple: a company that considers ESG an integral part of its operations and strategy is more likely to perform well over the long term, because it reduces risk and cost while increasing efficiency and competitiveness, as is evidenced from a growing body of literature (e.g., Doidge et al, 2001; Aysunn, F and Bluent , A , 2012; Klapper and Love (2002).

f. Development of Conceptual Framework

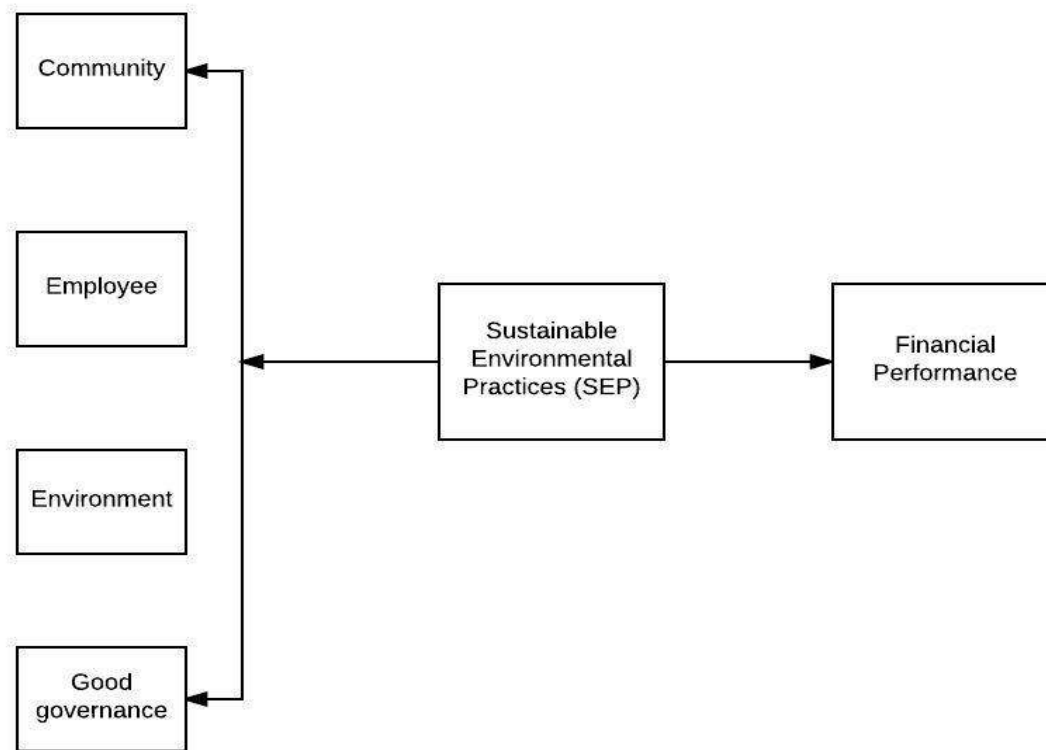
This study is designed to explore the relationship between sustainable environmental practices and financial performance of the firms. Following McKinsey Survey (2011) we report that if companies operationally assess sustainability along four major components such as employees, community, environment and governance, the companies would be able create sustainable performance in terms of return on capital, risk management and growth, mounting to revenue development and profitability, as depicted in figure 1. The four major components of sustainability and their operational definitions are depicted in Table 1



Table 1: Four sustainable dimensions and their operational dimensions.

Community	A sustainable community is one that is economically, environmentally, and socially healthy and resilient
Employees	Sustainable workplace practices," mean creating and maintaining a safe, healthy and functional workplace
Environment	This means environmental improvement, pollution prevention programs, resource management, waste management, climate change management, energy use , renewable energy, energy efficient operations, natural resource conservation etc).
Governance	This component focuses on how management is committed to sustainability and corporate responsibility at all levels

Fig. 1: Conceptual Framework



The above figure posits that sustainable environmental practices for community, employees, environment, and good governance will create sustainable value in terms of profitability, risk management and growth. Hope is that a better understanding of the key variables will advance our current literature in environmental sustainability. From managerial point of view it is a useful to help RMG managers design business strategy that will initiate and develop the practice of environmental sustainable activities in boosting profitability, managing risks and growth of the enterprises.



III. RESEARCH QUESTIONS

We formulate, therefore, the following research questions:?

- To what extent does a sustainable community enhance financial performance?
- To what extent does a healthy and sound workforce enhance financial performance?
- To what extent a sound and sustainable environment can affect firm's financial performance.
- To what extent good governance can affect firm's financial performance?
- Is there any overall significant relationship between sustainable environment and the firm's financial performance?

IV. CONCLUSION

This paper presents a general overview of the relationship between environmental sustainability and sustainable value creation and derives a conceptual model from the Literature review. Sustainable RMG should show a higher level of attention to the environment, social, and governance (ESG). Sustainable environmental practices are needed in order to support the growth of RMG industry. In this age of global competitiveness sustainable environmental practices will help RMGs stay competitive in global market. This research will provide information for managers and investors in RMG industry to gain an insight to practice sustainable environmental practices successfully. Secondly, It will provide knowledge and theoretical evidences for firms to ensure the success of sustained efforts.

V. RECOMMENDATIONS FOR FUTURE RESEARCH

The next stage of this paper is to test the reliability and validity of the model. The companies in RMG sector are privately-held companies survey. Probability is that they may not participate in the study. In that case questionnaire may be constructed to gather data on environmental sustainability practices they practice and the financial outcome (self-reported) for their companies out of these practices. Questions should be constructed using examples from scientific studies (Krajnc, and Glavic, 2003; Orlitzky et al., 2003). Surveys can help researchers to gather information from individuals about themselves or concerning the organizations to which they belong (Forza, 2002; Rossi et al., 2013). The survey is a very important method in the operations management field, especially in the case of theory development and theory testing (Forza, 2002). Since the 1980s, there has been a growing trend toward designing and executing surveys in operations management research (Rangtusanathan., 2003).

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