

THE TRANSFORMATION OF THE BUSINESS MODEL IN THE PROCESS OF THE TRANSFORMATION OF THE ECONOMIC SYSTEM ON THE ROAD TO SUSTAINABILITY: EUROPEAN PERSPECTIVE

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Abstract

This paper examines the transformation of the business model in the process of transformation of an economic system on the road to sustainability. The objective of the paper is to prove the transformation of the business model of companies in EU Member States due to the establishment of the new regulation framework on sustainability. The author's previous researches on corporate governance and sustainability, sustainable Global Value Chains and corporate sustainability,² as well her personal involvement in various consulting activities gradually determined the abovementioned topic of investigation. Although it was established that a limited number of scholars study the above phenomenon some findings in their publications have enabled the development of a conceptual framework of this paper. The first part the paper encompasses the results of the literature observation. The focus of the second part is on the EU regulation framework on sustainability. In the third part of the paper the transformation of the business model is analysed. Through the lens of good practice, some very interesting findings are revealed. The conclusion includes the findings of the study, the author's contribution and the path for the further study.

Key words: sustainability; business model, transformation; EU regulation framework on sustainability.

JEL: K2; M 160; Q580

Introduction

The topic under research is comparatively new for international business and management studies. Different schools of thought have investigated the changes in the business model determined by the economic, political and legal environment. It is worth to note that the innovation drivers, as well as digitalization, contribute to the changes in the “” internal environment “” of the company. In the last

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² Boeva, B. (2019) Capital, melting glaciers and 20C, Publishing House, Iztok-Zapad, S.

years environmental issues, resp. legal issues, respond to these challenges in the EU which lead to the transformation of business functions and the management of the companies. The objective of the paper is to communicate the author's findings about the impact of EU regulation on the sustainability of the business model as a system. It deals with the fundamental question: the balance between the state and market forces and the respective impact on the company. Views differ about the essence of the business model- from a model for planning, to a structure that encompasses the management, customers and suppliers and the objective- profit. This paper does not aim to kick off a discussion on what constitutes a business model. For the purpose of this publication the business model is considered a system with input and output and the respective changes are traced. Porter's value chain (productive and supportive operations)¹ suits this systematic approach to the business model.² The impact of the regulation on the transformation of the business model is examined through the impact on the input of the system (certain primary and supportive activities) and through the output (certain primary activities). The focus is on suppliers, customers and management. The thesis that the author defended is that the regulation on sustainability impacts the transformation of the business model. The scope of the research is the business model of EU listed companies³ and its respective transformation with regard to the requirements for sustainability and resilience. The research does not delve neither into the voluntary activities of business or the protection of the environment, nor into NGO activities. The author plans to examine how within the boundaries of a market economy regulators "design the business model." Armed with these views the author looks for theoretical support and evidence from practice.

Part one: How the research and the respective research strategy allow the author to provide solid arguments

1.1. Research strategy

As stated at the very beginning the problem perse is not new to the author. Previous publications on the purpose of the company, Business and human rights and the supply chain, comparative analysis on EU regulations and directives, as well on sustainable corporate governance have facilitated this research and publication. Naturally, more information is needed. An observation of academic publications, a survey on the most important events within the Green Deal- EU Regulation on

¹ Porter's value chain: primary activities: inbound logistics, operations, outbound logistics, marketing and sales and service; supportive activities: procurement, HR, technology and firm structure

² Certain K. Prahalad ideas about the organization were considered by the author

³ The information based on practice determined the above limitation.

sustainability; the examination of company documents, informal interviews, as well as personal experience are used.

About the research unit. In this paper the research unit is the company and its business model. As we see in STEM science, researchers in the domain of economics, business and management studies are venturing deeper into the substance (the Nobel prizes awarded in the last years reflect this view). As stated above the business model is analyzed from the perspective of the value chain (M. Porter's model).

1.2 Literature observation and discussion

The literature observation begins with a search in Scopus with a clear topic in mind – the transformation of the business model in the context of the transition to a net zero CO₂ economy. I reviewed 636 publications. The findings were somewhat disappointing: the focus of the papers was the transformation of traditional energy to green energy. My view about the transformation of the business model did not get the relevant support. Meanwhile other publications attracted my research interest. Chang (2020) reviews publications on sustainability and the business model and enables the view of many scholars on the parameters of the business model that prioritizes the sustainability objectives. The publication is a bibliometric study and its findings support a certain conclusion:

- the phenomenon “sustainable business model” is not defined. The author looks for publications and the parameters of the model
- according to the publications the focus on sustainability is on operations/ production
- the drivers of the transformation of the business model to a sustainable business model are not in the focus of the study

Another interesting finding ***on the sustainable business model is the publication*** of the BCG authors (Young, Gerard 2021). With regard to the objective of this paper, their view on the transformation of the business model (4 steps) should be underlined. The algorithm of the transformation is as follows: a study of the environment of the company - systematic approach; design of the model, testing and employing the new concept on how to run the company. Their concept rests on the examination of sustainability driven activities of companies on both sides of the Atlantic. The take away of this publication and the 4 steps model is as follows: a systematic approach and covering issues that are relevant to our study: the interplay between business and the government/lobbying activities); the transformation within the company and the transformations of the input (incl investments, suppliers) and on the output with a focus on the development of new competitive advantage: Sustainability

Aldowaish, A. J. Kokuryo (2022) research the integration of ESG into the business model of the companies. They review studies on the impact of ESG on competitiveness of the company incl. investment attractiveness, also on financial per-

formance. Their review of 326 publications shows only 29 publications on the interplay between sustainability and the business model. Their analysis of the above 29 publications sends a clear message- sustainability is related to the outcome/ exit of the company. What the authors do not clarify is their view about the business model and the drivers of the transformation of company business. The business model is made synonymous with strategy, operations; assets and advantages.

The two bibliometric studies, as well as the other publications under examination are helpful. The topic of the “inclusion of the sustainability in the companies” primary and supportive activities gradually gains momentum in the business and management studies. Although desk research strongly suggests that the study of the transformation is on the right path, the impact of the regulation on the business model is not covered. The observed publications do not facilitate the achievement of the objective of this paper.

2. Does the EU Regulation on sustainability impact the transformation of the business model of the companies?

Next step of this study is to answer the question whether regulation is one of the drivers of the transformation of the business model. I refer to regulations and directives with a strong impact on the business model: Taxonomy Regulation; Corporate Sustainability Reporting Directive (CSRD) and Corporate Sustainability Due Diligence Directive (CSDDD-draft).

The Taxonomy⁴ Regulation (JPMorgan 2021) sets clear conditions and objectives that the company has to meet:

- Condition I to meet objectives as follows: Climate change mitigation; Climate change adaptation ; The sustainable use and protection of water and marine resources ; The transition to a circular economy ; Pollution prevention and control; the protection and restoration of biodiversity and ecosystems climate change;
- Condition II to not significantly do harm (DNSH) with regard to above mentioned 6 objectives
- Condition III to meet the minimum of social safeguards

The Taxonomy Regulation (Taxonomy 2020) sets out not only objectives, but provides business with metrics to prove the achievement of these objectives. The metrics include information about the ratio of the turnover; capex and opex that prove that companies invest to mitigate negative climate change; that part of its operational expenditures and the products/ services supply support the mitigation of cli-

⁴ Taxonomy, a well-known term in the natural sciences is a “novelty” for the business area, finance and regulation. It is a scientific approach to codify businesses, that are aligned with the overarching goal of EU Member States – decarbonization and protection of the people and planet. This scientific approach plays a significant role for the politicians, policy makers, business, NGOs and communities for the elaboration of programmes, decisions and the mitigation of green was

mate change or climate adaptation. The metrics *per se* do not lead to the transformation of the components of the business model with a focus on input and output. But the objective and metrics impact the decisions for transformation. One of the respondents to the enquiry sends a clear message: “we have to think about changes in our activities.”⁵

The Taxonomy requirements direct the companies’ investment policies or “it is an industrial approach that aims at steering the company’s production structure via modifying financing conditions (Kooths 2022). “The new rules enable the companies to screen their investments; the operations and to assess how they contribute to the protection of the environment, human rights and good governance. The companies have to decide on how to invest; what activities to develop in order to build the new competitive advantage.

Bond and Dusik (2022) state that the Taxonomy sets a minimum standard for environmental performance. Although they do not provide arguments from the field, their position supports the thesis of the paper – sustainability regulations drive the transformation of the business model.

Irrespective of the fact that this article does not investigate the pros and cons of the Taxonomy regulation, it is noteworthy to point out the critics of the research. The balance between the market and regulation is broken. Taxonomy is a mission impossible (Kooths 2022) for companies that play on the playground of market economy.

Focus on the new (sustainability related) approach towards investments in the company can be found in the Regulation for the sustainability-related disclosure in the financial services sector (2019). At present the companies that are applying for investment support from the banks have to comply with this Regulation: they have to disclose their sustainable investment policy or to make sustainable investments.⁶ In a nutshell, on the input of financial resources many companies in EU

⁵ About 4000 large companies have started to disclose the implementation of the Taxonomy in their reports in 2023

⁶ sustainable investment’ means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance (Regulation 2019/2088

Member States are bound by different legal requirements and are forced to transform their business model.

This journey to providing arguments for the transformation of the business model requires a quick analysis of the *second most important* element of this framework: the **Corporate Sustainability Due Diligence Directive (draft)-CSD-DD**. The essence of the CSDDD is to make companies comply with the UN Guiding Principles on Business and Human Rights, as well with rules about the protection of the environment in their work with suppliers. It is well known that in 2017 the EU parliament passed another Regulation with the same objective but for the import of minerals from conflict zones (**Regulation EU) 2017/821**).

The new Directive (draft) will impact the general importing/buying policies of EU Member States companies with a focus on:

...”Identify actual or potential adverse impacts; Preventing and mitigating potential adverse impacts, Establishing and maintaining complain procedures Monitoring the effectiveness of their due diligence policy”” (article 4 CSDDD draft) The implementation of the due diligence procedure will impact the input of the business model. A number of companies report that they have initiated new alliances with their suppliers to ease the information flows from buyers to suppliers for the purposes of the due diligence process⁷.

The third component of the EU Regulation on sustainability is the CSRD/ Disclosure directive. The Directive and its transposition in local legal frameworks do not impact the business model directly. But the enlargement of the scope of disclosure (new reporting standards 12 ESRS⁸) will shed light on its activities and its results. Through the lens of sustainability reporting clients and consumers; investors, markets, community and stakeholders will screen the fitness of the company with regard to the Transformation Agenda of the European Union. Outside pressure will lead to inside transformations. There could be many examples of this: the standard regarding the climate, the standard regarding the consumers etc. The Directive via the market mechanism will make the companies transform various procedures and components of their business model. The above view is not new: for many years theories and practices have communicated the role of information and market signals/ feedback on the transformation of the company business model. CSRD poses the same imperative but with different content and again via market participants.

⁷ Statement of the ENI representative in EU issuers conference, October 2023; presentations on CSR Europe Conference October 2023

⁸ ESRS includes: ESRS1 General Requirements; ESRS2-General Disclosure; ESRS E1 Climate change; ESRS E2-Pollution; ESRS E3 Water and Marine Resources; ESRS E4 Biodiversity and Ecosystem; ESRS E5 Resource and circular economy; ESRS S1 -Own Workforce; ESRS S2 Workers in the Value Chain; ESRS S3 Affected Communities; ESRS S4 Consumers; ESRS G1 Business conduct;

Conclusion

The literature review does not support the thesis of this study. The business model used as a unit for investigation is not covered by the authors in the publications under observation. The transformation process is communicated by a limited number of research papers. The conceptual framework was partially supported by the brief analysis of the EU Regulation framework on the sustainability. The findings encourage further research activities: literature examinations, field researches and case studies, and approbation of the results with Bulgarian companies.

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business information

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