Chapter 18
The Effect of Environmentally Sustainable Practices on the Financial Performance of MSMEs in the Digital Age

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ABSTRACT

This study investigates the impact of Environmental Corporate Social Responsibility (EnvCSR) on the financial performance of Micro, Small, and Medium Enterprises (MSMEs), focusing on the mediating roles of organizational reputation and employee satisfaction. Using descriptive analysis, Pearson's correlation, hierarchical linear regression, and Sobel's Test, it explores how these factors influence financial outcomes. The findings reveal that EnvCSR significantly enhances financial performance, with reputation and employee satisfaction serving as key mediators. The study provides actionable insights for MSMEs to strategically implement CSR initiatives, prioritize impactful practices, and cultivate a culture of environmental responsibility.

INTRODUCTION

Microenterprises are firms with an investment in plant and machinery not exceeding One crore rupees and an annual turnover capped at Five Crore Rupees. Small enterprises have an investment limit of Ten Crore Rupees and a turnover of up to Fifty Crore Rupees. For medium enterprises, the investment and turnover limits are Rs. 50 crore and Rs. 250 crores, respectively (Ministry of Micro, Small and Medium Enterprises (MSME), Government of India. (Mitra, 2023). According to data provided by the World Bank, SMEs account for more than 90% of all enterprises and provide more than 50% of all jobs globally

(Algan,2019). The MSME sector accounts for around 30% of the country's overall GDP. Additionally, it generates employment for 11.1 crore people, accounts for 49.5% of the country's exports, and provides 45% of the nation's entire industrial production (Mitra,2023). Thus, it is apparent that MSMEs are essential to the nation's social and economic development, as they significantly increase inclusive economic growth, exports, and innovation.

But at the same time, it is polluting the environment. MSMEs have an enormous impact that cannot be ignored anymore, even while their contributions to environmental degradation are minimal (Eweje, 2020; Kariyapperuma & Collins, 2021). According to the studies (Caldera et al., 2022), MSMEs are to blame for more than half of all global pollution, 60% of GHG emissions, and more than 70% of discharges of industrial/commercial waste. This can be minimized by engaging in environmental CSR activities.

Economic, Social, and Environmental dimensions constitute CSR or sustainable development. The environmental dimension of sustainability has received more attention in current research than the social dimension (Lawrence et al., 2006), likely as a result of the contentious issues of global warming and climate change.

Due to the perception that big businesses were more likely than MSMEs to pollute the environment and owe more to the community and society at large (Courrent et al., 2018; Eweje, 2020). MSMEs, therefore, have lower adoption rates for environmental policies since they are less knowledgeable than large enterprises about sustainability challenges and the environmental repercussions of their operations (Boakye et al., 2020; Fleiter et al., 2012) .The environmental impact of their actions is overlooked because they are too preoccupied with ensuring their survival on a day-to-day basis.

Additionally, MSMEs encounter several difficulties when implementing environmentally sustainable practices, such as insufficient government assistance, laws (Lee & Klassen, 2008), and a lack of sufficient financial, technical, and human resources(Bakos et al., 2020). Although they are facing various challenges, many researchers in developed nations indicate various benefits that MSMEs can gain through adopting EnvCSR activities. Hence this study answers the question the question from an Indian perspective.

RQ1: What are the factors that influence an MSME to engage in EnvCSR activities?

Studies indicate that EnvCSR leads to the sound financial performance of an organization (Saeidi et al., 2015b). However, the impacts of EnvCSR on FP remain contradictory (Lioui & Sharma, 2012). Some studies found a positive relationship (Muchiri and Muigai 2019); some found a negative or no relationship (Agyemang & Ansong, 2017)(Lioui & Sharma, 2012). Studies indicate reputation mixed results with FP (Grewatsch & Kleindienst, 2017). Studies on this association can be strengthened via mediation, according to (Servaes & Tamayo, 2013) and (Galbreath & Shum, 2012). A few academics have attempted to elucidate the rationale behind the correlation between corporate social responsibility (CSR) and certain results.

For example, EnvCSR boosts enterprise performance through R&D (Lioui & Sharma, 2012), Innovation (Lioui & Sharma, 2012) competitiveness (Orij et al., 2021) and partnership restructure (Makhdoom et al., 2023). However, its relationship with business reputation and employee satisfaction is relatively under-researched (Yang et al., 2015). To address the issues, the research aims to study the impact of CSR on FP with a mediating role of reputation and Employee satisfaction in Indian MSMEs.

RQ2: Whether reputation and employee satisfaction mediate the effect of EnvCSR and firm performance.

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