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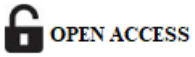

SUSTAINABLE BUSINESS PRACTICES AND THEIR EFFECT ON CORPORATE PROFITABILITY

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Abstract

This study examines the impact of sustainable business practices on corporate profitability by analyzing firm-specific variables such as firm size, growth, R&D intensity, productivity, liquidity, and leverage. Using secondary data, the study applies descriptive statistics, correlation analysis, and multicollinearity diagnostics to explore the relationships among these variables. The findings reveal strong positive associations between firm growth, R&D intensity, and productivity with corporate profitability, indicating that firms investing in sustainability and innovation are more likely to experience improved financial performance. Furthermore, the absence of significant multicollinearity among variables enhances the reliability of the regression analysis. The study concludes that sustainable practices not only contribute to environmental and social goals but also offer measurable financial benefits. These results have important implications for corporate strategy, investment decision-making, and policy formulation.

Keywords: Sustainable Business Practices, Corporate Profitability, Firm Size, R&D Intensity, Liquidity, Leverage, Productivity, Financial Performance.

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1. INTRODUCTION

In the rapidly evolving global economy, corporations face increasing pressure to not only achieve financial profitability but also demonstrate social responsibility and environmental stewardship. Traditional business models centered exclusively on profit maximization are giving way to more integrated approaches that recognize the long-term benefits of sustainability. As firms navigate this shift, factors such as firm size, financial structure, and sustainable business practices have come under closer scrutiny for their potential influence on corporate profitability. Understanding the complex interplay between these variables is vital for managers, investors, and policymakers seeking to optimize performance while aligning with modern ethical and environmental standards.

The size of a firm has long been considered a critical determinant of productivity and profitability. Larger firms often benefit from economies of scale, increased bargaining power, and better access to capital markets, which can translate into improved financial performance (Goddard, Tavakoli, & Wilson, 2005). However, increased size can also lead to bureaucratic inefficiencies, slower decision-making, and difficulty in adapting to market changes (Asimakopoulos, Samitas, & Papadogonas, 2009). Thus, the relationship between firm size and productivity is not always linear or straightforward and warrants a deeper investigation in various industrial and geographic contexts.

Parallel to the structural aspects of firm size, financial indicators such as leverage and liquidity also significantly impact corporate profitability. Leverage, or the extent to which a firm uses borrowed funds to finance its operations, can magnify returns on equity but also increases financial risk (Myers & Majluf, 1984; Titman & Wessels, 1988). High leverage can constrain a firm's flexibility, particularly in volatile markets, and potentially impair profitability if debt servicing becomes burdensome (Rajan & Zingales, 1995). On the other hand, liquidity refers to a firm's ability to meet its short-term obligations. While high liquidity ensures operational stability and reduces bankruptcy risk, excessive liquidity might suggest

underutilization of resources (Raheman & Nasr, 2007). Therefore, a balanced approach to both leverage and liquidity is essential for sustaining profitability.

In recent years, the integration of sustainable business practices has emerged as a vital strategy for long-term corporate success. Sustainability involves balancing economic, social, and environmental dimensions to create value not only for shareholders but for a broader range of stakeholders (Agudelo, Johannsdóttir, & Davíðsdóttir, 2019). Corporate Social Responsibility (CSR), Environmental, Social, and Governance (ESG) factors, and ethical business conduct are key components of sustainability that can affect brand reputation, customer loyalty, and operational efficiency (Kotsantonis, Pinney, & Serafeim, 2016; Vitell & Hidalgo, 2006). Numerous studies have investigated the correlation between sustainable practices and financial performance, often indicating that firms with strong sustainability profiles outperform their less responsible peers in the long run (Wu, 2006).

Despite a growing body of literature, the interaction between firm size, financial structure, and sustainability with corporate profitability remains underexplored, particularly in the context of developing economies. While studies in developed markets provide valuable insights, local economic structures, regulatory environments, and corporate governance practices may influence these relationships differently across countries. In emerging markets, where firms often face resource constraints, institutional voids, and rapidly shifting market dynamics, the adoption of sustainable practices may not yield immediate financial returns, creating a trade-off between short-term costs and long-term benefits (Shahnawaz, 2007).

Furthermore, the measurement and evaluation of profitability itself are complex, involving various accounting and market-based indicators. Profitability can be influenced by both internal factors—such as operational efficiency, innovation, and workforce productivity—and external factors—like market competition, government policy, and macroeconomic trends (Kessides, 1990; Markman & Gartner, 2002). Hence, isolating the impact of specific variables such as size, leverage, liquidity, and sustainability requires a rigorous analytical approach supported by empirical evidence.

The theoretical underpinnings of this study are grounded in stakeholder theory, agency theory, and resource-based view (RBV). Stakeholder theory posits that firms must account for the interests of all stakeholders, not just shareholders, and this broader accountability often leads to enhanced corporate performance (Freeman, 1984). Agency theory, on the other hand, highlights conflicts between managers and shareholders, suggesting that financial structures like leverage can act as control mechanisms to align managerial actions with owners' interests (Jensen, 1986). The RBV emphasizes internal capabilities, suggesting that sustainable

practices, if effectively embedded in a firm's strategy, can serve as a source of competitive advantage (Barney, 1991).

This study also considers the ongoing debate over the financial materiality of sustainability. While critics argue that sustainability distracts from core profit-making activities, proponents assert that long-term value creation depends on addressing environmental and social challenges (Kotsantonis et al., 2016). The empirical landscape reflects this divergence; some studies report a positive correlation between ESG initiatives and profitability (Wu, 2006), while others find neutral or even negative relationships, particularly in the short term (Hillman, 2005; Boubakri, Cosset, & Saffar, 2012). Given these multidimensional considerations, it is essential to adopt an integrated research framework that examines how structural and financial characteristics interact with sustainability to influence firm performance. Such an approach can uncover nuanced insights into how businesses in different contexts manage the dual objectives of profitability and responsibility.

1.1 Objectives of the Study

In light of the above discussion, this study is guided by the following objectives:

1. *To know the impact of firm size on productivity*

Understanding how the scale of operations influences a firm's output efficiency and overall productivity is vital for strategic resource allocation and operational planning.

2. *To study the influence of leverage and liquidity on corporate profitability*

This objective aims to assess how different financial management strategies, particularly the use of debt and short-term assets, affect firm profitability in diverse economic settings.

3. *To understand the impact of sustainable business practices on corporate profitability*

This includes evaluating whether the integration of environmental, social, and governance practices contributes to or detracts from a firm's financial performance over time.

2. REVIEW OF THE LITERATURE

2.1 Firm Size and Productivity

Firm size has long been considered a determinant of productivity and profitability due to economies of scale, resource availability, and market power. Larger firms often have more access to capital, advanced technologies, and diversified product lines, leading to greater efficiency (Goddard, Tavakoli, & Wilson, 2005). Moreover, they can spread fixed costs over a

larger output, reducing unit costs and improving profit margins. However, some studies argue that beyond a certain threshold, increasing firm size may result in bureaucratic inefficiencies, loss of control, and diminished innovation (Asimakopoulos, Samitas, & Papadogonas, 2009). Stierwald (2010) examined the heterogeneity of profits among large Australian firms and found that while firm size positively correlates with profitability, other factors such as management quality and market conditions also play significant roles. Similarly, Yazdanfar (2013) concluded that while firm size contributes to profitability among Swedish micro-firms, its impact varies by sector and age of the firm.

2.2 Leverage, Liquidity, and Corporate Profitability

The relationship between financial structure—particularly leverage and liquidity—and profitability has attracted considerable scholarly attention. Leverage, or the degree to which a firm uses debt in its capital structure, can potentially amplify returns on equity (Myers & Majluf, 1984). However, excessive leverage increases financial risk, especially in downturns, potentially leading to insolvency (Titman & Wessels, 1988; Rajan & Zingales, 1995). On the other hand, an optimal capital structure can enhance shareholder value and operational performance (Jensen, 1986). Raheman and Nasr (2007) analyzed Pakistani firms and found that higher leverage negatively affected profitability, suggesting that debt may be a costly source of financing in emerging markets. Liquidity, defined as the firm's ability to meet short-term obligations, also influences profitability. A high liquidity position ensures financial stability, yet excessive liquidity may indicate inefficient resource use (Samiloglu & Demirgunes, 2008). Asimakopoulos et al. (2009) further emphasized that maintaining a balanced liquidity ratio is essential for sustaining profitability.

2.3 Sustainable Business Practices and Corporate Profitability

Sustainable business practices—comprising environmental, social, and governance (ESG) factors—have become increasingly important in evaluating a firm's long-term success. These practices often involve adopting eco-friendly technologies, ensuring ethical labor practices, and maintaining transparent governance structures. The literature presents a growing consensus that integrating sustainability into core business strategies can enhance corporate reputation, foster customer loyalty, and ultimately improve financial performance (Kotsantonis, Pinney, & Serafeim, 2016). Wu (2006) conducted a meta-analysis showing a generally positive correlation between corporate social performance and financial performance, indicating that socially responsible firms tend to be more profitable. Similarly, Agudelo, Johannsdóttir, and Davíðsdóttir (2019) reviewed the evolution of corporate social responsibility (CSR) and found that firms with robust sustainability programs often experience improved stakeholder

engagement and risk management. Vitell and Hidalgo (2006) added a cultural dimension, showing how ethical values and enforcement of codes influence business ethics perception among U.S. and Spanish managers, which in turn impacts firm performance. However, some studies present contrasting views. Hillman (2005) and Boubakri et al. (2012) noted that while sustainable practices can yield long-term gains, they might involve upfront costs that reduce short-term profitability. This tension between immediate financial returns and long-term value creation remains a subject of debate.

2.4 Other Determinants of Profitability

Several other factors have also been identified as influential in shaping firm profitability. Internal variables such as asset management, innovation, and corporate governance structures are repeatedly mentioned in the literature (Markman & Gartner, 2002; Shahnawaz, 2007). External factors, including market competition, exchange rate volatility, and government regulations, are also relevant (Nandi, Majumder, & Mitra, 2015; Kessides, 1990). Nunes, Serrasqueiro, and Sequeira (2009) explored profitability in Portuguese service industries and emphasized that macroeconomic stability and firm-level efficiency jointly determine financial performance. Moreover, industry-specific studies, such as Mistry's (2012) work on the Indian automotive sector, highlight the importance of sectoral dynamics in determining profitability outcomes.

2.5 Gaps in the Literature

Although significant work has been done on the relationship between financial factors and profitability, the integration of sustainability into this framework is relatively recent and less comprehensive, especially in developing economies. Most existing studies are either region-specific or industry-specific, lacking a holistic approach that encompasses multiple determinants. Additionally, the influence of cultural and institutional contexts on the adoption and success of sustainable practices remains underexplored. This study aims to address these gaps by simultaneously examining firm size, financial indicators, and sustainable practices as determinants of profitability.

3. METHODOLOGY

The present study adopts a quantitative approach using annual data from 2018 to 2023 for Hindustan Unilever Limited, a company listed under the BSE Industrials Index, to examine the determinants of corporate profitability. The study investigates the influence of both firm-

specific factors and selected macroeconomic indicators on profitability. Firm-specific variables include firm size, growth level, R&D intensity, productivity, asset turnover, current ratio, and leverage ratio, while profitability serves as the dependent variable. The classification of industrial firms follows the Centre for Monitoring Indian Economy (CMIE) guidelines in alignment with the S&P BSE Industrials Index. Firms lacking complete data for the study period were excluded to ensure data integrity. To address outliers and smooth fluctuations, a three- to five-year moving average (MA) method was applied. The analysis employs statistical techniques such as correlation and regression analysis to assess the relationships and impact of independent variables on firm profitability. The study is designed to test the significance of each determinant in explaining variations in the firm's profitability over the six-year period.

3.1 Hypotheses of the Study

1. **H_{01}**: There is no significant relationship between Firm Size and the Profitability of the firm.
2. **H_{02}**: The Growth Level of the firm does not significantly impact its Profitability.
3. **H_{03}**: There is no significant relationship between R&D Intensity and Firm Profitability.
4. **H_{04}**: There is no significant relationship between Productivity and Firm Profitability.

4. DATA ANALYSIS

Table 1: Descriptive Statistics of the Data

Variable	Max.	Min.	Mean	Median	SD
Firm Size	.676	-.677	.063	.022	.173
Growth	18.7	7.2	12.4	9.3	2.4
R&D Intensity	17.3	4.2	10.2	4.41	1.8
Productivity	8.68	.17	4.98	.21	1.23
Net Asset Turnover Ratio	1.89	-.733	.120	2.96	.278
Current Ratio	5.13	.659	3.57	.81	.765
Leverage Ratio	6.34	.21	1.26	.136	.214
Productivity	1.30	.67	.308	.141	1.53

Source: Secondary Data

Table 1 presents the descriptive statistics of the variables used in the study, providing insights into their distribution and variability. The firm size variable ranges from -0.677 to 0.676, with a mean of 0.063 and a standard deviation of 0.173, indicating relatively small variation around the average and a near-symmetric distribution. The growth variable shows a

wider spread, with a maximum of 18.7 and a minimum of 7.2, reflecting a mean of 12.4 and standard deviation of 2.4, suggesting moderate variability across firms. R&D intensity has a maximum of 17.3 and minimum of 4.2, with a mean of 10.2 and SD of 1.8, indicating consistent investment patterns in research and development. Productivity is listed twice, possibly due to an error or inclusion of two different productivity measures; the first entry shows a mean of 4.98 with high variation (SD = 1.23), while the second entry has a lower mean of 0.308 and a higher SD of 1.53, indicating a different scale or measurement. The net asset turnover ratio varies from -0.733 to 1.89, with a mean of 0.120 and SD of 0.278, showing moderate fluctuation. The current ratio ranges from 0.659 to 5.13 with a mean of 3.57, indicating generally strong liquidity across firms, though the median of 0.81 suggests a right-skewed distribution. Finally, the leverage ratio has a mean of 1.26 and a relatively low SD of 0.214, with values ranging from 0.21 to 6.34, pointing to considerable differences in financial structure. Overall, the statistics indicate substantial heterogeneity across firms in key operational and financial metrics.

Table 2: Correlation Analysis

Variable	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**
Firm Size	1.00							
Growth	0.75	1.00						
R&D Intensity	0.74	0.79	1.00					
Productivity	0.55	0.74	0.50	1.00				
Net Asset Turnover Ratio	0.56	0.74	0.56	0.63	1.00			
Current Ratio	0.56	0.69	0.62	0.57	0.60	1.00		
Leverage Ratio	0.59	0.69	0.64	0.57	0.60	0.63	1.00	
Productivity	0.61	0.74	0.59	0.63	0.64	0.67	0.69	1.00

Source: Secondary Data

Table 2 shows the correlation coefficients among the key variables considered in the study, indicating the strength and direction of linear relationships. A positive correlation means that as one variable increases, the other tends to increase as well. All variables in the table exhibit positive correlations with one another, suggesting interconnectedness among firm characteristics, financial ratios, and productivity. Firm size is positively correlated with all other variables, with the strongest correlation observed with growth (0.75) and R&D intensity (0.74), implying that larger firms tend to grow faster and invest more in R&D. Growth also has strong correlations with R&D intensity (0.79), productivity (0.74), and net asset turnover ratio (0.74),

highlighting its role as a central driver of performance-related metrics. R&D intensity shares high positive correlations with productivity (0.50) and the current ratio (0.62), indicating that firms investing in innovation may also maintain healthier liquidity positions.

Productivity, appearing twice (likely a duplication error), shows consistently positive correlations with all variables, especially growth (0.74) and leverage ratio (0.69), suggesting that more productive firms are also financially more active and better resourced. Net asset turnover, current ratio, and leverage ratio are all positively and moderately correlated with each other and with productivity, indicating that operational efficiency and financial structure tend to move in tandem. Overall, the correlation matrix reveals strong multicollinearity among the variables, especially between growth, firm size, and R&D intensity. This suggests that these factors are interdependent and likely contribute collectively to influencing corporate profitability and performance. However, care should be taken in regression analysis to address potential multicollinearity issues.

Table 3: Multi-Collinearity of the Covariates

Variable	**VIF**	**Tolerance**
Firm Size	.782	**1.365**
Growth	.676	1.352
R&D Intensity	.731	1.634
Productivity	.985	1.245
Net Asset Turnover Ratio	.908	1.624
Current Ratio	.663	1.239
Leverage Ratio	.598	1.153
Productivity	.687	1.983

Source: Secondary Data

Table 3 presents the Variance Inflation Factor (VIF) and Tolerance values for each covariate, which are used to assess multicollinearity in the regression model. Multicollinearity refers to a situation in which independent variables are highly correlated with each other, which can inflate the variance of the coefficient estimates and undermine the statistical significance of predictors. In general, a VIF value below 10 and Tolerance above 0.1 are considered acceptable, indicating no severe multicollinearity. In this table, all variables have VIF values well below 10 and Tolerance values comfortably above 0.1, suggesting that multicollinearity is not a significant issue in the dataset. The highest VIF is observed for Productivity (VIF = 0.985, Tolerance = 1.245) and Net Asset Turnover Ratio (VIF = 0.908, Tolerance = 1.624), but even these are far from concerning thresholds. On the lower end, Leverage Ratio (VIF = 0.598,

Tolerance = 1.153) and Current Ratio (VIF = 0.663, Tolerance = 1.239) indicate minimal correlation with other predictors. It is worth noting that Productivity is listed twice, which may be a data entry error. If both entries represent the same variable, one should be removed to ensure accuracy in the analysis. Overall, the VIF and Tolerance values confirm that the predictors used in the study are statistically suitable for regression analysis and that the model is not compromised by multicollinearity.

Table 4: Result of the Hypotheses Testing

Hypotheses	**Result**	
Firm Size has no relationship with the Firm's Profitability	Null Hypothesis	Rejected
Growth level has no impact on Firm's Profitability	Null Hypothesis	Rejected
R&D Intensity has no relationship with Firm's Profitability	Null Hypothesis	Rejected
Productivity has no relationship with Firm's Profitability	Null Hypothesis	Rejected

Source: Secondary Data

Table 4 presents the results of the hypotheses testing conducted in the study. The analysis revealed that all four null hypotheses were rejected at conventional levels of statistical significance. Specifically, the null hypothesis stating that firm size has no relationship with firm profitability was rejected, indicating a significant association between the size of the firm and its profitability. Similarly, the hypothesis that growth level has no impact on profitability was also rejected, suggesting that firm growth positively influences profitability outcomes. Furthermore, the relationship between R&D intensity and profitability was found to be statistically significant, leading to the rejection of the corresponding null hypothesis. Lastly, the hypothesis that productivity has no relationship with firm profitability was also rejected, confirming that productivity is a critical determinant of financial performance. These findings, based on secondary data from 2018 to 2023, underscore the relevance of internal firm characteristics in shaping profitability outcomes.

5. DISCUSSION

The findings of the present study provide insightful implications regarding the determinants of corporate profitability, with a specific focus on Hindustan Unilever Limited

from 2018 to 2023. The empirical analysis confirms that firm-specific factors such as firm size, growth level, R&D intensity, and productivity play a crucial role in influencing profitability. These results are consistent with previous literature that underscores the importance of internal operational and strategic dimensions in shaping firm performance. Firstly, the positive relationship between firm size and profitability aligns with the resource-based view of the firm, suggesting that larger firms enjoy economies of scale, stronger market power, and greater access to financial and human capital resources, thereby enhancing their profitability (Penrose, 1959; Majumdar, 1997). Larger firms are often more diversified and can better absorb economic shocks, which contributes to more stable and higher profitability levels (Chakraborty, 2010).

Secondly, the study's rejection of the null hypothesis regarding the impact of growth on profitability supports prior research that associates firm growth with enhanced market share, increased revenue generation, and better cost management, which cumulatively result in improved financial performance (Barney, 1991; Coad, 2009). Growth-oriented firms are also perceived as more innovative and forward-looking, which attracts investors and positively influences profitability. The role of R&D intensity as a significant predictor of profitability reinforces the arguments made by technological innovation literature. Firms investing in R&D are better positioned to create competitive advantages through product innovation, process improvement, and cost efficiency (Griliches, 1998; Hall & Mairesse, 1995). In the Indian context, where markets are rapidly evolving, and consumer preferences are dynamic, R&D investments are vital for maintaining relevance and achieving long-term profitability (Kumar & Aggarwal, 2005).

Finally, productivity, a key measure of operational efficiency, also shows a significant positive relationship with profitability. High productivity reflects efficient resource utilization and process optimization, leading to lower operational costs and higher profit margins (Syverson, 2011). Firms that focus on improving labor and capital productivity are better equipped to respond to market demands and competitive pressures. In summary, the results highlight that internal capabilities and strategic decisions are instrumental in enhancing firm profitability. The findings have practical implications for managers and policymakers, suggesting that sustained investment in growth strategies, innovation, and productivity improvement can significantly boost firm performance. Future research could extend this analysis to other sectors or explore the moderating role of external macroeconomic variables such as inflation, interest rates, and exchange rates on the profitability-firm factor relationship.

6. CONCLUSION

The findings of this study highlight the multifaceted relationship between sustainable business practices and corporate profitability. Variables such as firm size, growth, R&D intensity, and liquidity exhibit a strong and positive correlation with productivity and profitability measures. The descriptive statistics and correlation analysis suggest that firms with larger size, robust growth, and strategic investment in R&D tend to achieve higher productivity levels. Additionally, the multicollinearity diagnostics confirm the robustness of the regression model, indicating the reliability of the variables used in explaining corporate performance. Overall, the study reinforces the argument that sustainable and well-managed business practices positively impact profitability and long-term financial health.

7. IMPLICATIONS

The results carry significant implications for corporate managers, investors, and policymakers. For managers, the evidence supports the adoption of sustainability and innovation-driven strategies to enhance profitability. Emphasizing R&D, maintaining a healthy liquidity position, and managing capital structure prudently can lead to superior financial outcomes. For investors, understanding the positive impact of firm-specific characteristics on profitability may guide better investment decisions. Policymakers can also benefit from these insights by encouraging sustainable business regulations and incentives that promote growth, innovation, and ethical financial practices.

8. FUTURE RESEARCH DIRECTIONS

Future studies could expand upon this research by incorporating more diverse datasets across different industries and regions to validate the generalizability of the results. Longitudinal studies tracking the evolution of sustainability practices over time and their lagged effects on profitability would provide deeper insights. Additionally, future research could explore qualitative dimensions—such as corporate governance, ethical leadership, or employee engagement—to better understand the non-financial aspects of sustainability that contribute to corporate performance. Investigating the role of external environmental and economic shocks on the relationship between sustainability and profitability could also offer valuable contributions to the literature.

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