



REFRAME

**Circular Economy strategy FRAMEwork
for sustainable SMEs**

IO3: Circular Economy Implementation Framework (CE Framework)

Disclaimer:

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SIGMA



3.2 Financial factors

CE transition can be accelerated or hampered by financial factors. The two most commonly acknowledged financial factors that may act as barriers to implementing CE are (a) the high up-front investment costs for conducting research, establishing new processes and installing new equipment, developing new products (e.g. from recycled materials or products with extended lifetime), etc. and (b) the higher operating costs related to CE business models for collecting, sorting and recycling waste material (especially compared to the cost of virgin material), operating a return logistic system cost for taking back products at the end of their life, using renewable energy sources, reaching economies of scale for 'green' products, etc. The above-mentioned financial barriers are especially prominent for SMEs and microenterprises because they lack financial capabilities, financial support from governments (e.g. through low rate loans and/or tax reductions and incentives), and access to capital. Moreover, SMEs and (especially) micro-enterprises are more susceptible to financial risks than large enterprises and, thus, they are more reluctant to undertake the transformations required to adopt CE principles.

On the other hand, financial factors may also act as drivers to change from the linear model to the circular one. In general, there are direct and indirect economic benefits associated with CE models. The direct gains are related mainly to cost savings from substituting virgin raw materials, consuming less energy, producing less waste, increasing resource efficiency, adopting lean production principles, etc. For instance, the Ellen Macarthur Foundation report (2012) looking only at a subset of EU manufacturing sectors estimated that CE could result in an annual net material cost-saving opportunity of up to USD 380 billion for a 'transition scenario' and up to USD 630 billion per year for an 'advanced scenario'. As far as the indirect economic benefits are concerned, the adoption of CE principles may help enterprises to differentiate their products and attract environmentally sensitive consumers through green marketing, minimise the financial burden of non-compliance with environmental laws, reduce the cost of capital, achieve better financial performance in terms of return on equity (ROE) and stock prices, gain a high company reputation, etc.

Financial factors are interrelated to other factors, especially market, legal, political, and supply chain factors. Regarding the market factors, for example, if the price of virgin materials is low, then the recycled materials will be less competitive and the cost of implementing CE principles will be higher. Also, if there is a lack of demand for reused or recycled products, their prices will be low and, consequently, will negatively affect CE transition. As far as legislation is concerned, in some countries, there is not a national strategy to promote CE or help the SMEs leading the way into a circular path or companies are faced with lengthy legal procedures. From a political perspective, national and European funds are essential to enhance the application of circular models and the same stands for the law enforcement regarding the environmental compliance

rules, the knowledge of policymakers about CE issues, etc. Finally, concerning the supply chain, the disruption all over the world due to the Covid-19 pandemic acted as a driver for closing the economic loop between raw materials, components and products. On the other hand, the lack of standardisation of the recycled materials, the lack of infrastructure or the limited number of suppliers increase the financial risks and costs and, thus, hinder the transition to CE.

To assess the importance of the financial factor, the following questions should be considered:

- What is the initial investment cost of CE transition?
- Will there be additional operating costs for establishing new CE processes (e.g. developing new products, collecting, sorting and recycling waste, operating a return logistic system, etc.)?
- Will there be financial benefits (direct or indirect) to the company as a result of the CE transition?
- Considering the costs and benefits of CE transition, will the investment be worth it?
- Are there any funding opportunities (national or European) aiming to help SMEs to go circular? Is there access to affordable financing?