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Making Sense of Circularity.

An institutional logic perspective on circular business model transitions in incumbent firms.

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Abstract

Circular business models (CBMs) promise improved resource efficiency, value creation and retention. Still, CBM operationalization among large incumbents remains slow in practice. Yet, this plays a critical role in driving industry transformations towards sustainability. Prior research outlines challenges that incumbents encounter when operationalizing CBMs - yet remains fragmented and unable to explain where these tensions come from and how to effectively address them. This paper draws on institutional logics and paradox theory to explore underlying logic tensions as a potential explanatory factor and conceptualizes incumbents' transition to CBMs from an institutional logics perspective. It thereby aims to strengthen CBM research's theoretical grounding and provide a more systematic, actionable understanding of challenges faced by established firms. The findings delineate the competing institutional logics that incumbents need to accommodate when transitioning to circularity (established 'business logic' and emerging 'circular logic'). Relating this to the business model, the paper structures and explains CBM challenges as logic tensions with incumbents' established business model, structures and routines. Subsequently, organizational responses based on logic hybridization are derived and exemplified through illustrative cases. This paper suggests that considering the multiple logics that incumbents in transition to circularity face as a missing link between idea and action helps (A) rationalize incumbents' challenges with (and hesitation towards) CBM operationalization and (B) develop organizational responses for more effective CBM uptake. Further research is needed to empirically validate the conceptualized logics and test how the theorized relations to CBM challenges and corresponding management strategies hold true in practice.

Keywords

Business model; circularity; logic hybridization; incumbent firms; transformation



INTRODUCTION

Circular business models (CBM) are a type of sustainable business model focused on “closing, narrowing, slowing, intensifying, and dematerializing loops” (Geissdoerfer *et al.*, 2018:p.713), e.g. through rental or pay-per-use models (Bocken *et al.*, 2014). Interest in CBMs is increasing in research and practice. However, uptake among incumbent firms is lagging despite playing a critical role in driving industry transformation towards sustainability (Hockerts & Wüstenhagen, 2010). While research exists on how established firms manage complexity between business models (Snihur & Tarzijan, 2018) or inherent paradoxical tensions in corporate sustainability (Hahn *et al.*, 2018, 2015), it remains unclear how they navigate transition processes and emerging tensions when implementing CBMs in the context of their existing business, structures, and thinking. Simultaneously, calls to consolidate and strengthen sustainable and CBM research by grounding it in existing theory are growing (Foss & Saebi, 2018; Pieroni, McAloone & Pigosso, 2019; Lüdeke-Freund, 2020).

Business models for sustainability and circularity have been described as a “paradigm shift” (Lüdeke-Freund, Gold & Bocken, 2019:p.6), a “fundamentally new logic of doing business” (Schaltegger, Lüdeke-Freund & Hansen, 2016:p.270) and “change in the basic logic of value creation” (Rauter, Jonker & Baumgartner, 2017:p.146). Likewise, circular economy is discussed as an emerging paradigm (Geissdoerfer *et al.*, 2017) and institution (Stål & Corvellec, 2018). Still, research that explicitly explores CBM operationalization from an institutional logics perspective is missing, beyond few recent exceptions (Ranta, Keränen & Aarikka-Stenroos, 2020; Fehrer & Wieland, 2020; Stål & Corvellec, 2018). Institutional logics are implicit guiding principles (Friedland & Alford, 1991) that shape organizational behavior and decision making (DiMaggio & Powell, 1983), often referred to as the “rules of the game” (Thornton & Ocasio, 2012:p.112) that prescribe ‘how we do things around here’. They represent socially constructed frames of thought that assign legitimacy to specific objectives (e.g. profit optimization, economic value creation), values and practices, and thereby help actors understand and navigate their social and organizational reality (Greenwood *et al.*, 2011; Besharov & Smith, 2014; Thornton & Ocasio, 2012).

For established companies, the process of going circular, thus, implies adopting a different logic than ‘business as usual’: This applies to product (or service or product-service-system) design, but extends further – changing the sales and marketing functions’ relation to customers (more continuous, long-term), supply decisions (managing reverse logistics, remanufacturing or closed loops, rethinking supply planning) and accounting for circular assets. Essentially, CBMs entail a different understanding of legitimate goals (Optimization of profits but also resource efficiency and effectiveness; Value creation – what type of value & for whom, shareholders or stakeholders?) and legitimate means to reach these goals (e.g. servitization, sufficiency business models) that reflect a different underlying rationale – a different logic – than incumbents’ current business. Yet, incumbents’ established business model, structures and routines continue to co-exist with the new business model. While CBMs are not necessarily incompatible with conventional business logic – CBMs can be both

resource effective and profitable – they add complexity and friction which can create conflict if left unmanaged.

This paper argues that incumbents' challenges with (and hesitation towards) CBM operationalization can be explained and rationalized when viewing the multiple institutional logics that incumbents in transition to circularity face as a missing link between idea and action. To conceptually develop this, the paper uses existing insights on conflicting logics from hybrid organizations (Besharov & Smith, 2014; Battilana *et al.*, 2015; Battilana & Dorado, 2010) and sustainable entrepreneurship research (York, Hargrave & Pacheco, 2016), and combines them with the related paradox theory (Smith & Lewis, 2011). Applied in corporate sustainability research (Byl & Slawinski, 2015; Hahn *et al.*, 2015, 2014), it focuses on "strategies that accept tensions and attend to different sustainability objectives simultaneously, even if they are conflicting" (Hahn *et al.*, 2018:p.237) and brings in an agency element for managing tensions, not explained by institutional logics. The research aim is to strengthen the theoretical foundation of CBMs by clarifying the role of underlying logics as a missing link to understanding CBMs' uptake and strategic management in incumbent firms.

The paper is structured as follows. First, it reviews research on business models for sustainability and circularity and their respective operationalization in industry to position this work in context. Next, the paper develops the theoretical basis, reviewing conflicting logics and tensions discussed in hybrid organizations, sustainable entrepreneurship and corporate sustainability literature. Third, the paper conceptualizes logic tensions encountered by incumbents when implementing CBMs: It applies paradox theory to categorize tensions and institutional logics to explain where tensions come from and how they are systematically connected. Based on this, the paper develops a conceptual model of incumbent responses. Illustrative cases are used to exemplify findings. Lastly, the conceptual work is discussed and conclusions for research and practice provided.

EXPECTED RESULTS

First, applying the institutional logics perspective, this paper differentiates and defines two distinct, potentially conflicting logics that occur in incumbents in transition to circularity. Logic tensions typically originate from different understandings of legitimate goals or legitimate means to achieve these prescribed goals. The logics are contrasted concerning primary goals (optimize profits vs. resource use), legitimate means of value creation (Sell goods vs. redesign-reduce-servitize-reuse-refurbish etc.) and legitimate ways of organizing (Hierarchical, top-down management & efficient coordination vs. Collaboration and interdependencies across departments & value chain).

Second, the paper theorizes how these underlying logic tensions play out on business model level and materialize as paradoxical tensions (Smith & Lewis, 2011) in business model elements as clashes between old and new ways of working. This lens is then applied to systematically link and explain prior empirical findings concerning challenges faced by incumbents.



Third, after proposing logic tensions as the root cause of incumbents' struggles, the paper conceptualizes logic hybridization pathways and organizational responses to paradoxical tensions. Essentially, incumbents in transition to circularity need to accommodate elements from both (established commercial and emerging circular) institutional logics. Specifically, two, tiered pathways are discerned in a 2x2-matrix: (A) incumbents who first hybridize logics across BM elements within distinct business divisions and, subsequently, roll this out across the organization (linked to business model experimentation, intrapreneurship, corporate venturing, acquisitions etc.). Alternatively, (linked to incremental innovation, strategic change, framing circularity as 'good business'), (B) incumbents first hybridize business and circular logics across divisions with focus on single element and, subsequently, broaden the scope across the business model.

PRELIMINARY CONTRIBUTIONS AND IMPLICATIONS

The intended contributions are threefold: First, the article strengthens the theoretical grounding of CBM research by applying institutional logics to organize and explain challenges faced by incumbent firms when operationalizing CBMs. Second, it develops a conceptual framework of organizational responses to logic tensions. Third, it provides a basis for further research and theory building across CBM and organization research.

Research is needed to empirically test, challenge and further develop the framework and defined relations based on organizational behavior found in practice. Further research could expand on organizational responses and develop corresponding management strategies to better understand active agency in hybridization processes, e.g., by further developing the connection to paradox theory. Research on business model experimentation offers a promising direction for understanding corporate venturing and intrapreneurship pathways towards logic hybridization and business model transition. Further research is needed to understand the second pathway and role of organizational change and strategic management in enabling and executing the transition towards circularity.

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