Unit 1: Introduction to Business Environment

The word 'Business Environment' has been defined by various authors is as follows:
"Business Environment encompasses the -climate' or set of conditions, economic, social, political or institutional in which business operations are Conducted."— **Arthur M. Weimer**
"Environment contains the external factors that create opportunities and threats to the business. This includes socio-economic conditions, technology and political conditions." – **William Gluck and Jauch**
''Business environment is the aggregate of all conditions, events and influences that surround and affect it."—**Keith Davis**
"The environment of business consists of all those external things to which it is exposed and by which it may be influenced directly or indirectly". —**Reinecke and Schoell.**
"The total of all things external to firms and industries that affect the function of the organization is called business environment."—**Wheeler**
"Civilizations require challenges to survive. Thus environment also contains hostilities and dangers that may be overcome by individuals and organizations."— **Arnold J. Toynbee**
On the basis of the above definitions, it is very clear that the business environment is a mixture of complex, dynamic and uncontrollable external factors within which a business is to be operated.
Apart from this, Business Environment can also be defined as a set of conditions – Social, Legal, Economical, Political or Institutional that are uncontrollable in nature and affects the functioning of organization.

Features of Business Environment:
Following are the features of business environment:
  i.   Dynamic: Business environment is dynamic in nature that means, it keeps on changing as the time pass by.
 ii.   Unpredictable: The change in business environment is unpredictable. It is a very difficult to predict the exact nature of future happening and the changes in economic and social environment.
iii.   Differ from place to place: Business environment differs from place to place, region to region and country to country. Political, economical, etc conditions in Nepal differ from China and other nations.
 iv.   Interrelatedness: The different factors of business environment are co-related. For example: Change in government may lead to change in economic policies.

v. **Complex:** Business environment comprises of many factors. All these factors are related to each other. Therefore, their individual effect on the business cannot be recognized. This is perhaps the reason which makes it difficult for the business to face them.

Significance/Importance of Business Environment:

Business Environment refers to the "Sum total of conditions which surround man at a given point in space and time. In the past, the environment of man consisted of only the physical aspects of the planet Earth (air, water and land) and the biotic communities. But in due course of time and advancement of society, man extended his environment through his social, economic and political function."

In a globalised economy, the business environment plays an important role in almost all business enterprises. The significance of business environment is explained with the help of the following points:

i. **Help to understand internal Environment:** It is very much important for business enterprise to understand its internal environment, such as business policy, organization structure etc. In such case an effective management information system will help to predict the business environmental changes.

ii. **Help to Understand Market Conditions:** It is necessary for an enterprise to have the knowledge of market structure and changes taking place in it. The knowledge about increase and decrease in demand, supply, monopolistic practices, government participation in business etc., is necessary for an enterprise.

iii. **Determining Opportunities and Threats:** The interaction between the business and its environment would identify opportunities and threats to the business. It helps the business enterprises for meeting the challenges successfully.

iv. **Giving direction for growth:** The interaction with the environment leads to opening up new frontiers of growth for the business firms. It enables the business to identify the areas for growth and expansion of their activities.

v. **Continuous learning:** Environmental analysis makes the task of managers easier in dealing with business challenges. The managers are motivated to continuously update their knowledge, understanding and skills to meet the predicted changes in realm of business.

vi. **Image building:** Environmental understanding helps the business organization in improving their image by showing their sensitivity to the environment with which they are working.

vii. **Meeting competition:** It helps the firms to analyze the competitors' strategies and formulate their own strategies accordingly.

viii. **Identifying firm's strength and weakness:** Business environment helps to identify the individual strengths and weakness in view of technological and global developments.

<u>Components of Business Environment</u>

The components of business environment are classified into two broad categories.

1. Internal Environment
2. External Environment
    1. Internal Environment: It is defined as all the controllable forces and conditions within an organization that influence organizational behavior. An organization's internal environment has following sub components:
        a. Employees: They are the main components and important assets of organizations. They are responsible to work as per the direction, goals, rules and regulation of the company .For their better performance, organizations have to motivate and satisfied them with fair and equitable rewards policies. The organizations' productivity can be enhanced only by the dedication, loyalty, and cooperation of employees.
        b. Shareholder and Board of Directors: Shareholders being the owners of business, have a direct interest in the performance of the organization. The board of directors is elected by them (shareholders) who represents shareholders' interest in the board. The board is responsible to manage company and formulate appropriate plans. They evaluate overall organizational performance and provide direction to the top level management for the growth of an organization.
        c. Organizational culture: Every organization has its own culture. Culture refers to set of values, beliefs, norms of an organization under which it operates. It helps to bind all the employees and comply with organizational rules and regulations. Culture has a powerful influence on the process of organizational change and decision making.
        d. Labour Union: Labour union represents the employees or labor working in an organization. It takes problems and feeling of the labors to the management for constructive solutions. The good relation between labor union and management avoids unnecessary disturbances in organizations.
        e. Organizational Structure: Structure is a framework of an organization. It clarifies the authority and responsibility roles and relations, hierarchy of management and coordination activities for business.

2. **External Environment:** External environment is the condition and forces outside the organization that are relevant to its operation and influence the organizational activities. There are two categories of external environment. They are:
   a. General Environment
   b. Task/Operation Environment

a. **General Environment:** General environmental factors have indirect impact on the activities and outcomes of the firms. Following are the components of general environment:

   i. **Political Environment:** It refers to the influence from government institutions, strategies of political parties, policies of state and local government and relationship between government and business. Mangers must know about political environment because:
      - It imposes certain legal constraint on the business.
      - It establishes a market atmosphere that maybe pro-business or anti-business.
      - It has the potential to provide stability needed for long-term planning.

   ii. **Economic Environment:** Economic conditions are critical to the success of the organizations. It is defined as the nature and direction of the economic system of a country and their impact on the individual organization. The economic factors such as: national income, saving ,investment, monetary policies, economic growth, interest rate, consumption pattern etc, have great impact on functioning of an organization. Therefore, managers should devote much of their time and resources to forecast the economy and possible changes.

   iii. **Socio-Cultural Environment:** The socio-cultural environment affects the behavior of people and their organizations. It includes values, belief, lifestyle, family system, opinions and assumptions widely held by the citizen of the particular country. These elements of society impact the business organizations.

   iv. **Technological Environment:** Technology is the practical application of scientific knowledge. Radical development has occurred over the past several years in communication, information and automation including robotics. This development brings both opportunity and threats for the organizations. Thus, organizations should utilize their strength to gain from opportunity and neutralize the threats.

b. **Task Environment:** Task environment has direct impact on the operation of the firms. Following are the components of task environment.

   i. **Customers:** Customers exchange resources, usually in the form of money for an organization's product and services. A customer maybe an individual, family, a business house or an institution. Customer not only buys the product or services they also give valuable ideas, opinions and reaction related to it. Thus, manager should maintain close relationship with them.

   ii. **Suppliers:** Suppliers are the organizations which provide resources like materials, men, machines etc to other firms. As the quality and price of the raw material received from the suppliers determine the quality of the output, the business firm tries to obtain lower prices, better quality and fast deliveries. This strengthens the competitive position of organizations.

   iii. **Government:** The role of the government is to regulate business system and to protect the interest of customers and general public. It formulates rules and regulation, business policies etc under which every firms need to operate. Therefore, government has great influence on corporate policies, procedures and business practices of modern organizations.

   iv. **Competitors:** It refers to organizations that compete for resources with other organizations and provides the similar or substitute product and services to the same group of people. The organization must analyze the competition and established clearly defined marketing strategies in order to provide superior customer satisfaction and to increase market share.

   v. **Media:** The media keeps eye on the vital decision or actions of the business firms having general public interest. Therefore managers need to have good communication with both media and external audiences and deal with them effectively and promptly.

   vi. **Financial institutions:** Organizations depends on a variety of financial institutions such as: banks, insurance companies, capital markets, etc to supply fund for maintaining and expanding their business activities. The terms and conditions of loans and advances and quality of promptness of their services have an impact on the performance of business firms.

   vii. **Special Interest Group:** It refers to environmentalist, unions, consumer advocates, civic society and other professional organization. These organizations pressurized the company to advance their position on the issues like quality services, reasonable price, waste management, environmental protection etc.

Environmental Scanning

Environmental scanning is X-ray of the environment. It is defined as the process of understanding the dynamism and trends of environment. In other words, it is the process that seeks information about events and relationships in a firm's environment, the knowledge of which help top management chart the firm's future.

Furthermore, Environmental scanning is a process that systematically surveys and interprets relevant data to identify external opportunities and threats. An organization gathers information about the external world, its competitors and itself. The company should then respond to the information gathered by changing its strategies and plans when the need arises.

Environmental scanning entails partitioning the external environment into sectors, namely, cultural, economic, political, technological, and so on. This helps establish a firm's information needs within those sectors. Data are usually collected by monitoring and forecasting changes in important variables identified in each sector. That data are then transformed into consolidated information, which is integrated into the firm's strategic planning process (Georgantzas and Acar 1995).

Environmental scanning is used to gather information from the environment. This information is used to craft a strategic plan that will help an organization achieve and maintain a competitive advantage. In order to be successful, the organization must align its strategies and plans with the information gathered from the environmental scanning.

Types of environmental Scanning:

i.   **Concentric scanning:** If only one factor of the environment is being analyzed to identify its cause and effect along with its cost and benefit, then it is called concentric scanning. For example: examining only economic environment to know the possible future profit prospects.

ii. **Comprehensive scanning:** If all the factors of the environment are being analyzed to identify their cause and effect along with their cost and benefit, then it is called comprehensive scanning.

Process of Environmental Scanning

Following process is adopted in environmental scanning:

1. Study of forces and nature of environment: This is the first step of environmental scanning in which organization studies the nature of environmental forces and their trends.

2. Determine the sources of information: A company can obtain information from different sources, but it should be ensured that the information is correct. The correct source should be tapped for specific information for more accuracy. Information received form secondary sources may sometimes even misguide strategy managers. Hence, it is important that information should be verified for correctness before it is processed and decisions are taken based on it. Different sources used to collect the information are:

   - Secondary sources: Newspaper, research articles, publications etc.

   - Mass media: Radio, TV , internet etc

   - Internal sources: Management information system, financial reports, etc.

   - External agencies: consumer, suppliers, distributors etc.

   - Formal research by organization and research agencies etc.

3. Determine the Approaches to Environmental Scanning: The experts have suggested three approaches, which could be adopted for, sort out information for environmental scanning.

   - Systematic Approach: Under this approach, information for environmental scanning is collected systematically. Information related to markets and customers, changes in legislation and regulations that have a direct impact on an organization's activities, government policy statements pertaining the organization's business and industry, etc, could be collected continuous updating such information is necessary not only for strategic management but also for operational activities.

   - Ad hoc Approach: Using this approach, an organization may conduct special surveys and studies to deal with specific environmental issues from time to time. Such studies may be conducted, for instance, when organization has to undertake special projects, evaluate existing strategy or devise new strategies. Changes and unforeseen developments may be investigated with regard to their impact on the organization.

   - Processed-form Approach: For adopting this approach, the organization uses information in a processed form available from different sources both inside and outside the organization. When an organization uses information supplied by government agencies or private institutions, it

uses secondary sources of data and the information is available in processed form.

4. Scan and Assess the trend: Finally organization specifies relevant environmental trends and their behaviors. And assess them in terms of opportunities and challenges.

Techniques/Methods of Environmental Scanning

Following are the methods of environmental scanning:

a. Executive opinion method: Under this environment is forecasted on the basis of opinion and views of top executives.

b. Delphi Techniques: Outsides experts are used in scanning the environmental factors and their impacts.

c. Extrapolating method: Under this method past information is used to predict the future. Trend analysis, regression analysis etc is being used to identify the trends.

d. Scenario building: Under this method, different scenario that may reflect the future are built. These scenarios address the contingencies and help in better understanding the changes and impacts of the environmental factors.

Environmental Analysis

It is a process of identifying the relevant factors that have direct or indirect impact on effective and efficient functioning of business.

In other words, Environmental analysis is a strategic tool. It is a process to identify all the external and internal elements, which can affect the organization's performance. The analysis entails assessing the level of threat or opportunity the factors might present. These evaluations are later translated into the decision-making process. The analysis helps align strategies with the firm's environment.

Process of environmental analysis:

Environment analysis is managerial decision-making based on the assessment of opportunities and threats in the environment. The steps in environmental analysis are:

1. Scanning: It involves information gathering for assessing the nature of the environment in terms of uncertainly, complexity and dynamics. It includes:
   a. Identifies early signs of future environmental changes. They are indicated by trends and events.
   b. Detects changes already underway. They are happening.

2. Monitoring: It involves tracking environmental trends and events. It is auditing of environment. The likely impact of environmental influences on business performance is identified.

3. Forecasting: This step forecast what is likely to happen. It lay out of path for anticipate changes. This step provides:
   a. Key forces at work in the environment. They can be political-legal, economic, social, cultural, and technological.
   b. Understanding of the nature of key influences and drivers of change.
   c. Projection of future alternatives paths available.

4. Assessment: This step identifies key opportunities and threats. The competitive position of business analyzed in terms of how the organization stands in relation to other organizations competing for some resource of customers.
   a. Opportunities are a favorable condition which creates risks and weakens the competitive position.
   b. Threat is an unfavorable condition which strengths, organization's competitive position of the organization.

Environment-Business Relations:

Business is the product of the technological, political-legal, economic, social – cultural, global and natural factors amidst which it functions. Three features are common to this web of relationship between business and its environment.

   i. There is symbolic relationship between business and its environment and among the environmental factors. In other words, business is influenced by its environment and in turn, to certain degree, it will influence the external forces. Similarly, political-legal environment influences economic environment and vice versa. The same relationship between other environment factors too.

   ii. These environmental forces are dynamic. They keep on changing as years roll by, so does business.

   iii. The third feature is that a particular business firm, by itself, may not be in a position to change its environment. But along with other firms, business will be in a position to mould the environment in its favor.