1
Business Environment

Learning Objectives

- Understand the term business and its objectives.
- Know the factors that influence a business.
- Understand what is environmental analysis and why is it needed.
- Have a basic knowledge of various types of environment.
- Have an understanding of different micro-economic factors that are affecting business.
- Know the various macro-economic factors and how they are related to business.
- Understand the various components of the competitive environment.

Awareness of the environment is not a special project to be undertaken only when warning of change becomes deafening...

Kenneth R. Andrews

It is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to change.

Charles Darwin

1. Introduction

Each business organization operates in its unique environment. Environment influence businesses and also gets influenced by it. No business can function free of interacting and influencing forces that are outside its periphery. In the new economy the facets of business are rapidly changing as compared to earlier years. The developments in technology and faster communication have lead to evolvement of newer kinds of businesses. The concept of businesses such as e-bay, rediff were non-existent in yesteryears. Businesses are conducted through internet and have lead to virtual shrinking of physical boundaries between nations.

2. Business

Etymologically the term business refers to the state of being busy for an individual, group, organization or society. The term is also interpreted as one's regular occupation or profession.

In another sense, the term refers to a particular entity, company or corporation. It is also interpreted as a particular market sector such as the computer business. Thus the term is wide and amenable to different usages. A business for our purposes can be any activity consisting of purchase, sale, manufacture, processing, and/or marketing of products and/or services.

It is said that a business exists for profits. Profit, as a surplus of business, accrues to the owners. It is their share, just as wages are the share of workers. People invest in business for getting a return. It is a reward for risk taking, so far as the owners are concerned. As a motive, profit serves as a stimulant for business effort.

For business enterprises, profit is often regarded as the overall measure of performance. It is treated as a financial yardstick for measuring business efficiency and for evaluating managerial competence – how well the decisions and actions of managers turn out to be effective; how well they are able to combine and utilise resources and to sustain the enterprise as a going and a growing concern. Other things being equal, the higher the efficiency the greater is the level and volume of profit. Business efficiency is often expressed in terms of percentage of profit to sales volume, to capital employed, to market value of corporate shares and so on. Outside investors also equate profit with the degree of business efficiency and managerial competence and commit their funds in light of such equation and other related assessments.

Peter F Drucker has drawn two important conclusions about what is a business that are useful for an understanding of the term business.

- The first thing about a business is that it is created and managed by people. There will be a group of people who will take decisions that will determine whether an organization is going to prosper or decline, whether it will survive or will eventually perish. This is true of every business.
- The second conclusion drawn is that the business cannot be explained in terms of profit. The economic criterion of maximising profits for a firm has little relevance in the present times. Profit maximization, in simple terms is selling at a higher price than the cost. Profit maximization has been qualified with the long-term perspective and has been modified to include development of wealth, to include several non-financial factors such as goodwill, societal factors, relations and so on.

3. Objectives of a Business

A business has some purpose. A valid purpose of business is to create customers. It is for the businesses to create a customer or market. It is the customer who determines what a business is. The customer is the foundation of business and keeps it in existence. A still broader view of business purpose is that business exists and functions for catering to the material needs and requirements of society, within the framework of general considerations of social interest. Business is society's organ of economic expansion, growth and change.

Enterprises pursue multiple objectives rather than a single objective. In general, we may identify a set of business objectives pursued by a large cross-section of enterprises. These

relate to profitability, productive efficiency, growth, technological dynamism, stability, self-reliance, survival, competitive strength, customer service, financial solvency, product quality, diversification, employee satisfaction and welfare, and so on. Enterprises seek to balance these objectives in an appropriate manner. We may now elaborate some of the important objectives of a business as:

- Survival: Survival is the will and anxiety to perpetuate into the feature as long as possible. It is a basic, implicit objective of most organizations. While survival is an obvious objective, it gains more value and prominence during the initial stage of the establishment of the enterprise and during general economic adversity. The ability to survive is a function of the nature of ownership, nature of business competence of management, general and industry conditions, financial strength of the enterprise and so on. However, business and other enterprises are interested in more than mere survival.
- Stability: One of the most important of objectives of business enterprises is stability. It is a cautious, conservative objective. In a sense, stability is a least expensive and risky objective in terms of managerial time and talent and other resources. A stable and steady enterprise minimises managerial tensions and demands less dynamism from managers. It is a strategy of least resistance in a hostile external environment.
- Growth: This is a promising and popular objective which is equated with dynamism, vigour, promise and success. Enterprise growth may take one or more of the forms like increase in assets, manufacturing facilities, increase in sales volume in existing products or through new products, improvement in profits and market share, increase in manpower employment, acquisition of other enterprises and so on. Growth may take the enterprise along relatively unknown and risky paths, full of promises and pitfalls.
- Efficiency: Business enterprise seek efficiency in rationally choosing appropriate means to achieve their goals, doing things in the best possible manner and utilising resources in a most suitable combination to get highest productivity. In a sense, efficiency is an economic version of the technical objective of productivity – designing and achieving suitable input output ratios of funds, resources, facilities and efforts. Efficiency is a very useful operational objective.
- Profitability: It is generally asserted that private enterprises are primarily motivated by the objective of profit. Some may go even further and emphasise that profit is the sole motive of business enterprises. All other objectives are facilitative objectives and are meant to be subservient to the profit motive. It is pointed out that private business enterprises are operated on behalf of and for the benefit of the owners who have assumed the business risk of investing their funds.

4. Environmental Influences on Business

All living creatures including human beings live within an environment. Apart from the natural environment, environment of humans include family, friends, peers, neighbours and society. It also includes man-made structures such as buildings, furniture, roads and other physical

infrastructure. The individuals do not live in a vacuum. They continuously interact with their environment to live their lives.

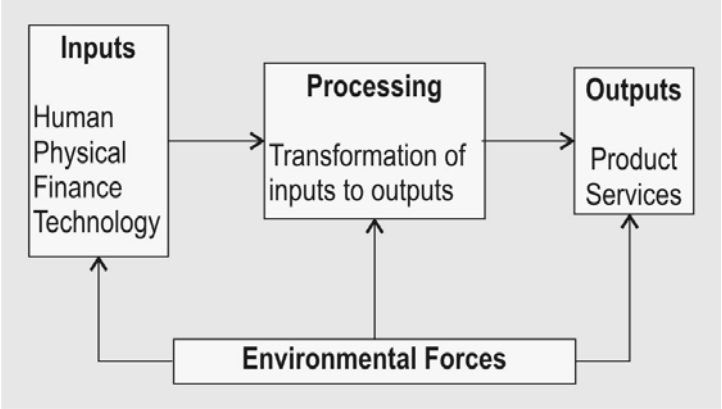
Just like human beings, business also does not function in an isolated vacuum. Businesses function within a whole gambit of relevant environment and have to negotiate their way through it. The extent to which the business thrives depends on the manner in which it interacts with its environment. A business which continually remains passive to the relevant changes in the environment is destined to gradually fade-away in oblivion.

To be successful business has to not only recognise different elements of the environment but also respect, adapt to or have to manage and influence them. The business must continuously monitor and adapt to the environment if it is to survive and prosper. Disturbances in the environment may spell extreme threats or open up new opportunities for the firm. A successful business has to identify, appraise, and respond to the various opportunities and threats in its environment.

Environment is sum of several external and internal forces that affect the functioning of business. According to Barry M. Richman and Melvyn Copen "Environment factors or constraint are largely if not totally, external and beyond the control of individual industrial enterprises and their managements. These are essentially the 'givers' within which firms and their managements must operate in a specific country and they vary, often greatly, from country to country." A strategist looks on the environment as posing threats to a firm or offering immense opportunities for exploitation. Stressing this aspect, Glueck and Jauch wrote: "The environment includes factors outside the firm which can lead to opportunities for or threats to the firm. Although there are many factors, the most important of the sectors are socio-economic, technological, supplier, competitors, and government. "

Business functions as a part of broader environment. The inputs in the form of human, physical, financial and other related resources are drawn from the environment. Business converts these resources through various processes into outputs of products and/or services. The latter are partly exchanged with the external client groups, say customers. The exchange process brings in some surplus (or profits, reputation, good public image and so on) to the business, which could be stored and used for further development and growth.

Different organizations use different inputs, adopt different processes and produce different outputs. For example, an educational institution produces literate people. A hospital provides health and medical services. Organizations depend on the external environment for the inputs required by them and for disposing of their outputs in a mutually beneficial manner. The input-output exchange activity is a continuous process and calls for an active interaction with the external environment.



4.1 Problems in understanding the environmental influences

In trying to understand the environment, managers face different problems as follows:

- The first difficulty is in diversity. The environment encapsulates many different influences; the difficulty is in making sense of this diversity in a way which can contribute to strategic decision-making. Listing all conceivable environmental influences may be possible, but it may not be of much use because no overall picture emerges of really important influences on the organization.
- The second difficulty is that of uncertainty. Managers typically claim that the pace of technological change and the speed of global communications mean more and faster change now than ever before. Whether or not change is in fact faster now than hitherto, and whether or not the changes are more unpredictable, it remains the case that, while it is important to try to understand future external influences on an organization, it is very difficult to do so.
- Managers are no different from other individuals in the way they cope with complexity. They tend to simplify such complexity by focusing on aspects of the environment, which, perhaps, have been historically important, or confirm prior views. These are not perverse managerial behaviours; they are the natural behaviour of everyone faced with complexity. Arguably, one of the tasks of the strategic manager is to find ways & means to break out of oversimplification or bias in the understanding of their environment, while still achieving a useful and usable level of analysis.

4.2 Framework to understand the environmental influences

In spite of the problems in understanding business environment, organizations cannot ignore it. We will make an attempt to identify a framework for understanding the environment of organizations. This will help in identifying key issues, find ways of coping with complexity and also assist in challenging managerial thinking.

- Firstly, it is useful to take an initial view of the nature of the organizations environment in terms of how uncertain it is. Is it relatively static or does it show signs of change, and

in what ways? Is it simple or complex to comprehend? This helps in deciding what focus the rest of the analysis is to take.

- The next step might be the auditing of environmental influences. Here the aim is to identify which of the many different environmental influences are likely to affect the organization's development or performance. This is done by considering the way in which political, economic, social and technological influences have a bearing on organizations. It is increasingly useful to relate such influences to growing trends towards globalization of industries. It may also be helpful to construct pictures - or scenarios - of possible futures, to consider the extent to which strategies might need to change.
- The final step is to focus more towards an explicit consideration of the immediate environment of the organization - for example, the competitive arena in which the organization operates. In competitive environment we will study five forces analysis *(discussed later in the chapter)* that aims to identify the key forces at work in the immediate or competitive environment and why they are significant. There should be an attempt to understand why the forces are of strategic significance. It is also required to analyse the organization's competitive position: that is, how it stands in relation to those other organizations competing for the same resources, or customers, as itself.

5. Why Environmental Analysis?

When the company ceases to adjust the environment to its strategy or does not react to the demands of the environment by changing its strategy, the result is reduced achievement of corporate objectives. From environmental analysis strategists get time to anticipate opportunities and to plan to take optional responses to these opportunities. It also helps strategists to develop an early warning system to prevent threats or to develop strategies which can turn a threat to the firm's advantage. It is clear that because of the difficulty to assessing the future, not all future events can be anticipated. To the extent that some or most are anticipated by this analysis and diagnosis, managerial decisions are likely to be better. And the process reduces the time pressures on the few which are not anticipated. Thus, the managers can concentrate on these few instead of having to deal with all the environmental influences.

In general, environmental analysis has three basic goals as follows:

- *First,* the analysis should provide an understanding of current and potential changes taking place in the environment. It is important that one must be aware of the existing environment. At the same time one must have a long term perspective about the future too.
- *Second,* environmental analysis should provide inputs for strategic decision making. Mere collection of data is not enough. The information collected must be useful for and used in strategic decision making.

- *Third,* environment analysis should facilitate and foster strategic thinking in organizations-typically a rich source of ideas and understanding of the context within which a firm operates. It should challenge the current wisdom by bringing fresh viewpoints into the organization.

> "Positive trends in the environment breed complacency. That underscores a basic point: in change there is both opportunity and challenge". - Clifton Garvin

6. Characteristics of Business Environment

Business environment exhibits many characteristics. Some of the important – and obvious – characteristics are briefly described here.

- Environment is complex: the environment consists of a number of factors, events, conditions and influences arising from different sources. All these do not exist in isolation but interact with each other to create entirely new sets of influences. It is difficult to comprehend at once the factors constituting a given environment. All in all, environment is a complex that is somewhat easier to understand in parts but difficult to grasp in totality.
- Environment is dynamic: the environment is constantly changing in nature. Due to the many and varied influences operating, there is dynamism in the environment causing it to continuously change its shape and character.
- Environment is multi-faceted: What shape and character an environment assumes depends on the perception of the observer. A particular change in the environment, or a new development, may be viewed differently by different observers. This is frequently seen when the same development is welcomed as an opportunity by one company while another company perceives it as a threat.
- Environment has a far reaching impact: The environment has a far reaching impact on organizations. The growth and profitability of an organization depends critically on the environment in which it exists. Any environment change has an impact on the organization in several different ways.

7. Components of Business Environment

The environment in which an organization exists could be broadly divided into two parts *the external* and *the internal* environment. Since the environment is complex, dynamic, multi-faceted and has a far reaching impact, dividing it into external and internal components enables us to understand it better. Here we deal with the appraisal of the external environment. This is done through a description of important characteristics of the environment, dividing the environment into its external and internal parts, observing how a systematic approach can help in environmental appraisal, and classifying the external environment into two parts, the general and the relevant environment. Next, we see how the external environment can be divided into different components.

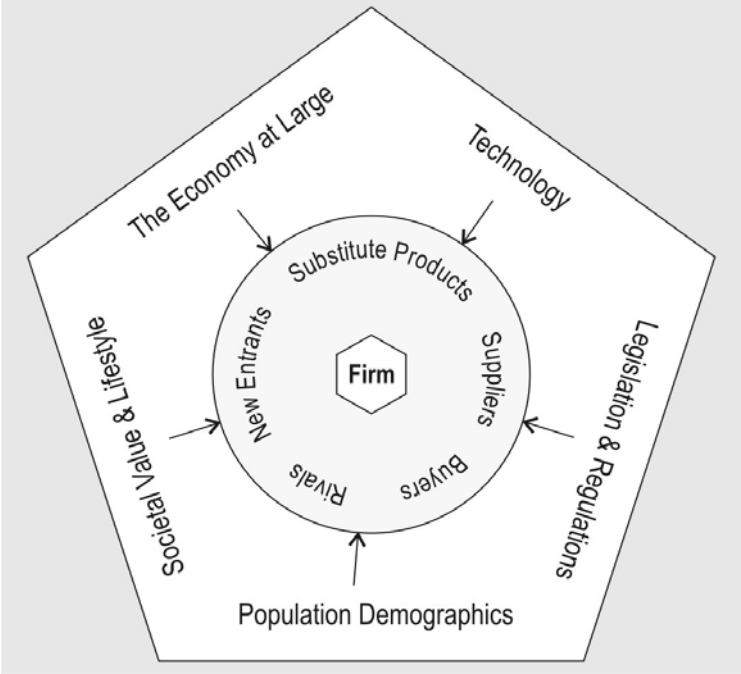


Figure: A Company's Business Environment

The *external environment* includes all the factors outside the organization which provide opportunity or pose threats to the organization. The *internal environment* refers to all the factors within an organization which impart strengths or cause weaknesses of a strategic nature.

The environment in which an organization exists can, therefore, be described in terms of the opportunities and threats operating in the external environment apart from the strengths and weaknesses existing in the internal environment. The four environmental influences could be described as follows:

- *An opportunity* is a favourable condition in the organization's environment which enables it to consolidate and strengthen its position. An example of an opportunity is growing demand for the products or services that a company provides.
- *A threat* is an unfavourable condition in the organization's environment which creates a risk for, or causes damage to, the organization. An example of a threat is the emergence of strong new competitors who are likely to offer stiff competition to the existing companies in an industry.
- *A strength* is an inherent capacity which an organization can use to gain strategic advantage over its competitors. An example of strength is superior research and development skills which can be used for new product development so that the company gains competitive advantage.

- *A weakness* is an inherent limitation or constraint which creates a strategic disadvantage. An example of a weakness is over dependence on a single product line, which is potentially risky for a company in times of crisis.

An understanding of the external environment, in terms of the opportunities and threats, and the internal environment, in terms of the strengths and weaknesses, is crucial for the existence, growth and profitability of any organization.

A systematic approach to understanding the environment is the SWOT analysis. Business firms undertake *SWOT analysis* to understand the external and internal environment. SWOT, which is the acronym for *strengths, weaknesses, opportunities and threats.* Through such an analysis, the strengths and *weaknesses* existing within an organization can be matched with the opportunities and threats operating in the environment so that an effective strategy can be formulated. An effective organizational strategy, therefore, is one that capitalises on the opportunities through the use of strengths and neutralises the threats by minimizing the impact of weaknesses. The process of strategy formulation starts with, and critically depends on, the appraisal of the external and internal environment of an organization. We will learn more about SWOT analysis in the third chapter.

8. Relationship between Organization and its Environment

In relation to the individual corporate enterprise, the external environment offers a range of opportunities, constraints, threats and pressures and thereby influences the structure and functioning of the enterprise. As a sub-system, the corporate enterprise draws certain inputs of resources, information and values from the larger environmental system, transforms them into outputs of products, services, goals and satisfactions and exchanges with or transmits them into the external environment.

The relationship between the organization and its environment may be discussed in terms of interactions between them in several major areas which are outlined below:

- *Exchange of information*: The organization scans the external environmental variables, their behaviour and changes, generates important information and uses it for its planning, decision-making and control purposes. Much of the organizational structure and functioning is attuned to the external environmental information. Information generation is one way to get over the problems of uncertainty and complexity of the external environment. Information is to be generated on economic activity and market conditions, technological developments, social and demographic factors political-governmental policies and postures, the activities of other organizations and so on. Both current and projected information is important for the organization.

  Apart from gathering information, the organization itself transmits information to several external agencies either voluntarily, inadvertently or legally. Other organizations and individuals may be interested in the organization and its functioning and hence approach the organization for information. It is also possible to glean information from the behaviour of the organization itself, from its occasional advertisements, and from

annual reports. Also, the organization may be legally or otherwise bound to supply information on its activities to governmental agencies, investors, employees, trade unions, professional bodies and the like.

- *Exchange of resources*: The organization receives inputs—finance, materials, manpower, equipment etc., from the external environment through contractual and other arrangements. It sustains itself by employing the above inputs for involving or producing output of products and services. The organization interacts with the factor markets for purposes of getting its inputs; it competes sometimes and collaborates sometimes with other organizations in the process of ensuring a consistent supply of inputs.

  The organization is dependent on the external environment for disposal of its output of products and services to a wide range of clientele. This is also an interaction process—perceiving the needs of the external environment and catering to them, satisfying the expectations and demands of the clientele groups, such as customers, employees, shareholders, creditors, suppliers, local community, general public and so on. These groups tend to press on the organization for meeting their expectations, needs and demands and for upholding their values and interests.

- *Exchange of influence and power*: Another area of organizational-environmental interaction is in the exchange of power and influence. The external environment holds considerable power over the organization both by virtue of its being more inclusive as also by virtue of its command over resources, information and other inputs. It offers a range of opportunities, incentives and rewards on the one hand and a set of constraints, threats and restrictions on the other. In both ways, the organization is conditioned and constrained. The external environment is also in a position to impose its will over the organization and can force it to fall in line. Governmental control over the organization is one such power relationship. Other organizations, competitors, markets, customers, suppliers, investors etc., also exercise considerable collective power and influence over the planning and decision making processes of the organization.

  In turn, the organization itself is sometimes in a position to wield considerable power and influence over some of the elements of the external environment by virtue of its command over resources and information. The same elements which exercise power over the organization are also subject to the influence and power of the organization in some respects. To the extent that the organization is able to hold power over the environment it increases its autonomy and freedom of action. It can dictate terms to the external forces and mould them to its will.

In delineating the relationship between the organization and the environment, one has to be clear on the diversity of both these entities. On the one hand, the nature of relationship depends on the size of the organization, its age, the nature of business, the nature of ownership, degree of professionalization of management, etc. On the other hand, the

relationship depends on the fact whether the external environmental elements behave in a random or structured manner (uncertainty *v.* predictability), whether such elements are placid or turbulent, whether they are slow-changing or fast changing, whether they are simple or complex, and so forth. The degree of interaction between the organization and the external environment is set by the above characteristics. It follows therefore that all organizations do not behave in the same way in relation to their external environment. Their structures and functions are shaped in tune with the demands of the external environment.

9. The Micro and Macro Environment

The environment of business can be categorised into two broad categories micro-environment and macro-environment. Micro-environment is related to small area or immediate periphery of an organization. Micro-environment influences an organization regularly and directly. Within the micro or the immediate environment in which a firm operates we need to address the following issues:

- The employees of the firm, their characteristics and how they are organised.
- The customer base on which the firm relies for business.
- The ways in which the firm can raise its finance.
- Who are the firm suppliers and how are the links between the two being developed?
- The local community within which the firm operates.
- The direct competition and how they perform.

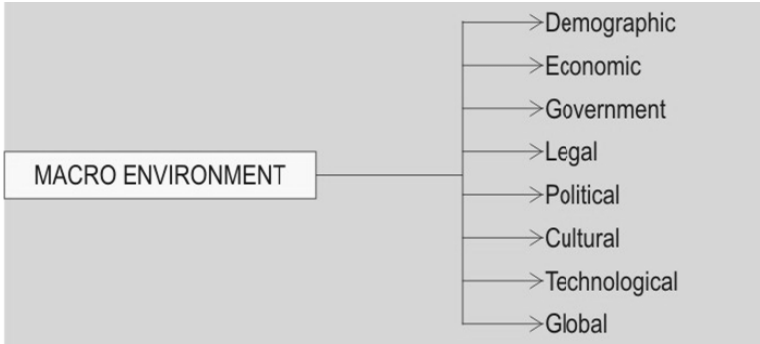
This last point might act as a convenient linking point as we move towards the macro issues influencing the way a firm reacts in the market place. Macro environment has broader dimensions. It mainly consists of economic, technological, political, legal and socio-cultural. The issues concerning an organization are:

- Who are their threats in the competitive world in which they operate and why?
- Which areas of technology might pose a threat to their current product range and why?
- The bargaining power of suppliers and customers?
- The type of competition they are facing and their perceived threats and weaknesses?

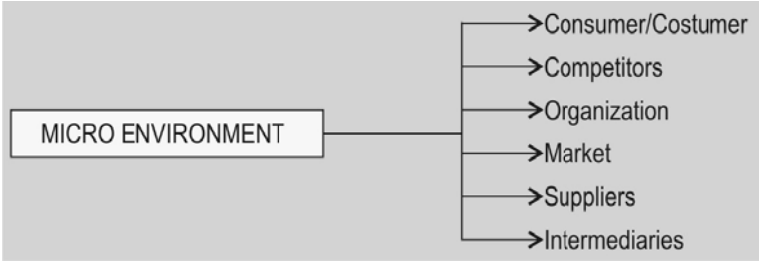
The classification of the relevant environment into components or sectors helps an organization to cope with its complexity, comprehend the different influences operating, and relating the environmental changes to its strategic management process. Different bases for classification have been adopted. As already discussed earlier there are two types of environmental forces, which influence an organizations business operation. Some of these forces are external to the firm and the organization has little control over them. Whereas the

other types of forces which comes from within the organization and can be controlled by it. Hence, the business environment can be divided into two major components:

Macro Environment: consists of demographics and economic conditions, socio-cultural factors, political and legal systems, technological developments, etc. These constitute the general environment, which affects the working of all the firms.



Micro environment: consist of suppliers, consumers, marketing intermediaries, etc. These are specific to the said business or firm and affects it's working on short term basis.



10 Environmental Scanning

Organizational environment consists of both external and internal factors. Environment must be scanned so as to determine development and forecasts of factors that will influence organizational success. Environmental scanning can be defined as the process by which organizations monitor their relevant environment to identify opportunities and threats affecting their business for the purpose of taking strategic decisions. It is the process of gathering information regarding company's environment, analysing it and forecasting the impact of all predictable environmental changes. It helps the managers to decide the future path of the organization. Scanning must identify the threats and opportunities existing in the environment. While strategy formulation, an organization must take advantage of the opportunities and minimize the threats. A threat for one organization may be an opportunity for another. The factors which need to be considered for environmental scanning are events, trends, issues and expectations of the different interest groups. These factors are explained below:

- Events are important and specific occurrences taking place in different environmental sectors. Events are certain happening in the internal or external organisational environment which can be observed and tracked.
- Trends are the general tendencies or the courses of action along which events take place. Trends are grouping of similar or related events that tends to move in a given direction, increasing or decreasing in strength of frequency of observation; usually suggests a pattern of change in a particular area (for example, consumer behaviour, technology use).
- Issues are the current concerns that arise in response to events and trends. Identifying an emerging issue is more difficult. Emerging issues start with a value shift, or a change in how an issue is viewed.
- Expectations are the demands made by interested groups in the light of their concern for issues.

11. Elements of Micro Environment

This is also known as the task environment and affects business and marketing in the daily operating level. When the changes in the macro environment affect business in the long run, the effect micro environmental changes are noticed immediately. Organizations have to closely analyse and monitor all the elements of micro environment in order to stay competitive.

11.1 Consumers/Customers

According to Peter Drucker the aim of business is to create and retain customer. Customers are the people who pay money to acquire an organization's products. The products may be both in form of goods or services. The organizations cannot survive without customers. They will cease to exist. Customers may or may not be a consumer. Consumer is the one who ultimately consumes or uses the product or service. A father may buy a product as a customer for his daughter who will be a consumer. A consumer occupies the central position in the marketing environment. The marketer has to closely monitor and analyze changes in consumer tastes and preferences and their buying habits.

- ♦ Who are the customers/consumers?
- ♦ What benefits are they looking for?
- ♦ What are their buying patterns?

11.2 Competitors

Competitors are the other business entities that compete for resources as well as markets. Competition shapes business. A study of the competitive scenario is essential for the marketer, particularly threats from competition. Following are a few of major questions that may be addressed for analysing competitions:

- ♦ Who are the competitors?
- ♦ What are their present strategy and business objective?

- Who are the most aggressive and powerful competitors?

Competition may be direct or indirect. Direct competition is between organizations, which are in same business activity. At the same time competition can also be indirect. For example, competition between a holiday resort and car manufacturing company for available discretionary income of affluent customers is indirect competition.

11.3 Organization

Individuals occupying different positions or working in different capacities in organizations consists of individuals who come from outside. They have different and varied interests. In micro environment analysis, nothing is important as self-analysis by the organization itself. Understanding its own strengths and capabilities in a particular business, i.e., understanding a business in depth should be the goal of firm's internal analysis. The objectives, goals and resource availabilities of a firm occupy a critical position in the micro environment.

"*We have met the enemy and he is us*" - Pogo.

An organization has several non-specific elements of the organization's surroundings that may affect its activities. These consist of specific organizations or groups that are likely to influence an organization. These are:

- *Owners:* They are individuals, shareholders, groups, or organizations who have a major stake in the organization. They have a vested interest in the well-being of the company.
- *Board of directors:* Board of directors are found in companies formed under the Companies Act, 1956. The board of directors is elected by the shareholders and is charged with overseeing the general management of the organization to ensure that it is being run in a way that best serves the shareholders' interests.
- *Employees:* Employees are the people who actually do the work in an organization. Employees are the major force within an organization. It is important for an organization that employees embrace the same values and goals as the organization. However, they differ in beliefs, education, attitudes, and capabilities. When managers and employees work toward different goals everyone suffers.

11.4 Market

The market is larger than customers. The market is to be studied in terms of its actual and potential size, its growth prospect and also its attractiveness. The marketer should study the trends and development and the key success factors of the market he is operating. Important issues are :

- Cost structure of the market.
- The price sensitivity of the market.
- Technological structure of the market.
- The existing distribution system of the market.

- Is the market mature?

11.5 Suppliers

Suppliers form an important component of the micro environment. The suppliers provide raw materials, equipment, services and so on. Large companies rely on hundreds of suppliers to maintain their production. Suppliers with their own bargaining power affect the cost structure of the industry. They constitute a major force, which shapes competition in the industry. Also organizations have to take a major decision on "outsourcing" or "in-house" production depending on this supplier environment.

11.6 Intermediaries

Intermediaries exert a considerable influence on the business organizations. They can also be considered as the major determining force in the business. In many cases the consumers are not aware of the manufacturer of the products they buy. They buy product from the local retailers or big departmental stores such as Big bazaars, Subhiksha and Vishal Mega Mart that are increasingly becoming popular in some big cities.

12. Elements of Macro Environment

Macro environment is explained as one which is largely external to the enterprise and thus beyond the direct influence and control of the organization, but which exerts powerful influence over its functioning. The external environment of the enterprise consists of individuals, groups, agencies, organizations, events, conditions and forces with which the organization comes into frequent contact in the course of its functioning. It establishes interacting and interdependent relations, conducts transactions, designs and administers appropriate strategies and policies to cope with fluctuations therein and otherwise negotiates its way into the future.

12.1 Demographic Environment

The term demographics denotes characteristics of population in a area, district, country or in world. It includes factors such as race, age, income, educational attainment, asset ownership, home ownership, employment status and location. Data with respect to these factors within a demographic variable, and across households, are of interest, to businessmen in addition to economist. Marketers and other social scientists often group populations into categories based on demographic variables. Some of the demographic factors have great impact on the business. Factors such as general age profile, sex ratio, education, growth rate affect the business with different magnitude. India has relatively younger population as compared to some countries. China on the other hand is having an aging population. Many multinationals are interested in India considering its population size. With having approximately sixteen percent of the world's population, the country holds huge potential for overseas companies.

Business Organizations need to study different demographic factors. Particularly, they need to address following issues:

- What demographic trends will affect the market size of the industry?
- What demographic trends represent opportunities or threats?

The business, as such, is concerned with a population's size, age structure, geographic distribution, ethnic make-up, and distribution of income. While each of the major elements of discussed below, the challenge for strategists is to determine what the changes, that have been identified in the demographic characteristics or elements of a population, imply for the future strategic competitiveness of the company. We will briefly discuss a few factors that are of interest to a business.

(i) *Population Size:* While population size itself, large or small, may be important to companies that require a "critical mass" of potential customers, changes in the specific make-up of a population's size may have even more critical implications. Among the most important changes in a population's size are:

- Changes in a nation's birth rate and/or family size;
- Increases or declines in the total population;
- Effects of rapid population growth on natural resources or food supplies.

Changes in a nation's population growth rate and life expectancy can have important implications for companies. Are people living longer? What is the life expectancy of infants? There will be implications for the health care system (for companies serving that segment) and for the development of products and services targeted at older (or younger) population.

(ii) *Geographic Distribution:* Population shifts from one region of a nation to another or from non-metropolitan to metropolitan areas may have an impact on a company's strategic competitiveness. Issues that should be considered include:

- The attractiveness of a company's location may be influenced by governmental support.
- Companies may have to consider relocation if population shifts have a significant impact on the availability of a qualified workforce.
- The concepts of working-at-home and commuting electronically on the information highway have also started in India in a very small level. These may imply changes in recruiting and managing the workforce.

(iii) *Ethnic Mix:* This reflects the changes in the ethnic make-up of a population and has implications both for a company's potential customers and for the workforce. Issues that should be addressed include:

- What do changes in the ethnic mix of the population imply for product and service design and delivery?
- Will new products and services be demanded or can existing ones be modified?

- Managers prepared to manage a more culturally diverse workforce?
- How can the company position itself to take advantage of increased workforce heterogeneity?

(iv) *Income Distribution:* Changes in income distribution are important because changes in the levels of individual and group purchasing power and discretionary income often result in changes in spending (consumption) and savings patterns. Tracking, forecasting, and assessing changes in income patterns may identify new opportunities for companies

12.2 Economic Environment

The economic environment refers to the nature and direction of the economy in which a company competes or may compete. The economic environment includes general economic situation in the region and the nation, conditions in resource markets (money market, manpower market, raw material components, services, supply markets and so on) which influence the supply of inputs to the enterprise, their costs, quality, availability and reliability of supplies.

Economic environment determines the strength and size of the market. The purchasing power in an economy depends on current income, prices, savings, circulation of money, debt and credit availability. Income distribution pattern determines the marketing possibilities. The important point to consider is to find out the effect of economic prospect and inflation on the operations of the firms. Strategists must scan, monitor, forecast, and assess a number of key economic factors mentioned in the table below for both domestic and key international markets.

Key Economic Factors

♦ Shift to a service economy	♦ Availability of credit
♦ Level of disposable income	♦ Propensity of people to spend
♦ Interest rates	♦ Inflation rates
♦ Tax rates	♦ Money market rates
♦ Government budget deficits	♦ Gross national product trend
♦ Consumption patterns	♦ Trade Block Formations
♦ Demand shifts for different categories of goods and services	♦ Income differences by region and consumer groups
♦ Price fluctuations	♦ Worker productivity levels
♦ Global movement of labour and capital	♦ Monetary & Fiscal policies
♦ Stock market trends	♦ Foreign countries' economic conditions
♦ Import/export factors	♦ Company of Petroleum Exporting Countries (OPEC) policies
♦ Coalitions of Countries/ Regional blocks	♦ Unemployment trends

12.3 Political-Legal Environment

This is partly general to all similar enterprises and partly specific to an individual enterprise. It includes such factors as the general state of political development, the degree of politicalization of business and economic issues, the level of political morality, the law and order situation, political stability, the political ideology and practices of the ruling party, the purposefulness and efficiency of governmental agencies, the extent and nature of governmental intervention in the economy and the industry, Government policies (fiscal, monetary, industrial, labour and export-import policies), specific legal enactments and framework in which the enterprise has to function and the degree of effectiveness with which they are implemented, public attitude towards business in general and the enterprise in particular and so on. There are three important elements in political-legal environment.

(i) Government: Business is highly guided and controlled by government policies. Hence the type of government running a country is a powerful influence on business: A strategist has to consider the changes in the regulatory framework and their impact on the business.

Taxes and duties are other critical area that may be levied and affect the business. For example, introduction of Fringe benefits Tax has major impact on the business.

(ii) Legal: Business Organizations prefer to operate in a country where there is a sound legal system. However, in any country businesses must have a good working knowledge of the major laws protecting consumers, competitions and organizations. Businesses must understand the relevant laws relating to companies, competition, intellectual property, foreign exchange, labour and so on.

(iii) Political: Political pressure groups influence and limit organizations. Apart from sporadic movements against certain products, service and organizations, politics has deeply seeped into unions. Also special interest groups and political action committees put pressure on business organizations to pay more attention to consumer's rights, minority rights, and women rights.

12.4 Socio-Cultural Environment

This is too general an entity which influence almost all enterprises in a similar manner. It is a complex of factors such as social traditions, values and beliefs, level and standards of literacy and education, the ethical standards and state of society, the extent of social stratification, conflict and cohesiveness and so forth.

Socio-cultural environment consist of factors related to human relationships and the impact of social attitudes and cultural values which has bearing on the business of the organization. The beliefs, values and norms of a society determine how individuals and organizations should be interrelated. The core beliefs of a particular society tend to be persistent. It is difficult for

businesses to change these core values, which becomes a determinant of its functioning.

Some of the important factors and influences operating in this environment are:

- Social concerns, such as the role of business in society, environmental pollution, corruption, use of mass media, and consumerism.
- Social attitudes and values, such as expectations of society from business, social customs, beliefs, rituals and practices, changing lifestyle patterns, and materialism.
- Family structure and changes in it, attitude towards and within the family, and family values.
- Role of women in society, position of children and adolescents in family and society.
- Educational levels, awareness and consciousness of rights, and work ethics of members of society.

The social environment primarily affects the strategic management process within the organization in the areas of mission and objective setting, and decisions related to products and markets.

12.5 Technological Environment

The most important factor, which is controlling and changing people's life, is technology. Technology has literally created wonder. Man could realise its dream of walking in the moon, traveling in spaceships, and go to the other side of the globe within few hours. They have already started dreaming of living of very extended life of hundreds years with the latest development of genetic sciences and technology.

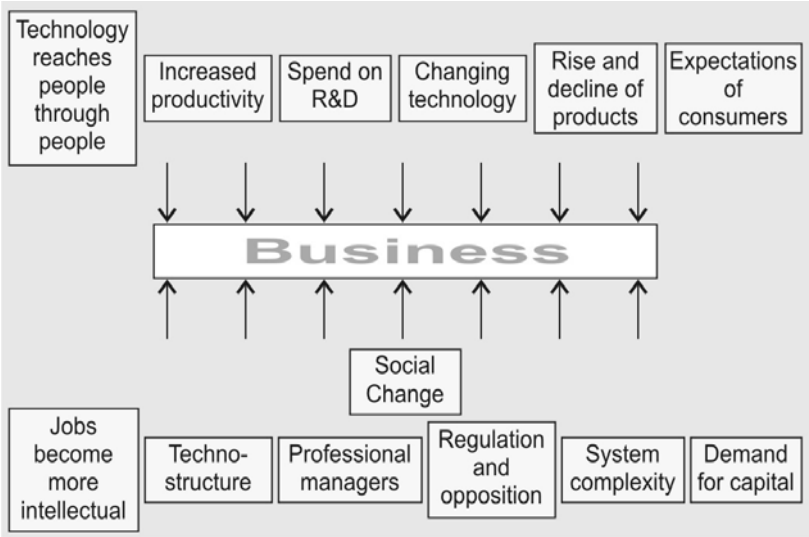


Figure: Interference between Business & Technology

Technology has changed the way people communicate with the advent of Internet and telecommunication system. Technology has changed the ways of how business operates now. This is leading to many new business opportunities as well as making obsolete many existing systems. The following factors are to be considered for the technological environment:

- The pull of technological change.
- Opportunities arising out of technological innovation.
- Risk and uncertainty of technological development.
- Role of R&D in a country and government's R&D budget.

Technology can act as both opportunity and threat to a business. It can act as opportunity as business can take advantage of adopting technological innovations to their strategic advantage. However, at the same time technology can act as threat if organisations are not able to adopt it to their advantage. For example, an innovative and modern production system can act as threat if the business is not able to change their production system. New entrants can always use availability of technological improvements in products or production methods that can be a threat to a business.

Technological opportunities and threats are not limited to the product or production. Technology permeates whole gambit of business. It can transform how a business acts and functions.

The technology and business are highly interrelated and interdependent also. The fruits of technological research and development are available to society through business only and this also improves the quality of life of the society. Hence, technology is patronized by business. Then again technology also drives business and makes a total change on how it is carried out. The interface between business and technology is explained in the figure: Interface between Business & Technology. Important technology-related issues that might affect a broad variety of companies include:

- Access to the "information highway" through the Internet which may enable large numbers of employees to work from home or provide strategists with access to richer sources of information,
- Business-to-business sales and exchanges,
- Providing customers with access to online shopping through the Internet.

For example, Dell Computer Corporation reduces its paperwork flow, schedules its payments more efficiently, and is able to coordinate its inventories efficiently and effectively by using the capabilities of the Internet. This helps to eliminate/reduce paperwork, flatten companies, and shrink time and distance, thus capturing a competitive premium for the company. Because the technological aspects are so important, some of the key questions that can be asked in assessing the technological environment are given below.

- What are the technologies {both manufacturing and information technologies} used by

the company?

- Which technologies are utilised in the company's business, products, or their parts?
- How critical is each technology to each of these products and businesses?
- Which external technologies might become critical and why? Will they remain available outside the company?
- What has been the investment in the product and in the process side of these technologies? For the company and for its competitors? Design? Production? Implementation and service?
- What are the other applications of the company's technologies? In which applications does the company currently participate and why? In which application does the company does not participate and why?
- Which technological investments should be curtailed or eliminated?
- What additional technologies will be required in order to achieve the current corporate business objectives?
- What are the implications of the technology and business portfolios for corporate strategy?

12.6 Global Environment

Today's competitive landscape requires that companies must analyse global environment as it is also rapidly changing. The new concept of global village has changed how individuals and organizations relate to each other. Further, new migratory habits of the workforce as well as increased offshore operation are changing the dynamics of business operation. Among the global environmental factors that should be assessed are:

- Potential positive and negative impact of significant international events such as a sport meet or a terrorist attack.
- Identification of both important emerging global markets and global markets that are changing. This includes shifts in the newly industrialised countries in Asia that may imply the opening of new markets for products or increased competition from emerging globally competitive companies in countries such as South Korea and China.
- Differences between cultural and institutional attributes of individual global markets.

Due to economic reforms, Indian businessmen are also out to see beyond the physical boundaries of the country. The Indian companies are acquiring business in different countries. The need to think and act from global perspective is universal. For a long time businessmen everywhere believed that home markets were adequate and safe. They never felt the need to explore the overseas markets in a big way. "If they could pick up some extra sales through exporting, these businessmen were more than satisfied. The scenario is different now. The companies are increasingly interested in globalising.

Nature of Globalization: Globalization means several things for several people. For some it is a new paradigm - a set of fresh beliefs, working methods, and economic, political and socio-cultural realities in which the previous assumptions are no longer valid. For developing countries, it means integration with the world economy. In simple economic terms, globalization refers to the process of integration of the world into one huge market. Such unification calls for removal of all trade barriers among countries. Even political and geographical barriers become irrelevant

At the company level, globalization means two things: (a) the company commits itself heavily with several manufacturing locations around the world and offers products in several diversified industries, and (b) it also means ability to compete in domestic markets with foreign competitors.

A company which has gone global is called a multinational (MNC) or a transnational (TNC). An MNC is, therefore, one that, by operating in more than one country gains *R&D,* production, marketing and financial advantages in its costs and reputation that are not available to purely domestic competitors. The global company views the world as one market, minimises the importance of national boundaries, sources, raises capital and markets wherever it can do the job best.

To be specific, a global company has three characteristics:

- It is a conglomerate of multiple units (located in different parts of the globe) but all linked by common ownership.
- Multiple units draw on a common pool of resources, such as money, credit, information, patents, trade names and control systems.
- The units respond to some common strategy. Nestle International is an example of an enterprise that has become multinational. It sells its products in most countries and manufactures in many. Besides, its managers and shareholders are also based in different nations.

A further development, perhaps, will be the *super-national enterprise.* It is a worldwide enterprise chartered by a substantially non-political international body such as IMF or World Bank. It operates as a private business without direct obligations. Its function is international business service, and it remains viable only by performing that service adequately for nations which permit its entry. With its integrative view, it should be able to draw the economic world closer together. It could serve all nations without being especially attached to anyone of them.

Why do companies go global?

There are several reasons why companies go global. These are discussed as follows:

- One reason could be the rapid shrinking of time and distance across the globe thanks to faster communication, speedier transportation, growing financial flows and rapid technological changes.
- It is being realised that the domestic markets are no longer adequate and rich.

Japanese have flooded the U.S. market with automobiles and electronics because the home market was not large enough to absorb whatever was produced. Some European companies have gone global for similar reason.

- According to Raymond Vernon companies that develop attractive new products sell them first in their home markets. Sooner or later, foreigners may learn about these products. At this stage, most companies would export the product or service rather than produce it abroad. But as foreign demand grows, the economics of foreign production change. Eventually, the foreign market becomes large enough to justify foreign investment.
- Another reason for going overseas may also vary by industry. Petroleum and mining companies often go global to secure a reliable or cheaper source of raw-materials. Some manufacturing companies, by contrast, have often ventured overseas to protect old markets or to seek new ones. For example cheap labour in India lure foreign investors.
- Companies often set up overseas plants to reduce high transportation costs. The higher the ratio of the unit cost to the selling price per unit, the more significant the transportation factor becomes.
- The motivation to go global in high-tech industries is slightly different. Companies in electronics and telecommunications must spend large sums on research and development for new products and thus may be compelled to seek ways to improve sales volume to support high overhead expenses. If domestic sales and exports do not generate sufficient cash flow, the companies naturally might look to overseas manufacturing plants and sales branches to generate higher sales and better cash flow.

The following developments are also responsible for transnational operation of companies.

- Increasing emphasis on market forces and a growing role for the private sector in nearly all developing countries;
- Rapidly changing technologies that are transforming the nature, organization, an location of international production;
- The globalization of firms and industries;
- The rise of services to constitute the largest single sector in the world economy; and regional economic integration, which has involved both the world's largest economies as well as select developing countries.

Manifestation of Globalization: Globalization manifests itself in many ways. important of them are:

- Configuring anywhere in the world: An MNC can locate its different operations in different countries on the basis of raw material availability, consumer markets and low-cost labour.
- Interlinked and independent economies: In terms of economic-welfare, globalization

refers to the unique economically interdependent international environment. Each country's prosperity is interlinked with the rest of the world. No nation can any longer hope to lead an existence of solitude and isolation in which only domestic industries can function.

- Lowering of trade and tariff barriers: The apparent and real collapse of international trade barriers proposes a new global cooperative arrangement and a redefinition of roles of state and industry. The trend is towards increased privatization of manufacturing and services sectors, less government interference in business decisions and more dependence on the value-added sector to gain market place competitiveness. World over, governments are pulling out from commercial business. The trade tariffs and custom barriers are getting lowered, resulting in cheaper and abundant supply of goods.
- Infrastructural resources and inputs at International prices: Infrastructural inputs must be ensured at competitive prices, if the companies were to compete globally. The advantages of cheap labour (and other inputs) evaporate in the face of continuous inflation and high infrastructural costs.
- Increasing trend towards privatization: Governments are everywhere withdrawing from owning and running business enterprises. Private entrepreneurs are given greater access and freedom to run business units. The role of government is reduced to the provider of infrastructure for private business to prosper.
- Entrepreneur and his unit have a central economic role: In the emerging world order, the entrepreneur and his unit become central figures in the process of economic growth and development of a nation. Given the right environment, businesses are able to innovate, bring in new products, and contribute to nation's wealth. For the risk he takes and efforts he puts in, the businesses are rewarded with profits. Related to this is the viability of the business unit. Only firms which are cost effective and quality oriented survive and prosper. Weak and marginal firms die their natural death.
- Mobility of skilled resources: Skilled labour was once considered to be the decisive factor in plant location and even in determining comparative advantage of a nation. Skilled labour is highly mobile. Modern factories use highly skilled labour which is freely mobile. Where labour is unskilled, managements are spending vast sums of money to train workers become skilled in their jobs. Besides labour, other factors of production (land and capital) are also mobile. A developing country which is long on land and short on capital can invite foreign investment and make good the deficiency. Similarly, a developed country which is long on capital and short on land can use a developing country as a base for its manufacturing operations.

  Thus, the traditional factors of production, viz., land, labour and capital, are no more immobile or restricted for usage with. They are transferable from any part of the world to any other part of the globe. The entire world has become a global village.

- **Market-side efficiency:** Integration of global markets implies that costs, quality processing time, and terms of business become dominant competition drivers. Customers can make a genuine choice of products and services on the basis of maximum value for money. The exclusive markets which were once enjoyed are no longer available to a firm. The inexorable pressure of technology and need for its integration means that customers no longer have to be satisfied with shoddy products and services provided by the state monopolies.
- **Formation of regional blocks:** A final corollary to globalization is the formation of trade blocks. The reasons for forming such blocks are obvious. Countries, like corporations, have to form strategic alliances to ward off economic and technological threats and leverage their respective comparative and competitive advantages. The signing of NAFTA (North American Free Trade Area) among N. America, Canada, and Mexico creates new markets and manufacturing opportunities for these countries and threatens to disrupt the plans and strategies of world powers such as Japan. Similarly formation of European Union and ASEAN affects the World trade balance.

  India is part of South Asian Association for Regional cooperation (SAARC). SAARC consist of seven South Asian Countries with Bangladesh, Bhutan, Maldives, Nepal, Pakistan and Sri Lanka as its members in addition of India. SAARC endevours to accelerate economic growth in the Region. It also strives for social progress and cultural development in the region, promotion of active collaboration and mutual assistance in the economic, social, cultural, technical and scientific fields and strengthening of cooperation among the member states in the International forums on matters of common interest.

13. PESTLE Analysis

The term PESTLE is used to describe a framework for analysis of macro environmental factors. PESTLE analysis involves identifying the political, economic, socio-cultural, technological, legal and environmental influences on an organization and providing a way of scanning the environmental influences that have affected or are likely to affect an organization or its policy. 'PESTLE analysis is an increasingly used and recognized term, replacing the traditional framework for monitoring environment known as PEST analysis. PESTLE is an acronym for:

- P- political
- E- economic
- S- socio-cultural
- T- technological
- L- legal
- E- environmental

The PESTLE analysis is a simple to understand and quick to implement. The advantage of this tool is that it encourages management into proactive and structured thinking in its decision making.

The Key Factors

- Political factors are how and to what extent a government intervenes in the economy and the activities of corporate. Political factors may also include goods and services which the government wants to provide or be provided and those that the government does not want to be provided. Furthermore, governments have great influence on the health, education and infrastructure of a nation.
- Economic factors have major impacts on how businesses operate and take decisions. For example, interest rates affect a firm's cost of capital and therefore to what extent a business grows and expands. Exchange rates affect the costs of exporting goods and the supply and price of imported goods in an economy. The money supply, inflation, credit flow, per capita income, growth rates have a bearing on the business decisions.
- Social factors affect the demand for a company's products and how that company operates.
- Technological factors can determine barriers to entry, minimum efficient production level and influence outsourcing decisions. Furthermore, technological shifts can affect costs, quality, and lead to innovation.
- Legal factors affect how a company operates, its costs, and the demand for its products.
- Environmental factors affect industries such as tourism, farming, and insurance. Growing awareness to climate change is affecting how companies operate and the products they offer--it is both creating new markets and diminishing or destroying existing ones.

On the basis of these, it should be possible to identify a number of key environmental influences, which are in effect, the drivers of change. These are the factors that require to be considered in the matrix. Then transpose the final items that we have identified from your list to a PESTLE matrix.

The PESTLE Matrix

Political	Economic
• Political stability • Political principles and ideologies • Current and future taxation policy • Regulatory bodies and processes • Government policies • Government term and change • Thrust areas of political leaders.	• Economy situation & trends • Market and trade cycles • Specific industry factors • Customer/end-user drivers • Interest and exchange rates • Inflation and unemployment • Strength of consumer spending

Social • Lifestyle trends • Demographics • Consumer attitudes and opinions • Brand, company, technology image • Consumer buying patterns • Ethnic/religious factors • Media views and perception	Technological • Replacement technology/solutions • Maturity of technology • Manufacturing maturity and capacity • Innovation potential • Technology access, licensing, patents • Intellectual property rights and copyrights
Legal • Business and Corporate Laws • Employment Law • Competition Law • Health & Safety Law • International Treaty and Law • Regional Legislation	Environmental • Ecological/environmental issues • Environmental hazards • Environmental legislation • Energy consumption • Waste disposal

14. Strategic Responses to the Environment

The business organization and its many environments have innumerous interrelationship that at times, it becomes difficult to determine exactly where the organization ends and where its environment begins. It is also difficult to determine exactly what business should do in response to a particular situation in the environment. Strategically, the businesses should make efforts to exploit the opportunity ad thought the threats.

In this context following approaches may be noted:

(i) Least resistance: Some businesses just manage to survive by way of coping with their changing external environments. They are simple goal-maintaining units. They are very passive in their behaviour and are solely guided by the signals of the external environment. They are not ambitious but are content with taking simple paths of least resistance in their goal-seeking and resource transforming behaviour.

(ii) Proceed with caution: At the next level, are the businesses that take an intelligent interest to adapt with the changing external environment. They seek to monitor the changes in that environment, analyse their impact on their own goals and activities and translate their assessment in terms of specific strategies for survival, stability and strength. They regard that the pervasive complexity and turbulence of the external environmental elements as 'given' within the framework of which they have to function as adaptive-organic sub-systems. This is an admittedly sophisticated strategy than to wait for changes to occur and then take corrective-adaptive action.

(iii) Dynamic response: At a still higher sophisticated level, are those businesses that regard the external environmental forces as partially manageable and controllable by their actions. Their feedback systems are highly dynamic and powerful. They not merely recognise and ward off threats; they convert threats into opportunities. They are highly conscious and confident of their own strengths and the weaknesses of their external environmental 'adversaries'. They generate a contingent set of alternative courses of action to be picked up in tune with the changing environment.

Shaping external environment

How far is it possible for organizations to actively shape their relevant environments is an critical question? Can human organizations ever become such super-powerful entities? Is total environmental control and command worth the cost? What are the self-defeating elements in such an approach? Admittedly, the very dominating behaviour of command organizations may generate powerful countervailing pressures and forces in the environment. It should be remembered that the external environment in larger and more inclusive than the individual organization; presumably the former commands more resources and its interests and values are much broader than those of the latter.

An innovative and autonomous organization generates its own constraints. It is not above the rule of law and logic of the external environment. Within certain limits, such an organization can shape part of its relevant external environment on a reciprocal basis.

15. Competitive Environment

The essence of strategy formulation is coping with competition. Although competition makes organizational working difficult, intense competition is neither a coincidence nor bad luck. All organizations have competition. Multinationals and large organizations clash directly on every level of product and service. Mid-sized and small business also chases same customers and find that prices and product quality are bounded by the moves of their competitors. Even large public sector monopolies are gradually getting privatised and facing competition. The monopolies enjoyed by the Bharat Sanchar Nigam Ltd and Mahanagar Telephone Nigam Ltd have faded away after entry of private players. For a single business organization the competition spells out freedom of entry and exit in the market and affects its prices and scale of operations.

The benefits of competition are also enjoyed by the society and the markets in which organisations operate. The customers are able to get products at lower costs and better quality. They get better value of their money because of competition.

The nature and extent of competition that a business is facing in the market is one of the major factors affecting the rate of growth, income distribution and consumer welfare. Businesses have to consider competitors' strategies, profits levels, costs, products and services when preparing and implementing their business plans.

While formulating strategies, organizations have to separately identify and concentrate on the

competitors who are significantly affecting the business. Lesser attention may be given to smaller competitors who have little or no impact the business. There can be several competitors vying to satisfy same needs of customers. Competition is not necessarily restricted to same product or services. Coke and Pepsi may be obvious competitors. At the same time they have to compete with other companies such as Hindustan Lever Ltd whose Kissan squashes will be directed towards same needs. They have to also compete with natural juices such as Real.

A better understanding of the nature and extent of competition may be reached by answering the following questions:

(i) Who are the competitors?

(ii) What are their product and services?

(iii) What are their market shares?

(iv) What are their financial positions?

(v) What gives them cost and price advantage?

(vi) What are they likely to do next?

(vii) Who are the potential competitors?

Cooperation in a Competitive Environment: In economics we study oligopoly, wherein a small number of only manufactures/sellers of a product may join together to have monopolistic behaviour. An example of oligopoly can be Organization of the Oil Exporting Countries (OPEC), which is collective group of nations extracting and exporting oil. Its aim according to its Statute, is 'the coordination and unification of the petroleum policies of member countries and the determination of the best means for safeguarding their interests, individually and collectively; ways and means of ensuring the stabilization of prices in international oil markets with a view to eliminating harmful and unnecessary fluctuations. The cooperation in organizations forming *cartels* (a term used to define the groups in oligopoly) may be in form of deciding market shares, prices and profits. It is not necessary that the organizations form explicit cartels as they may have tacit arrangements not known to general public.

The cooperation may also be witnessed in highly competitive business environment. Tata and Fiat have arrangements in relations to cars. Such cooperation is not necessarily restricted to the organizations producing or dealing in same product or services. They may identify some common interest for cooperation between them. A cold drink manufacture may enter into arrangement with a chain of restaurants to offer its beverages to the clients of restaurants. Lately, various credit card companies are entering into arrangements with other businesses to launch co-branded credit cards. Such arrangements help in reaching greater number of customers.

The benefits of cooperation are also seen in Japan, where large cooperative networks of businesses are known as *kieretsus*. These are formed in order to enhance the abilities of individual member businesses to compete in their respective industries. A *kieretsu* is a

loosely-coupled group of companies, usually in related industries. *Kieretsu* members are peers and may own significant amounts of each other's stock and have many board members in common. However, they are different from conglomerates (Common in western countries and also found in India) wherein all members are lineated through ownership pattern. A *kieretsu* also differs from a consortium or an association, as the primary purpose of a *kieretsu* is not to share information or agree industry standards, but to share purchasing, distribution or any other functions. In *Kieretsu* members remain independent companies in their own right: the only strategy they have in common is to prefer to do business with other *kieretsu* members, both when buying and when selling.

Cooperation on account of family ownership: Theoretically, cooperation generates automatically in businesses owned by a same family. The ownership, groups are engaged in the management of their enterprise in a direct manner. Commonly, the ownership group is nothing but a family and its kith and kin. In India, a very large number of business enterprises, big, medium and small, are family-managed enterprises. These include large business houses such as Tata, Birla, Godrej, Reliance, Modi, Escorts and *et al*. Major decisions and sometimes even minor decisions are made by members of the family who manage the enterprise. The interests of the family largely influence the managerial decisions and activities of the enterprise. There is a total identity between the needs and goals of the family and of the enterprise.

Sometimes, quarrels and conflicts among the managing members of the family on family matters tend to distort their behaviour in managing the enterprise also and thereby damage its functioning. Succession remains a tricky and conflicting issue in businesses. Be it the Ambanis of Reliance Industries, the Bajajs of Bajaj Auto, the Nandas of Escorts, or the Modis of Modi Rubber - each family has, in the recent past, faced succession and ownership issues and found them tough to resolve. However, one can count several counter examples of family-run businesses that have resolved these issues amicably. The Murugappa Group in the South, the Burmans of Dabur India and the Thapars have settled succession issues without coming into the public eye.

16. Porter's Five Forces Model - Competitive Analysis

To gain a deep understanding of a company's industry and competitive environment, managers do not need to gather all the information they can find and waste a lot of time digesting it. Rather, the task is much more focused. Thinking strategically about a company's competitive environment entails using some well defined concepts and analytical tools.

The character, mix, and subtleties of competitive forces are never the same from one industry to another. A powerful and widely used tool for systematically diagnosing the significant competitive pressures in a market and assessing the strength and importance of each is the *five-forces model of competition.(see figure)* This model holds that the state of competition in an industry is a composite of competitive pressures operating in five areas of the overall market:

- Competitive pressures associated with the market manoeuvring and jockeying for buyer patronage that goes on among *rival sellers* in the industry.
- Competitive pressures associated with the threat of *new entrants* into the market.
- Competitive pressures coming from the attempts of companies in other industries to win buyers over to their own *substitute products.*
- Competitive pressures stemming from *supplier* bargaining power and supplier-seller collaboration.
- Competitive pressures stemming from *buyer* bargaining power and seller-buyer Collaboration.

The way one uses the five-forces model to determine what competition is like in a given industry is to build the picture of competition in three steps:

Step 1: Identify the specific competitive pressures associated with each of the five forces.

Step 2: Evaluate how strong the pressures comprising each of the five forces are (fierce, strong, moderate to normal, or weak).

Step 3: Determine whether the collective strength of the five competitive forces is conducive to earning attractive profits.

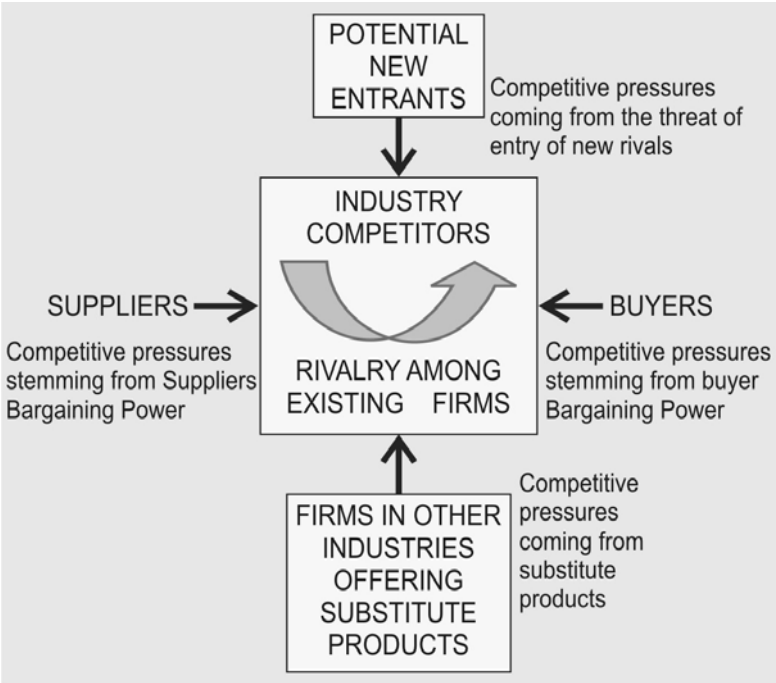


Figure: The Five Force Model of Competition

Threat of new entrants: New entrants are always a powerful source of competition. The new capacity and product range they bring in throw up new competitive pressure. And the bigger the new entrant, the more severe the competitive effect. New entrants also place a limit on prices and affect the profitability of existing players.

Bargaining power of customers: This is another force that influences the competitive condition of the industry. This force will become heavier depending on the possibilities of the buyers forming groups or cartels. Mostly, this is a phenomenon seen in industrial products. Quite often, users of industrial products come together formally or informally and exert pressure on the producer in matters such as price, quality and delivery. Two top CDMA service providers Reliance and Tata Teleservices had put a simultaneous pressure on Qualcomm to reduce the royalties on the CDMA based handsets.

Such collusion on the part of buyers can be a major force in some industries. The bargaining power of the buyers influences not only the prices that the producer can charge but also influences in many cases, costs and investments of the producer because powerful buyers usually bargain for better services which involve costs and investment on the part of the producer.

Bargaining power of suppliers: Quite often suppliers, too, exercise considerable bargaining power over companies. The more specialised the offering from the supplier, greater is his clout. And, if the suppliers are also limited in number they stand a still better chance to exhibit their bargaining power. The bargaining power of suppliers determines the cost of raw materials and other inputs of the industry and, therefore, industry attractiveness and profitability.

Rivalry among current players: The rivalry among existing players is an idea that can be easily understood. This is what is normally understood as competition. And it is obvious that for any player, the competitors influence prices as well as the costs of competing in the industry, in production facilities product development, advertising, sales force, etc.

Threats from substitutes: Substitute products are a latent source of competition in an industry. In many cases they become a major constituent of competition. Substitute products offering a price advantage and/or performance improvement to the consumer can drastically alter the competitive character of an industry. And they can bring it about all of a sudden. For example, coir suffered at the hands of synthetic fibre. Wherever substantial investment in R&D is taking place, threats from substitute products can be expected. Substitutes, too, usually limit the prices and profits in an industry.

So, in addition to existing rivals or competitors proper, forces such as new entrants, customers, suppliers, and substitutes have all to be viewed as forces governing competition in the industry. A firm has to give due weightage to each of these forces as a fight can emerge from any quarter.

The five forces together determine industry attractiveness/profitability. This is so because these forces influence the causes that underlie industry attractiveness/profitability. For

example, elements such as cost and investment needed for being a player in the industry decide industry profitability, and all such elements are governed by these forces. The collective strength of these five competitive forces determines the scope to earn attractive profits. The strength of the forces may vary from industry to industry..

Summary

We began this chapter by understanding the concept of business. A business is society's organ of economic expansion, growth and change. A business for our purpose can be any activity consisting of purchase, sale, manufacture, processing, and/or marketing of products and/or services. The objectives and the environmental influences on business are also discussed in this chapter. This chapter explains the three basic goals of environmental analysis and business environment with its characteristics such as complexity, dynamism, multi-faceted nature and far reaching impact. The relationship between organization and its environment is also discussed in terms of interactions between them in several major areas.

The environment in which an organization exists could be broadly divided into two categories - external and internal environment. The external environment is further classified into two categories micro and macro environment. Micro environment relates to those forces that fall within immediate small periphery of an organization. It consists of customers, competitors, organization, market, suppliers, intermediaries, etc. Macro environment is at a distance and has broader dimensions. It consists of demographic, economic, political-legal, socio-cultural, technological and global environment, etc.

We have also introduced PESTLE analysis which is used to analyze the external environment. Organizations may follow different approaches of strategic responses to the environment has also discussed in this chapter.

To gain a deeper understanding of competitive environment of a business organisation, we learned, Michael Porter's five forces model. The five forces – threat of new entrants, bargaining power of customers, bargaining power of suppliers, rivalry among current players and threats from substitutes – impact organizations in significant and different manner.