

Chapter-1 Business Environment

CONCEPT OF BUSINESS ENVIRONMENT

Like HUL, each organisation is an integral part of society. These organisations exist and operate in a dynamic environment comprising various groups, e.g., customers, competitors, vendors, regulatory authorities and government agencies, media, banking and financial institutions, etc. All such groups exercise influence in the organisations.

We all are continuously engaged in some activity or other in order to satisfy our unlimited wants. We use the term 'Business' in one way or other in our daily lives. *For example*, a consumer needs a product; he visits the nearest retail shop. To arrange that product, retailer contacts the wholesaler who in turn gets the product from the manufacturer. This cycle of business continues to satisfy human wants. Business is an economic activity, which is related with continuous and regular production and distribution of goods and services for satisfying human wants.

"Business is an institution which produces goods and services demanded by people".

—Brown and Petrello

The word "Environment" is derived from the French word "*Environ*" which means "surrounding", i.e., external conditions involving manifold variables like objects or conditions affecting the development and growth of all living organisms including human beings. Environment can be divided into two broad categories: micro and macro. Micro environment consists of two categories of factors: external and internal. Micro environment has direct impact on the business while macro environment comprises only external factors and is the general environment. Let us now discuss business environment in detail.

A business enterprise is an open system. It gets resources from the environment and supplies its goods and services to the environment. The environment surrounding the business enterprise involves multiple set of complex economic, social or political forces including suppliers, customers, competitors, etc., having an impact on the operations of the enterprise. Every business organisation operates in a distinctive environment, as it cannot exist in vacuum. An environment influence business and also gets affected by its activities. There is a close and continuous interaction between business and its environment. This interaction helps in strengthening the business enterprise and using its resources more effectively. A business can be established, but to successfully sustain it, the environment needs to be understood. *For example*, a business enterprise would need raw material from different vendors, finances would have to be raised from banks or financial institutions, labour to produce, customers to whom the goods would be sold, etc. All these activities will have to be carried out within the overall prevailing economic environment and the legislative framework imposed by the government.

"Business environment is the aggregate of all conditions, events and influences that surround and affect it".

—Keith Davis

"Business Environment encompasses the climate or set of conditions—economic, social, political or institutional—in which business operations are conducted."

—Arthur M. Weimer

FEATURES OF BUSINESS ENVIRONMENT

Various features of business environment are as follows:

1. **Integral:** Environment is an integral part of any business. No business enterprise can work in an isolated manner or vacuum. Environment influences business and also gets affected by its activities. *For example*, business organisations continuously interact with the environment for inputs like raw

materials, labour, etc., and transform the inputs received into final goods and services and supply the same to diverse customers.

2. **Uncertainty and Risk:** Uncertainty is an inherent part of business environment. Uncertainty implies lack of precise forecast of future happenings. There is no single best way to address environmental uncertainty. Generally, uncertainty like earthquake may impact all entities but certain uncertainty may be business-specific, *e.g.*, fluctuation in exchange rates, oil prices, etc. Thus, risk is inherent part of any business environment which cannot be avoided. The best way to cope with uncertainty is to gather sufficient information about the various factors affecting the business environment.
3. **Relativity:** Business environment is a relative concept. The economic environment, local laws and regulations, climatic conditions, etc., differ from one country to another, from one region to another within the same country or even over a period of time within the same region. Thus, business environment shall be different for different business enterprises.
4. **Dynamic:** Business environment is dynamic, that is, it keeps changing with time. *For example*, change in taste and preferences of customers, change in government policies, etc., affect the business and its working.
5. **Internal and External Forces:** Business environment comprises internal and external factors. Internal environment includes plans, policies, goals, employees, etc. External environment comprises micro and macro environment. Micro environment has direct impact on the business, *e.g.*, customers, suppliers, etc. whereas Macro environment is the general environment, *e.g.*, social, economic, technological factors, etc.
6. **Opportunities and Threats:** Business environment presents both opportunities and threats. An opportunity is a favourable condition which enables an organisation to strengthen its position. A threat is an unfavourable condition that affects an organisation's position adversely.
7. **Complexity:** Environment comprises multiple, diverse and inter-related factors. Naturally, all such factors interact with each other and thus, it is a very complex scenario and one cannot work out the individual effect of each factor. Any change in the environment can adversely affect the business organisation. The changes are unpredictable and non-uniform. Therefore, analysis of business environment becomes quite difficult.

SIGNIFICANCE OF UNDERSTANDING BUSINESS ENVIRONMENT

The understanding of business environment is quite significant, particularly in the context of a highly complex and globalised economic environment. Its significance is explained as under:

1. **Helps in identification of opportunities and threats:** An analysis of the external environment helps the business enterprise to identify the opportunities in the market. Early identification of business opportunities will help to capture the market first without losing the market share in favour of competitors. Every business has to face threat from its competitors. Early identification of threats and challenges helps the business to plan strategically and deal with the situations. Also, it helps to minimise the risk of loss.
2. **Helps in identification of internal environment:** Business enterprises analyse the internal environment such as organisation structure, business policy, etc. to assess their own strengths and weaknesses. The management information system helps to analyse and predict business environmental changes.
3. **Helps in understanding the economic environment:** The understanding of prevailing economic environment includes economic policy and market conditions so as to assess their impact on the business from different perspectives. For instance, business environment helps in understanding economic policies like export-import policy, monetary policy, industrial policy, etc., which have

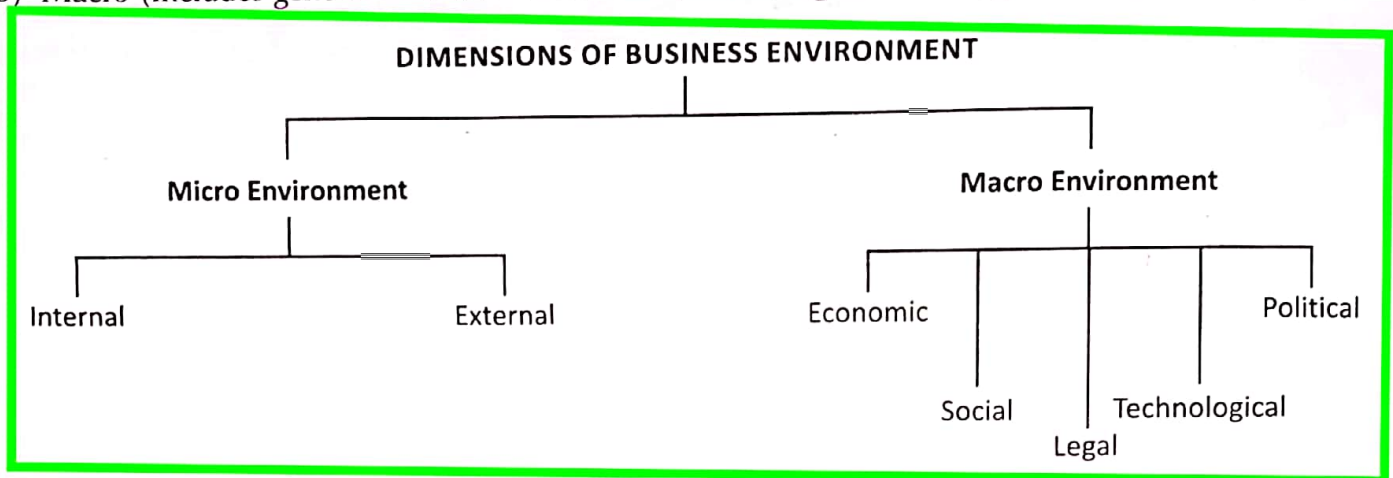
a significant impact on business. The study of business environment also helps in understanding the prevailing market structure and demand-supply relationship necessary from operational point of view.

4. **Helps in understanding future problems and prospects:** The study of business environment helps the business enterprise to understand future problems and prospects in advance. This enables the enterprise to plan for the problems and cope with them.
5. **Helps in the growth of business:** Understanding of business environment helps the business enterprise to make changes in its policies for capturing the market, facing competition, etc., which in turn helps in the growth and survival of the business.

DIMENSIONS OF BUSINESS ENVIRONMENT

The dimensions or the factors constituting the business environment are divided into two broad categories:

- (a) Micro (includes internal and external factors)
- (b) Macro (includes general factors like economic, social, legal, technological and political factors)



Factors constituting business environment are considered important for taking decisions and for improving the operations of a business enterprise. These factors are briefly discussed below:

I. Micro Environment

Micro environment refers to the internal and external factors which are close to a business that have a direct impact on its business operations and success. Micro Environment is also termed as the Direct Environment. It may be classified into two categories; viz, internal and external factors.

A. Internal Factors

Forces or conditions or surroundings within the boundary of the organisation are the elements of the internal micro environment. Internal factors can be controlled because these are within the decision-making power of the business enterprise. *For example*, a business enterprise can change the internal policies to keep pace with the changing environment. Some of the internal factors which influence the business are as follows:

- (i) **Management Structure:** Management structure includes the composition of the board of directors, pattern of shareholding, organisational structure, etc. These factors influence the decision-making.
- (ii) **Value System:** The value system of an organisation means the beliefs that help the organisation in achieving its objective. Value system of a business enterprise has an important bearing on the choice of business, policies, behaviour towards employees, society, etc.

- (iii) **Mission & Objectives:** The objective of any business is to maximise its profits. However, mission is the overall purpose for the existence of business enterprise. Objective is a much narrower concept as compared to mission. Both Objective and Mission influence short-term and long-term decision-making of the business and determine its strength and weaknesses.
- (iv) **Organisational Culture:** Corporate culture is an important factor for determining the internal environment of a company. Top-level management and lower-level managers communicate freely in open type of corporate culture. However, in closed type of corporate culture, decisions are taken by top-level managers only and there is no participation of the middle and lower level management. The success of any business depends mainly on creating parity between all levels of management.
- (v) **Human Resources:** The success of a business enterprise depends to a great extent on the skills and capabilities of its employees. Employee-friendly management is most likely to achieve the desired objectives. Employees should be kept motivated by providing various benefits like, bonus, good performance appraisals, awards and recognition, etc. A well-motivated employee helps a business to effectively and efficiently achieve its objectives.
- (vi) **Technological Capabilities:** Technological capabilities of a business enterprise determine its competitive edge which is an important factor in determining its work efficiency. A business enterprise should keep pace with the latest technological changes going on in the environment so that it can produce goods and services efficiently. This also helps in reducing the cost of production, thereby increasing the profits.
- (vii) **Brand Equity:** While raising finance, entering into contracts, launching new products, etc., the image and position of a company in the market plays a vital role. The experience of the existing customer base reflects the brand power of the business. A business enterprise should always focus on providing quality goods and services so as to maintain its brand equity in the market.

B. External Factors

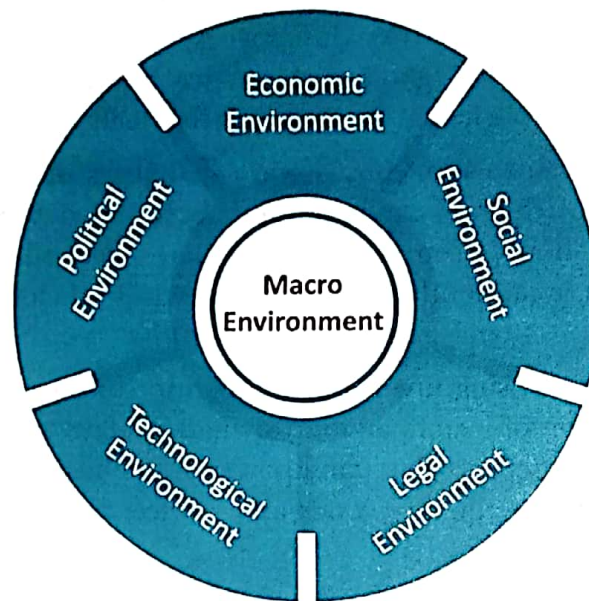
An external environment is comprised of all those outside factors or influences that impact the operation of a business enterprise. Micro external forces have a significant effect on business operations of a firm. Some of the external factors which influence the business are as follows:

- (i) **Suppliers:** Inputs such as raw material, fuel, etc., are provided by the suppliers and help in smooth conduct of the business. A business enterprise should have more than one supplier so that change in policies of one supplier does not affect the smooth functioning of the business.
- (ii) **Competitors:** Business firms compete with each other to gain competitive edge. They constantly watch the competitor's policies and adjust their policies accordingly.
- (iii) **Customers:** Since sale of a product or service is critical for a firm's survival and growth, customers must be satisfied with the performance of the business. A business enterprise supplies goods and services to different categories of customers like households, government, foreign customers, etc. A business firm must understand the needs and requirements of its customers so as to ensure success.
- (iv) **Market Intermediaries:** Market intermediaries are the links that help to promote, sell and distribute the products to final consumers. Market intermediaries include agents and merchants such as wholesalers, retailers, etc. They are an important link between a business enterprise and its buyers. A business must maintain good relations with the intermediaries if it has to succeed in this age of intense competition.

- (v) **Public:** Public is any group that has an actual or potential interest in or impact on an organisation's ability to achieve its objectives. Business enterprises should observe the behaviour of the public in making policies. The existence of various types of public groups such as women's association, consumer protection groups, citizen associations, etc., influences the working of the business enterprises.

2. Macro Environment

Macro environment refers to the general environment that can affect the working of all business enterprises. It influences the business either indirectly or distantly because the business is not continuously interacting with the Macro Environment. Therefore, Macro Environment is also known as Indirect Environment. Macro Environment factors are uncontrollable. These comprise the following elements:



(i) Economic Environment

Economic Environment refers to all those economic factors, which have a bearing on the functioning of a business enterprise. Economic Environment impacts the business environment directly, e.g., rise in income of people increases the demand for goods and vice versa, increase in inflation rate increases the cost of living, etc. Following are the main components of Economic Environment of a business:

- (a) Economic policies such as industrial policy, monetary policy, etc.
- (b) Inflation rate, tax rates, interest rates, etc.
- (c) Demand and Supply pattern
- (d) Industrial and economic development
- (e) General price level changes
- (f) Composition of trade, pattern of investment etc.
- (g) Economic system (budgets, five-year plans, etc.)
- (h) Infrastructure (transportation, power, etc.)

(ii) Social Environment

Social Environment of business comprises all factors which socially affect a business enterprise. Social factors include customs, fashions, traditions, level of education, religious values, etc. *For example,* the young generation prefers to shop online while older generation will prefer traditional shopping methods, i.e., by visiting the stores. Following are the main components of Social Environment:

- (a) Educational level
- (b) Demographic trends (growth, structure and movement of population)
- (c) Customs, culture and traditions—as per culture and tradition, festivals like Eid, Diwali, Xmas, etc., provide opportunities for consumer durables, restaurants, sweets, etc.
- (d) Social trends—the craze for health and fitness led to a revolution in establishing fitness spas as well as diet foods.
- (e) Social concerns (e.g., concern for pollution)
- (f) Business ethics and values

(iii) Legal Environment

The legal or regulatory environment comprises diverse laws, e.g., the Indian Contract Act, 1872, the Sale of Goods Act, 1930, the Consumer Protection Act, 1986, various other industrial and labour laws, etc., passed by the government of a country, court judgments, administrative orders issued by government authorities etc. For instance, companies in India are required to comply with the requirements of the Companies Act, 2013. It is important for the entrepreneurs to understand the legal framework in running the business smoothly and to avoid legal consequences, if any.

(iv) Technological Environment

Technological Environment includes the discovery of new methods of producing goods and services, new techniques of operating business, innovations and improvements in the existing method of doing business, etc. The survival of a business largely depends upon its technological advancement. *For example*, innovations in mobile industry by the entry of smartphones had a great impact on camera companies like Kodak.

(v) Political Environment

Political environment in a country affects the business organisations. The political environment may change because of the policies of governments. Following factors affect the political environment:

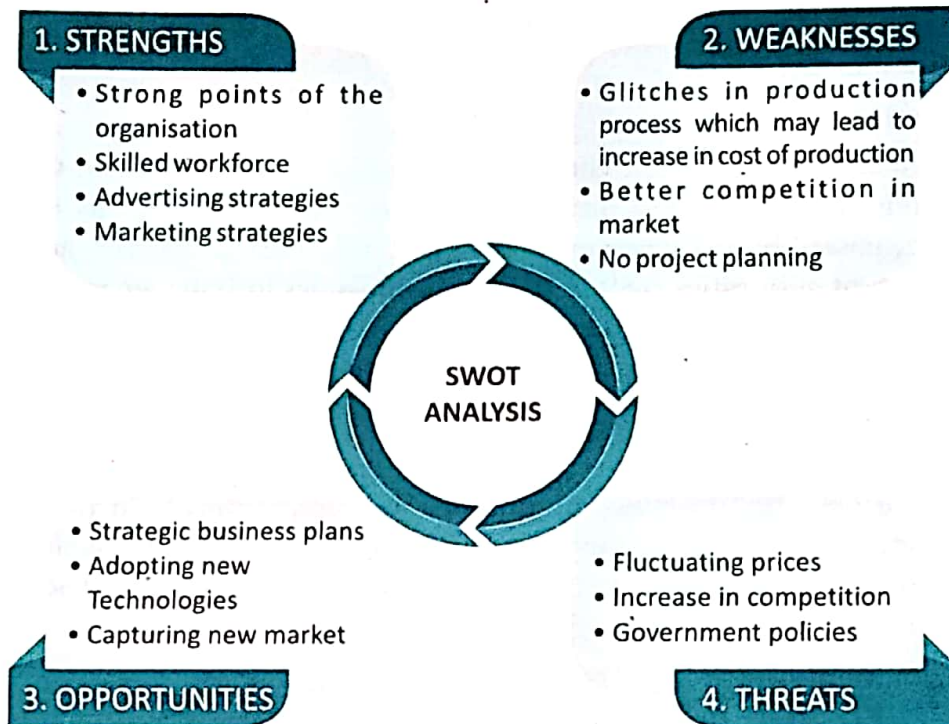
- (a) Policies of the ruling party
- (b) Political stability
- (c) Extent of government intervention in business
- (d) Type of Government (i.e., single-party or multi-party)
- (e) Peace in the country

DIFFERENCE BETWEEN MICRO AND MACRO ENVIRONMENT

S.No.	Basis of Difference	Micro Environment	Macro Environment
1.	Meaning	Micro environment is defined as the immediate environment, under which the firm operates.	Macro environment refers to the general environment that can affect the working of all business enterprises.
2.	Factors	Specific. <i>For example</i> , employees, customers, suppliers, etc.	General. <i>For example</i> , economic factors, social factors, technological factors, etc.
3.	Controllability of factors	Generally controllable	Beyond the control of business enterprise. However, their behaviour can be studied and analysed.
4.	Impact of factors	Direct	Indirect
5.	Nature of impact of factors	Regular	Distant

SWOT ANALYSIS

SWOT is an acronym that stands for Strengths, Weaknesses, Opportunities, and Threats. Strengths and weaknesses are internal factors (within the organisation like committed employees, no debt, etc.) Opportunities and threats are external factors (outside the organisation like suppliers, competitors etc.) Strength and Weakness are positive and negative factors respectively. Similarly, Opportunities and Threats are positive and negative factors respectively.



1. **Strengths:** Strengths differ from opportunities. Strengths are internal to the business whereas opportunities are external. A business can control its strengths. Analysing strengths is important because it allows better decision-making and planning. *For example*, turnover of a particular product can be increased if the product is of premium quality. So, maintaining high quality standards is a factor which is internal to the business and within its control which can lead to high sales.
2. **Weaknesses:** Weaknesses are the factors that prevent the business from accomplishing its objectives. *For example*, poor decision-making by the management. Analysing weaknesses is very important because without getting rid of weaknesses, a business cannot survive.
3. **Opportunities:** Opportunities are a combination of different circumstances that offer a positive outcome to the business. Opportunities are external to the business and need detailed analysis. *For example*, a new residential apartment is an opportunity for local vendors to increase their sales.
4. **Threats:** Threats are external and uncontrollable. They challenge the stability and survival of a business, ultimately damaging the business. *For example*, availability of low-cost imported electronic products is a threat to the domestic products which are quite expensive.

Objectives of SWOT Analysis

SWOT analysis is conducted to develop a sound business strategy by making sure that business's strengths and weaknesses, as well as the opportunities and threats are analysed and taken into account.

Some of the objectives are:

- (i) To make an analysis of external and internal factors affecting the business.
- (ii) It is a platform for strategic planning to conduct business efficiently.

- (iii) To build strengths and overcome weaknesses of the business.
- (iv) To prepare the management to prioritise decisions as business situation demands.
- (v) Overcoming threats from external forces.
- (vi) Taking advantage of the opportunities available.
- (vii) To forecast the budget taking into consideration past trends.
- (viii) To deal strategically with the competitors.

Benefits of SWOT Analysis

SWOT Analysis helps a business to focus on important areas. It helps a business to:

- (i) Understand business requirements
- (ii) Grab opportunities
- (iii) Address weaknesses
- (iv) Plan to develop strengths
- (v) Plan to deal with threats
- (vi) Plan strategies

Limitations of SWOT Analysis

SWOT analysis is looking at the strengths, weaknesses, opportunities and threats. It has several limitations. It does not give due importance to urgent issues that should be given priority. Also, it only identifies problems, but does not offer solutions to cope with the same. At times, it provides so many alternatives but does not help to choose the best alternative.

SWOT Analysis of Dabur

STRENGTHS	WEAKNESSES	OPPORTUNITIES	THREATS
<ul style="list-style-type: none"> Large number of products and variants Market standing (More than 100 years of presence) Better understanding of Indian market Well established worldwide brand Number of certifications registered in its name 	<ul style="list-style-type: none"> Some products are expensive compared to other products (Like real fruit juice is expensive compared to aerated drinks available in the market) Dabur stores are not present anywhere. Lack of awareness of products by customers 	<ul style="list-style-type: none"> Favourable market in India (Make in India initiative is boosting the domestic companies) People are understanding the value of Ayurvedic medicines and as a result sales are increasing Quality products as compared to the low-quality products available in the market 	<ul style="list-style-type: none"> Presence of major competitors like Pepsi, Maaza, Himalaya, etc. People often visit the doctor and they provide their own medicines. Allopathic medicines pose a threat to the Ayurvedic medicines



Important Short Questions

TEST YOUR KNOWLEDGE

Short Answer Questions

1. What is technological environment?

Ans. Technological environment includes the discovery of new methods of producing goods and services, new techniques of operating business, innovations and improvements in the existing method of doing business etc. The survival of a business largely depends upon its technological advancement. *For example*, innovations in mobile industry by the entry of smartphones had a great impact on camera companies like Kodak.

2. What is the meaning of business environment?

Ans. According to Keith Davis, Business environment is the aggregate of all conditions, events and influences that surround and affect it.

A business enterprise is an open system. It gets resources from the environment and supplies its goods and services to the environment. The environment surrounding the business enterprise involves multiple set of complex economic, social or political forces including suppliers, customers, competitors, etc., having an impact on the operations of the enterprise.

3. What is economic and non-economic environment of business?

Ans. Economic environment refers to all those economic factors, which have a bearing on the functioning of a business enterprise. Economic environment impacts the business environment directly, *e.g.*, rise in income of people increases the demand of goods and vice-versa. All non-economic issues related to business enterprise are included in non-economic environment. The non-economic environment of business includes social, legal, political and technological factors impacting business.

4. Write a short note on legal environment.

Ans. The legal or regulatory environment comprises diverse laws, *e.g.*, the Sale of Goods Act, the Consumer Protection Act, 1986, various other industrial and labour laws, etc., passed by the government of a country, Court Judgments, administrative orders issued by government authorities, etc.

5. Write a short note on macro environment.

Ans. Macro environment refers to the general environment that can affect the working of all business enterprises. It influences the business either indirectly or distantly because the business is not continuously interacting with the Macro environment. Therefore, macro environment is also known as the Indirect Environment.

6. What is SWOT Analysis?

Ans. SWOT is an acronym that stands for Strengths, Weaknesses, Opportunities, and Threats. Strengths and weaknesses are internal factors (within the organisation like committed employees, no debt, etc.) Opportunities and threats are external factors (outside the organisation like suppliers, competitors, etc.) Strengths and Weaknesses are positive and negative factors respectively. Similarly, Opportunities and Threats are positive and negative factors respectively. SWOT analysis is conducted to develop a sound business strategy by making sure that business's strengths and weaknesses, as well as the opportunities and threats are analysed and taken into account.

Important Long Questions

2. Explain the importance of business environment.

Ans. Importance of business environment is given below:

- (i) **Helps in identification of opportunities and threats:** An analysis of the external environment helps the business enterprise to identify the opportunities in the market. Early identification of business opportunities will help to capture the market first without losing the market share in favour of the competitors. Every business has to face threat from its competitors. Early identification of threats and challenges helps the business to plan strategically and deal with the situations. Also, it helps to minimise the risk of loss.
- (ii) **Helps in identification of internal environment:** Business enterprises analyse the internal environment such as organisational structure, business policy, etc., to assess its own strengths and weaknesses. The management information system helps to analyse and predict the business environmental changes.
- (iii) **Helps in understanding the economic environment:** The understanding of prevailing economic environment includes economic policy and market conditions so as to assess the impact on the business from different perspective. For instance, business environment helps in understanding economic policies like export-import policy, monetary policy, industrial policy, etc., which have quite significant impact on business. The study of business environment also helps in understanding the prevailing market structure, demand-supply relationships and thus necessary from operational point of view.
- (iv) **Helps in understanding future problems and prospects:** The study of business environment helps the business enterprise to understand future problems and prospects in advance. This enables the enterprise to plan for the problems and cope with them.

3. What is SWOT Analysis?

Ans. SWOT is an acronym that stands for Strengths, Weaknesses, Opportunities, and Threats. Strengths and weaknesses are internal factors (within the organisation like committed employees, no debt, etc.) Opportunities and threats are external factors (outside the organisation like suppliers, competitors, etc.) Strengths and Weaknesses are positive and negative factors respectively. Similarly, Opportunities and Threats are positive and negative factors respectively.

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- (iv) **Threats:** Threats are external and uncontrollable. Threats challenge the stability and survival of a business, ultimately damaging the business. *For example*, availability of low-cost imported electronic products is a threat to the domestic products which are quite expensive.

4. Explain any three external components of micro business environment.

Ans. Micro external forces have an important effect on business operations of a firm. Some of the external factors which influence the business are as follows:

- (i) **Suppliers:** Inputs such as raw material, fuel, etc., are provided by the suppliers and help in smooth conduct of the business. Business enterprises should have more than one supplier so that change in policies of one supplier does not affect the smooth functioning of the business.
- (ii) **Competitors:** Business firms compete with each other to gain competitive advantage. Business enterprises constantly watch competitors' policies and adjust their policies accordingly.
- (iii) **Customers:** Since sales of a product or service is critical for a firm's survival and growth, customers must be satisfied with the performance of the business. A business enterprise supplies goods and services to different categories of customers like households, government, foreign customers, etc. A business firm must understand the needs and requirements of its customers so as to ensure success.

5. What is social environment? Enumerate any five components of social environment.

Ans. Social environment of business comprises all factors which socially affect a business enterprise. Social factors include customs, fashions, traditions, level of education, religious values, etc. *For example*, the young generation prefers to shop online while older generation will prefer traditional shopping methods, i.e., by visiting the stores. Following are the main components of social environment:

- (i) Educational level
- (ii) Demographic trends (growth, structure and movement of population)
- (iii) Customs, culture and traditions—as per culture and tradition, festivals like Eid, Diwali, Xmas, etc., provide opportunities for consumer durables, restaurants, sweets, etc.
- (iv) Social trends—the craze for health and fitness led to a revolution in establishing fitness spas as well as diet foods.
- (v) Social concerns (e.g., concern for pollution)

6. Explain any four components of internal micro environment.

Ans. Some of the internal factors which influence the business are as follows:

- (i) **Management Structure:** Management structure includes the composition of the board of directors, pattern of shareholding, organisational structure, etc. These factors influence decision-making.
- (ii) **Value System:** The value system of an organisation means the beliefs that help the organisation in achieving its objective. The value system of a business enterprise has an important bearing on the choice of business, policies, behaviour towards employees, society, etc.
- (iii) **Mission & Objectives:** The objective of any business is to maximise its profits. However, mission is the overall purpose for the existence of business enterprise. Objective is a narrower concept as compared to mission. Both Objective and Mission influence short-term and long-term decision-making of the business and determine its strengths and weaknesses.
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