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## **Unit 1 □ Business Environment – An Overview**

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## 1.0 Objectives

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Business may be identified as the act of combining the resources or factors of production for pursuing a particular economic or commercial activity with the objective of making profit. The ultimate purpose of a business is to maximize owner's value over the long term by selling goods and services. But as an institution in society catering to the needs of people and drawing resources or factors of production from society, every business entity has to take into consideration the circumstances around it, the sum total of which is business environment. Thus, business environment refers to all the external forces that have a bearing on the functioning of business. Some external forces help and some hinder business. Just as the life and success of an individual depends on his innate capability, including psychological factors, traits and skills; to cope with the environment, so also the survival and success of a business entity depends on (1) its innate strength- the resources at its command, including physical resources, skill and organization-and (2) its adaptability to the environment. The total business system thus operates with two sets of factors- the internal factors and the external factors.

The internal factors, coming from within the firm, are the factors over which the firm has control. It can more or less alter or modify such factors as its personnel, physical facilities, organization and functional means (such as the marketing mix) to suit a specific situation. These factors are therefore generally regarded as controllable variables. They are variables in the sense that in accordance with the needs of a particular situation some changes may be introduced to their quantity or quality. The internal factors are varied by business from time to time to suit the requirements of business. These internal factors are sometimes regarded as constituting a micro environment, while the external factors are said to constitute a macro environment. Adaptability with the environment is one of the secrets of business success. The external factors, coming from outside the firm, are the factors more or less beyond the control of the firm, for example, **the economic environment, political environment, legal environment, socio-cultural environment, demographic environment, competitive environment, technological environment, global environment and natural environment.** These environmental factors are largely regarded as uncontrollable variables for business.

As the environmental factors are, by and large, uncontrollable, the success of a business depends to a very large extent on its adaptability to the environment, that is, its ability to properly design and adjust the internal controllable factors to cope with the business environment. The external factors, are not static. They change through time, as the state of the economy or the polity or the society or as the international economy changes. Hence, business organizations have to remain alert about the changes taking place in the environment around them and adjust their internal factors to cope with the changing environment, so that they might survive and succeed.

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## 1.1 Introduction

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### 1.1.1 Characteristics of Modern Business

Modern business has certain characteristics. The characteristics are partly the outcome of the changes in environment that are taking place through time. The characteristics are :

**Change :** Change is the basic characteristic of business. If there is any single word that can best describe today's business, it is change. Business was always dynamic because the society is dynamic, human wants are dynamic. But modern business is more dynamic than the businesses of the yesterdays, as the pace of scientific and technological change in modern times has become faster. New technologies herald the arrival of new products leaving behind the old ones. "Today's growth product", aptly remarked Theodore Levitt, "may be tomorrow's earthen pot". The ever-changing market place has become a 'battle ground' for different companies surviving on consumers' loyalty and preferences. For developing new products to suit the customer's demand and survive in competition the companies are spending more and more on Research and Development.

**Large-Scale Operation :** Mass production and mass marketing are the norms followed by modern business enterprises. Machines are fast replacing manual labour in the manufacturing process. With machines operating machines, production in bulk has become possible. Marketing activities are being stepped up to match massive production. New channels of distribution, super markets, discount houses and trade fairs have sprung up to meet the challenges of mass production and ultimately they cater to the demands of consumers.

Mass production and mass marketing has ensured economies of scale to the manufacturers, and the benefits of increasing scale of operation also accrue to the consumers in the form of reduced price, per unit of product. But large-scale production has also brought problems of management in every sphere of production and distribution. Hence, survival in business has become very tough.

**Diversification :** Today's business is characterized by diversification. The product portfolio of any medium or large business house is widely diversified, because business today do not like to keep their investments tied to any single line of manufacturing or service for fear of losing every thing if the particular venture fails or does not perform well. Risk diversification ensures risk reduction through product diversification. Moreover, diversification through product differentiation enables well established companies to cater to the multidimensional needs of the consumers and thereby enjoy their continued patronage, so that they may expand their consumer base. Well-known Indian companies, like the Tatas, and the Birlas, have diversified into wide variety of products and services for the purpose of extending their operation to a large number of customers spread over wider areas.

Companies also follow the merger and acquisition route to diversification. The nineties witnessed a surge in mergers and acquisitions across the globe. The value of cross border mergers and acquisitions has risen more than seven times between 1987 and 1999. “The value of completed cross-border mergers and acquisitions rose from little less than \$100 billion in 1987 to \$720 billion in 1999”. The developed countries accounted for more than 65 percent of the mergers and acquisitions in terms of value, and the balance went in favour of the developing nations and Central and Eastern European Countries. With the repeal of the provisions relating to the regulation of monopolies in the MRTP Act, 1969, many Indian successful companies have started acquiring smaller companies for expanding their share of the market and diversifying production and distribution of goods and services in recent times. The high-tech IT industries of Indian origin are also acquiring foreign companies in developed countries.

**Globalisation :** Since end of the World War-II and particularly since the coming into existence of the Bretton Woods system, the countries of the world have come closer to each other every day. The process has been further accelerated by the World Trade Organisation. Today the world has become virtually boundaryless. Goods and services produced in one country can be sold to other countries across the world without much difficulty. Production facilities are being set up in different countries and products are being sold through a global network. Gradually, business houses are exposed to global competition which augers well for consumers, requiring quality goods at reasonable prices.

Infact, internationalisation or globalisation is fast becoming imperative for modern business due to technological innovations; crumbling trade barriers, freer flow of capital and technology, information explosion, intensity of market competition, changing life styles and the demand for new products. Internationalisation of business is a means of sustaining a strong domestic base in terms of technology, product, market and capital over a long period.

**Science :** Science and scientific ideas also occupy a major role in the global economic scenario. Infact, since the beginning of production for market man has tried to improve upon the tools and techniques of production to reduce the cost of production and develop new products and services for gaining greater share of markets. The development, first of electricity and then atomic power, advances in metallurgy and allied fields, accomplishments relating to the space-age programmes, application of mathematics in managerial decision-making have made business processes more rational and precise than before.

**Information :** Another characteristic of contemporary business is the growing importance of information. Businessmen, having better information about markets, products, customer profile and the strategies of their competitors, always gain over others in the field. With the development of information technology it is now possible to collect, store, analyse, manipulate and transfer data and information from one place to another at a lightening speed. Hence, business information system and its management have assumed

additional importance in modern business. Businessmen are now free from the drudgery of much detailed paper work. They can progress further by feeding light people with light information at the light time.

**Government Regulation :** In the 17th, 18th and 19th centuries government's role in business was the minimum. Adam Smith was the apostle of free trade within as well as between nations. But unrestricted competition did achieve neither full employment nor maximum wellbeing everywhere. The Great Depression, which started in the USA and spread to many other countries in the 30s of the last century, led to the arrival of the welfare state concept whose economic advocate was Keynes. Keynes' plea for government participation in the economy for offsetting the short fall of private investment was accepted by most economists. Subsequently, government regulations for controlling the abuses of unrestricted private business became a feature of policy throughout the world. These persist in India even in the post-reform era.

### 1.1.2 Objectives of Business

Before we discuss business objectives, it is desirable to be clear about the meaning of two other relevant concepts, viz., vision and mission of business. Vision refers to the goals that are broad, most general, and all-inclusive. A vision describes aspirations for the future, without specifying the means necessary to achieve those aspirations. A vision becomes tangible as a mission statement. Objectives render mission statements more concrete. In other words, mission statements seek to make a vision more specific, and objectives are attempts to make mission statements more concrete. Objectives, therefore, represent the operational side of an organization.

It may be stated that a typical business unit seeks to achieve more than one objective and there are always constraints on the attainment of some objectives. Objectives vary with the passage of time, as people's requirements change, so also change the technological and other variables. However, objectives common to most business are the following :

**Profit :** Making profit is the primary goal of any business enterprise. Profit is the excess of income over expense. Profit is the main incentive, motivator, strong sustainer, and judicious allocator of resources, objective indicator of productivity and a solid basis for growth, expansion and survival. Profit enables a businessman to realize his other objectives too.

But some enterprises are not primarily and exclusively interested in making profits. For example, hospitals, schools, charitable institutions and government agencies are not basically concerned with the making of profit only. The non-profit enterprises customarily rely on gifts, endowments, receipts from money-raising projects, subsidies or taxes for sustenance. The basic objectives of these establishments are the provision of services that are socially desirable and useful.

In profit-making enterprises profit should not be the end in itself. Profit should be the beginning-the prime motivator for further developments in all other respects. Profit should

promote the well being of all concerned. All the stakeholders should share the profit according to their respective takes in the business, so that they remain contented with the functioning of the business.

**Growth :** Growth is the next most important objective of business. Just as a living being cannot remain static, it either grows or declines and ultimately dies; a business can also hardly remain static for long. The strategies adopted to achieve growth are the following.

- (a) Production of more goods and services and expansion of the horizon of operation by extending to new markets;
- (b) Diversification into new geographical areas of production and distribution of goods and services;
- (c) Forward and backward integration for expansion in operation;
- (d) Increasing the share of the market;
- (e) Reduction in the cost of production and increase in productivity.

**Power :** Business houses have vast resources at their command. These resources confer enormous economic and political power on the owners and managers. Several enlightened businessmen, like J. N Tata, I. D Birla, and Dhirubhai Ambani have used their power for the good of society by providing the government with novel ideas for economic development of the country. Examples of successful businessmen playing important role in providing political and even academic leadership, particularly in the field of development of management science, are many. Hence, successful businessmen can make their experience available to society for the good of mankind.

**Employee Satisfaction and Development:** Success of a business depends, amongst others, on a contented and competent workforce. Hence, employee satisfaction and development is a very important objective of business. Successful business houses everywhere in the world care most for their employees. After all it is the employees who work and the result of their work is reflected in the growth of the business in terms of profit and expansion. Human resource development is a concern of every business organisation now-a-days.

**Quality Product and Service :** Providing quality product and service is yet another objective of business. For a short period of time a company can survive through aggressive marketing strategy without bothering for quality. But in the long run companies who bother about quality and customer satisfaction only survive. Quality earns brand loyalty and brand loyalty ensures expansion of the business through diversification. Side by side with production of quality products the business should provide prompt quality service to its customers. Defects remain in the products even in spite of strict quality control. So the producer must be ready to entertain customers complain. Thus, even the new products coming from the houses of Tata, Godrej, Hindustan Liver, etc. get easier access to the market because of their quality consciousness and customer care. Hence, one objective

of a business house has to be providing customer satisfaction through quality products and services.

**Market Leadership :** Market leadership is the ultimate objective of every business. However, in order to achieve the position business houses encourage innovation. Schumpeter pinpointed innovation as crucial for business growth. Innovation may take place in the development of a new product, improvement in the quality of existing products) advertising, distribution, finance or any other relevant field. Market leadership means rising above others in the market. This cannot be achieved without being ahead of others.

**More Joy and Pleasure for People :** Economic development in many countries has now reached a stage where men's demand for services is increasing faster than that for basic necessities. The basic reason behind this increase in demand for services is growing demand for joy and pleasure. After all, the driving factor behind human civilization is quest for pleasure and comfort. From the day of fabrication of tools for hunting to the development of computer and information technology the motive that drove mankind is more benefit and pleasure at lesser effort. In the developed countries today around 70 per cent of the working people find employment in the service sector and the percentage of national income derived from the service sector is higher. In the context of the above, business houses should strive to give people more joy and pleasure by designing their products and services accordingly.

**Good Corporate Citizenship :** A business organization has a separate entity distinct from the members composing it. As an entity it has to work within the framework of different rules and laws enacted by the State. Good corporate citizenship implies that a business unit obeys the laws of the land, pays taxes, and honours all commitments like every good citizen. Bending rules to its favour, not abiding by the different laws of the land by adopting all dubious means might help earning high profit and enable a company to keep its shareholders in good humour. But it cannot earn respectability. Further, business organizations indulging in malpractices may land in trouble any time. It has been found that many otherwise successful business houses find it difficult to come out of the inglorious situation once they are found indulging in such activities. Hence, every business house should strive to be a good corporate citizen.

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## 1.2 Business Environment

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Business environment is the environment within which business operates, determined by political, economic, social, legal and technological factors originating at home and abroad.

### 1.2.1 Economic Environment

Economic health of the country, economic policies and economic systems are the important external factors that constitute the economic environment of business.

The economic conditions of a country—for example, the state of health of economy, the stage of development of the economy, economic resources, the levels of income and prices, the pattern of distribution of income and assets, etc. are among the important determinants of business strategies.

In a developing country, the low per capita income of people is one of the reasons for very low demand for products of luxurious consumption and high demand for essential commodities. However, in such countries the market for products for which the demand is income-elastic expands with increase in income. As the business houses are unable to increase the purchasing power of the people to generate a higher demand for its costlier products, they may have to reduce the price and concentrate on the production of essential commodities. It may even be necessary to develop new low-cost products to suit the low-income market. On the other hand, business prospects are generally bright in countries where investment and incomes are high and rising.

The economic policy of the government, needless to say, has a very great impact on business.

For example, a restrictive import policy, or a policy of protection, may greatly help the import-competing industries, while a liberalization of imports may put such industries in a difficult position. In every country such changes in policy occur from time to time and the business houses are required to be alert about it.

In India, the government's concern about the concentration of economic power had restricted the role of the large business houses and foreign concerns to the core sector, the heavy investment sector, the export sector and the backward regions. But with the liberalization of Indian economy through new economic policy in 1991, most of those restrictions having been withdrawn, the Indian and foreign corporates are investing in all the sectors except the defence and strategic industries.

The monetary and fiscal policies of a government can provide incentives and disincentives to economic development in a country. In India, cheap money (low interest) policy combined with budgetary (fiscal) tax and other concessions have brought about a revival of India's corporate sector after 2001 (which sector was depressed since 1994 for all sorts of reasons). These policy-measures of the government provide the environment under which business houses operate in the country.

The scope of private business in a country largely depends upon the economic system of the country. At the one end there are the free market economies or capitalist economies and at the other end there are the centrally planned economies, with a large number of countries in between the two extremes. However, with the disintegration of the East European communist countries the importance of state command and control in economic development has declined since late eighties. But the developing countries of Asia, Africa and Latin America largely follow a policy of mixed economy. The freedom of private enterprise is

maximum in the free market economies, whereas in the developing countries the extent of State intervention being greater, the degree of freedom of operation of business houses is less. So the business houses operating in a country have to take into consideration the nature of the prevailing economic system and its constraints.

### **1.2.2 Political and Legal Environment**

Political environment refers to the condition created by the political factors operating within the country. Important among such factors are the nature of the government and the character of the party system. The government may be dictatorial or democratic. In a dictatorship policy making is a one-man or one-party show. In a democracy policy making is in the hands of the majority party (in power) elected through a process of free vote by all adult citizens for a specific period of time. In a multiple party regime the citizens, including business houses, have greater opportunities to ventilate and redress their grievances and fight for their interests than in a single-party system. The majority party (forming the government) is checked and balanced by the opposition. The level and rate of business growth have been generally higher in democratic than in dictatorial countries.

The legal environment is created by the legal enactments, conventions and practices prevailing in the country. If it is not helpful, business would stumble and suffer. In India we have a framework of helpful industrial and commercial laws, supported by an independent judiciary, which is conducive to good business.

### **1.2.3 Socio-Cultural Environment**

The socio-cultural fabric is an important environmental factor that should be analysed while formulating business strategies. The socio-cultural environment is the sum total of the customs, traditions, beliefs, tastes and preferences, and values of people. The customs and traditions of people reflect basic tenets of their civilization. They generally change very slowly with economic development and changes in the social relations. Hence, any thing that apparently goes against the customs and beliefs of people will not get approval of the people of the society. Marketing strategy has to take note of this. Thus, for a business to be successful, its strategy should be the one that is appropriate in the prevailing socio-cultural environment. The marketing mix shall have to be designed as best to suit the environmental characteristics of the market. In the competition for expanding their markets in the developing and the least developed countries, many multinational companies of Europe and America had to change the characteristics of their products and marketing mix to suit the beliefs, customs, traditions, etc. of people of those countries. For example, Helene Curtis had to switch to black shampoo in Thailand to satisfy popular local demand; Nestle today brews more than forty varieties of instant coffee to satisfy different national tastes. But tastes and beliefs can also be changed by aggressive marketing, as has been the case with women's wear in India in the last two decades (an illustration of western cultural imperialism).

Social inertia and associated factors come in the way of the promotion of certain product, services or ideas. We come across such social stigmas in marketing of family planning ideas, use of biogas for cooking, etc. In such circumstances, the success of marketing depends, to a very large extent, on the success of coping with social attitudes or value systems of the country concerned.

#### **1.2.4 Demographic Environment**

The demographic environment (really a part of the economic environment) is created by the different characteristics of the population. A high-population country is a country with a high market potential.

A rapidly increasing population indicates a growing demand for many products. High population growth rate also indicates an increase in labour supply. As labour is cheap relatively to capital, countries with huge population generally use labour-intensive technology unlike in countries with low-population (Europe and America).

Similarly, the age composition and sex ratio determines what are to be produced and how they are to be produced. In countries with higher longevity of people and lower birth and death rates, there will be plenty of senior people. Thus, goods and services used by the senior people will be very much on demand. On the other hand, with decline in the number of middle aged and younger people there will be dearth of skilled and energetic people to man the factories and workshops. To day there is a growing demand in the developed countries of West for technically skilled manpower from the developing countries like India and China. Side by side, most of the high-tech industries of those countries are also outsourcing their jobs to these countries to discourage immigration from these countries and also having the work done at a lower cost with the skilled workers working in their own countries and thereby having a greater margin of profit. This has led to the growth of “call-centres” around the world to do specialists job with the help of information technology system stationing oneself any where in the world.

Lastly, the occupational mobility of people also influences the pattern of business development of a country. Higher mobility of people ensures dispersal of industries for the purpose of getting maximum advantage in the form of economics of localization of industries and scale of operation.

#### **1.2.5 Competitive Environment**

Competition is another very important external factor that influences sustainability and growth of business entities in a country. Business strategy of a firm is highly influenced by the nature and degree of competition prevailing in a country. Since the dawn of civilization mankind thrived and enriched themselves in all spheres of life through competition. Business, being a part of human society, cannot succeed and reach perfection without healthy competition. Cost-effectiveness and product quality cannot be ensured in a non-competitive environment.

In countries with absolute State control over all forms of economic activities development could not proceed beyond certain levels and this actually led to the disintegration of the erstwhile East European communist countries and subsequent opening up of the economies of China and some other countries like Vietnam, Albania, etc.

In India, on the other hand, there existed strict control over big business houses for a pretty long time under the Monopolies and Restrictive Trade Practices Act 1969. But in course of time it was realized that restrictions on growth in the scale of operation of business houses actually discourage efficiency in operation and economics of scale. Hence, with the adoption of the New Economic Polity in 1991, the operation of the Act has come to be limited to only the restrictive trade practices, pre-entry scrutiny of investment decisions by the big business houses has been dispensed with. The Act has been repealed and in its place the Competition Act, 2002 has been brought to ensure competition among business houses. Moreover, no discrimination is now made among the Indian and foreign enterprises with respect to the operation of the policy on monopolies and restrictive trade practices in the country. This change in policy has led to an increase in foreign investment in the country through equity participation (portfolio investment) and direct investment (foreign direct investment). As a result of these investments foreign technologies are also flowing in to the country, paving the way for opening up of the new horizons in development.

### **1.2.6 Technological Environment**

Technological environment refers to the situation in respect of the state of technology in the country. With respect to the state of technological development countries differ widely. In this difference lies the advantage of certain nations in the specialization of production and distribution. Hence, the technologies are patented. The countries possessing the patents and trademarks do not like to share them with others unless the terms and conditions of sharing the technology are favourable to the supplier of technology. Naturally, even as some technologies are shared, all the technologies are not shared, and the countries have to depend largely on their own technological capabilities.

Thus, business houses setting up their working facilities in a country have to take into consideration the state of technology available in the country. The principal purpose of a business entity being making of profit, it has to ensure itself about the best way of doing the work so that the cost of production and the quality of products can be acceptable to people of the country.

Again, a firm that cannot cope with the technological changes taking place in the country may not survive. Further, the different technological environments of different markets or countries may call for product modifications. Because, people will not accept a technology with which they are not familiar or not convinced about the desirability of the use of technology. The application of a particular technology in a country also requires trained manpower capable of working with the technology. So all these factors are required to be taken into consideration before deciding upon the use of technology in production or distribution of goods and services in the country.

### **1.2.7 Global Environment**

The global environment is the totality of forces, originating from outside the country and having impact, good or bad, upon domestic businesses. In the circumstances, global environment is very important from the point of view of certain categories of business. It is particularly important for industries directly depending on imports or exports and also for import competing industries. For example, a recession in foreign markets, or the adoption of protectionist policies in foreign nations, may create difficulties for export industries. On the other hand, a boom in the export market or a relaxation of the protectionist policies abroad may help the export-oriented industries. A liberalization of imports may help some industries that use imported items in the manufacturing of some final products, but may adversely affect import-competing industries.

It has been observed that major international developments have their spread effects on countries across the world. The Great Depression in the United States in the 1930s, sent its shock waves to a number of other countries. Oil price hikes by OPEC had adversely affected a number of economies. These hikes increased the cost of production and the price of certain products, such as fertilizers, synthetic fibers, etc. in India. The situation also created demand for automobile models that economise energy consumption.

A good export market also enables a firm to develop a profitable product mix and to consolidate its position in the domestic market. Export market facilitates the attainment of optimum capacity utilization; a company may be able to mitigate the effects of domestic recession by exporting. However, a company, which depends too much on the export market has also to face the impact of adverse developments in foreign markets. Exports add to national income.

### **1.2.8 Natural Environment**

This is given by the state of country's natural resources, including air and water and climate and topography and access to the sea. Differences in geographical conditions between markets may sometimes call for change in the marketing mix. Geographical and ecological factors also influence the location of certain industries. For example, industries with high material index tend to be located near the sources of raw materials. Climate and weather conditions influence the location of certain industries like the cotton textile industry, tea and coffee industries. Temperate climate promotes labour efficiency. Business activities have effects upon the natural environment. Hence, business has a responsibility to see to it that its practices do not lead to an excessive depletion of a scarce natural resource and/or a degradation of the natural environment. Hence, business has a responsibility to see to it that its practices do not lead to an excessive depletion of a scarce natural resource and/or a degradation of the natural environment around it (through, for example, pollution or ecological destruction). Legislation has been passed in many countries, including India, for preventing environmental destruction by individuals or institutions. The environment factor is considered in social audit of many firms.

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## 1.3 Knowing the Environment

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Business being a product of different environmental factors, there develops a web of relationships between business and its environment. First, there is symbiotic relationship between business and its environment and among the environmental factors. Business both influences and is influenced by, its natural environment. Secondly, these environmental factors are dynamic; they keep on changing as years roll by. Lastly, a particular business firm, by itself, may not be in a position to change its environment. But along with other firms, business will be in a position to mould the environment in to their favour, to a large extent.

The environment, as described above, provides a mass of information some of which may be ambiguous or not necessary. It is the task of a business house to select the information relevant to it and adjust its operations to conform to the requirement of the environment. Three different steps seek to address this problem. They are : (i) the enacted environment, (ii) the domain and domain consensus, and (iii) the task environment.

Enacted environment an organization seeks to create its own environment out of the total external environment. The environment that the organization creates is called enactment. Enactment implies that the organization creates a relevant environment for itself by aggressively scopping, narrowing and scanning the external environment. In effect, the organization creates the environment to which it reacts. It does not react to the entire environment because every thing there is not relevant to it.

Domain and domain consensus the domain is that part of the enacted environment, which the organization carves out for itself. The firm delineates its own territory out of the environment. The delineated territory comprises the range of products offered, population served and services rendered. The organization focuses its efforts on these three areas while paying less attention to other areas.

As is well known, an organization has many stake holders-owner, employees, customers, government, public, suppliers and lenders. Domain consensus is formed when all the stakeholders agree upon the domain of the organization.

When domain consensus is not reached, conflicts may arise regarding which part of the environment should be monitored. This conflict causes confusion and backbiting, when the company is blind-sided by an unexpected occurrence from a poorly monitored sector. Hence, in order to reach domain consensus the enterprise should identify the domain for itself that is accepted by the concerned stakeholders.

The task environment this specifies the range of products to be offered, the technology to be employed and the production strategies to be used to counter competition. The task environment being the final stage from where the result emerges requires constant and careful surveillance. At the same time the other elements are also not to be ignored or paid less attention.

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## 1.4 Importance of environment analysis

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Environment analysis has three basic goals. First, the analysis provides an understanding of the current environment and the changes likely to take place in the task environment. It is important that one must be aware of the existing environment. At the same time, one must also have the vision to see far into the future. After all, every business should have a long-term projection (or forecast).

Secondly, environmental analysis provides inputs for strategic decision-making. Mere collection of data and information about the different constituents of the environment is not enough. The information collected should be used in strategic decision-making to gain maximum advantage out of them.

Thirdly, environmental analysis should facilitate and foster strategic thinking organisations 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 organisation. To be specific, the benefits of environmental study are as follows :

1. Development of broad strategies and long-term policies of the firm.
2. Development of action plans to deal with technological changes.
3. To foresee the impact of socio-economic changes at the national and international levels on the firm's stability (future).
4. To analyse competitors' strategies and formulate effective counter-strategies.
5. To keep the business on the dynamic path to development.

Management has to take decisions quickly and correctly to cope with the changing scenario. Hence, business decisions taken under the pressure without proper analysis of the environment is likely to be incorrect or misleading. It is true that in an ever-changing situation every decision taken may not be correct, but every effort should be made to make it appropriate to the particular situation. "Environmental analysis and diagnosis give strategists time to anticipate opportunities and to plan to take optimal 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". When conducted properly, environmental analysis leads to the enhanced capacity and commitment to understanding, anticipating and responding to external changes on the part of the firm's key strategic managers. Responsiveness is achieved by inducing managers to think beyond their task or industry environments, often forcing them to reflect upon their cognitive biases. In short, at the process level, environmental analysis offers one basis for organizational learning. In the real world of business, firms that systematically analyse and diagnose the environment succeed more than those who do not.

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## 1.5 Process of environmental analysis

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Environment analysis is a challenging, time-consuming and expensive affair. The analysis proceeds through four distinct sequential steps; (i) scanning, (ii) monitoring, (iii) forecasting, and (iv) assessment.

*Scanning* : Being the first step in the process of environmental analysis, it involves general surveillance of all environmental factors and their interactions in order to (a) identify early signals of possible environmental change, and (b) detect environmental changes already under way.

Scanning is not a structured analysis. It is a general analysis of the relevant variables. The potentially relevant data for scanning are unlimited, but are sometimes scattered, vague and imprecise. The fundamental purpose of the analysis in scanning is, therefore, to make the data and information precise, relevant and purposeful through proper selection, arrangement and study.

*Monitoring* : Monitoring involves tracking the environmental trends, sequences of events, or streams of activities. It frequently involves following the relevant signals or indicators identified during scanning. The purpose of monitoring is to assemble sufficient data to discern whether certain trends and patterns are emerging. Thus, as monitoring progresses, the data frequently turn precise and purposeful. Three outcomes emerge from monitoring : (a) a specific description of environmental trends and patterns to be forecast; (b) the identification of trends for further monitoring, and (c) the identification of areas for further scanning. The outputs of this stage become the input of the subsequent stage, that is, forecasting. They may also require further scanning and monitoring, if necessary.

*Forecasting* : Scanning and monitoring provide a picture of the trend of what has taken place-the relationship between cause and effect. Strategic decision-making for the future, however, requires understanding of the possible future path of events. Naturally, forecasting calls for rigorous analysis of the essential elements of the environment and linking them with the prospects of the firm.

Forecasting is concerned with developing plausible projections of the direction, scope, and intensity of environmental changes. It tries to layout the evolutionary path of anticipated changes. Unlike two earlier steps (scanning and monitoring), forecasting is well-focused and is a much more deductive and complex activity. This is so because the focus, scope and goals of forecasting are more specific than the earlier two stages of environmental analysis.

*Assessment* : Scanning, monitoring and forecasting are not the ends in themselves. Unless their outputs can be assessed to determine their implications for the organisation's current and potential strategies, scanning, monitoring and forecasting would simply provide 'nice-to-know' information. Assessment involves identifying and evaluating how and why current and projected environmental changes affect or will affect strategic management of the organization.

In assessment, the frame of reference moves from understanding the environment-the focus of scanning, monitoring and forecasting-to identifying what the understanding means for the organization. Assessment, therefore, tries to answer questions such as what are the key issues in the environment, and what the implications of such issues for the organization are.

### **Linkages among the four steps**

Though conceptually scanning, monitoring, forecasting and assessment are separate activities they are very much linked with each other. For example, upon unearthing an emerging trend in the consumers' demand through scanning, one might quickly start analyzing the potential implication of the trend for the organization by implicitly forecasting the future path of the trend. If warranted by the potential impact, one may then continue scanning and monitoring. Also, forecasting often proves difficult, if not impossible, because of insufficient knowledge and data about the topic or trends being forecast, thus forcing a return to scanning and monitoring efforts. The resulting implications often require the organisation to conduct further scanning, monitoring and forecasting. Thus, environmental analysis is not as easy as moving from scanning to monitoring and the other two earlier steps.

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## **1.6 Limitations of environmental analysis**

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Environmental analysis, as with any other analysis, has certain limitations. These limitations are :

1. Environmental analysis does not foretell the future, nor does it eliminate uncertainty for any organisation. It helps fight uncertainty. Thus, organisations that practice environmental analysis sometimes confront unexpected events-events not anticipated during environmental analysis. Environmental analysis, however, should reduce the frequency and extent of surprises that may confront a company.
2. Environmental analysis itself is not a sufficient guarantor of organization effectiveness. It is only one of the inputs in strategy development and testing.
3. The potential of environmental analysis is often not realised. It is some times used for comparing results and at times managers place uncritical faith in the data without thinking about the data's verifiability or accuracy.
4. Too much reliance is often placed on the information collected through environmental scanning. When there is overloading of information, one is likely to get lost in the mass of information and become purposeless. So, effort must be given to collect only the data and information necessary for the organisation, and they should be analysed with due care in accordance with the steps suggested.

Success lies in adventure and strategic risk-taking. It eludes those who hesitate to venture forward. Environmental analysis often makes an individual too cautious in his approach, and he is likely to be overtaken by events.

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## 1.7 Summary

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Business organisations operate in a particular socio-economic-geographical-political-natural environment. The factors of the environment are external to business. Hence, they are more or less uncontrollable and even unmanipulable by business. Further, these external factors change from time to time in accordance with changes in peoples' need, belief and use. But, the factors internal to business, particularly its resources and other operational advantages, are controllable and manipulable. In order to cope with the external environment, business organisations use their internal factors and resources. But, the purposeful use of internal resources by business for strategic decision-making cannot be made without an analysis of the environment around it.

The analysis of the environment is required to be done by top executives of business for decision making. To be specific, top executives in marketing, finance and human resource, who make important decisions in business about fixing of targets of production and sale are the persons who undertake environmental analysis. With the rapid improvement in information technology the task has become easier. The business organisations now maintain Management Information System to handle the job of analysing the environment. In a competitive world every organisation tries to be ahead of others, and for this they have to commit more time, resource and energy to environmental analysis. Ultimately the success of a business depends on how perfectly strategic decisions are taken and how efficiently they are executed.

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## 1.8 Exercise

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### Long answer type :

1. What is business? What do you understand by internal and external factors of business? Examine their relevant importance in business operations.
2. Examine the principal characteristics of modern business.
3. State and explain the principal characteristics of modern business. Show how they influence business activities.
4. What do you understand by vision, mission and objectives of business? Explain the principal objectives of business.
5. What do you understand by business environment? Give a brief account of the different constituents of business environment.

6. State the importance of environment analysis in business. Give an account of the process of environment analysis.
7. State how different steps of environment analysis are linked with each other. Mention the limitations of environment analysis.

**Short answer type :**

1. Mention the major types of environment in which businesses operate.
2. State the role of internal factors in business.
3. State the characteristics of modern business.
4. What is meant by domain and domain consensus?
5. Define and explain task environment.
6. Mention the external factors in business.
7. State what is meant by environment analysis.
8. Mention how four steps of environment analysis are linked with each other.
9. State how environment scanning is made.

**Objective type :**

Find the correct answer :

1. Broad goal of business is set by—
  - (a) vision
  - (b) mission
  - (c) objectives
  - (d) none of the above.
2. Political environment refers to—
  - (a) influence exerted by political system,
  - (b) influence exerted by strikes,
  - (c) influence exerted by legislature, executive and judiciary,
  - (d) influence exerted by the President of India.
3. Process of environmental analysis begins with—
  - (a) firecasting
  - (b) scanning
  - (c) monitoring
  - (d) information management

4. New economic policy was announced in–
- (a) 1987
  - (b) 1990
  - (c) 1991
  - (d) 1995

**Answer of objective type question : 1. (a), 2.(a), 3. (b) and 4. (c).**

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## **1.9 References**

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