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COMMERCE
PAPER NO. 5 : BUSINESS ENVIRONMENT
**MODULE NO. 1 : CONCEPT ,SIGNIFICANCE & NATURE OF
 BUSINESS ENVIRONMENT**

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1. Learning Outcomes

After studying this module, you shall be able to

1. Know the concept of business environment
2. Understand the nature of business environment
3. Appreciate the importance of business environment
4. Analyze the impact of environment on business and vice versa

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2. Introduction

Understanding the environment within which the business has to operate is very important for running a business unit successfully at any place. Because, the environmental factors influence almost every aspect of business, be it its nature, its location, the prices of products, the distribution system, or the personnel policies. Hence it is important to learn about the various components of the business environment, which

consists of the economic aspect, the socio-cultural aspects, the political framework, the legal aspects and the technological aspects etc. In this chapter, we shall learn about the concept of business environment, its nature and significance and the various components of the environment.

When we talk about the concept of business environment as per the business dictionary it is defined as

“The combination of internal and external factors that influence a company’s operating situation. The business environment can include factors such as: clients and suppliers; its competition and owners; improvement in technology; laws and government activities; and market, social and economic trends.”

The success of every business depends on adapting itself to the environment within which it operates. For example, when there is a change in the government policies, the business has to make the necessary changes to adapt it to the new policies. Similarly, a change in the technology may render the existing products obsolete, as we have seen that the introduction of computer has replaced the typewriters; the colour television has made the black and white television out of fashion. Again a change in the fashion or customers’ taste may shift the demand in the market for a particular product, e.g., the demand for jeans reduced the sale of other traditional wear. All these aspects are external factors that are beyond the control of the business. So the business units must have to adapt themselves to these changes in order to survive and succeed in business. Hence, it is very necessary to have a clear understanding of the concept of business environment and the nature of its various components.

3. Success story of Starbucks

Success story of Starbucks in China by efficiently tackling its business environment

If there is one company that should have failed in china, it would be Starbucks. China has thousands of years of history drinking tea and a strong culture associated with it. No one could have guessed that Chinese would ever drink coffee instead of tea.

Yet, Starbucks have successfully opened more than 570 stores in 48 cities since it first entered years ago. Building on this momentum, it plans to open 1,500 stores by 2015. What did the Seattle-based coffee company do right in China?

Think Different

When Starbucks entered china in 1999, many were skeptical that Starbucks had a chance. Given the fact that Chinese people have traditionally favored tea, it seemed impossible that Starbucks would be able to break into this market.

However, Starbucks did not let this skepticism stop it. A careful market study revealed that as the Chinese middle class emerged, there existed an opportunity for Starbucks to introduce a western coffee experience, where people could meet their friends with drinking their favourite beverages.

Starbucks literally created that demand .Now you can find a Starbucks almost on every major street of the coastal cities in china

Position Smart

The net thing Starbucks did was to capitalize on the tea dinking culture of Chinese consumers by introducing beverages using popular local ingredients such as green tea. This strategy has effectively turned potential obstacles into Starbucks' favour.

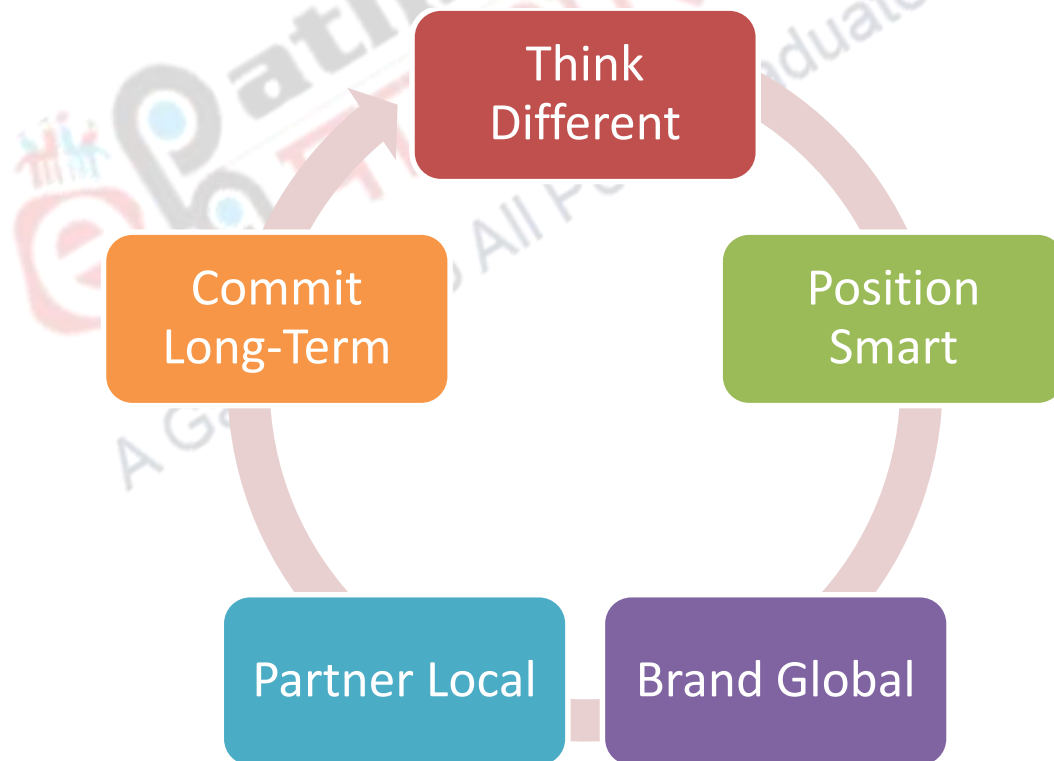


Figure 1: STARBUCKS SUCCESS MODEL

Brand Global

Starbucks understand the value of its global brand and has taken steps to maintain brand integrity.

Global brand does not mean “global products,” or “global platform” as eBay mistakenly tried. Starbucks has highly localized menu of beverages that is particularly tailored to Chinese consumer. It has done an extensive consumer taste profile analysis to create a unique “East and West” blend.

Partner Local

China is not one homogenous market. There are many China’s. The culture from northern China is very different from that of the east. Consumer spending power inland is not on par with that in coastal cities. To address this complexity of the Chinese market, Starbucks partnered with three regional partners as part of its expansion plans. In the north Starbucks entered a joint-venture with Beijing Mei Da Coffee Company. In the east, Starbucks partnered with the Taiwan-based Uni-President .In the south, Starbucks worked with Hong Kong-based Maxim’s Caterers. Each Partner brings different strengths and local expertise that helped Starbucks gain insights into the tastes and preferences of local Chinese consumers.

Commit Long Term

China is not as easy market to crack. It requires a long term commitment. Long term commitment also means patience, it takes time to educate the market and gain customer loyalty. The companies that invest in long term plans can be sure to reap handsome rewards.

4. Nature of Business Environment

1. **Environment is complex**-Business environment consist of a number of factors, events and influences arising from different sources. All these factors no way exist in isolation but continuously interact with each other to create entirely new sets of influence. It is very much difficult to comprehend at once that what all factors constitute a given environment. Overall there is a general conclusion that environment is a complex phenomenon relatively easier to understand in parts but difficult to grasp in its totality.
2. **Dynamic**- Business environment is constantly changing in nature. Due to many influences there is dynamism in environment, causing it to change its shape and character continuously. The changes in business environment are unpredictable. It is very difficult to predict the exact nature of future happenings and the changes in economic and social environment. .

3. **Environment is multi-faceted**-Shape and character of every environment depends upon the perception of the observer. A particular change in the environment, or a new development going to be viewed differently by different observers. This is seen frequently when the same development seen as opportunity by one company and threat by another company.
4. **Far reaching impact**-Environment has very much far reaching impact on business environment. Growth, success and profitability of every organization depend upon the environment in which it exists. A minor environmental change may impact organization in several different ways.
5. **Environment is wider**-Environment is very much wider in nature. It covers all factors and forces like customers, competitors, suppliers, government, and the social, cultural, political, technological and legal conditions.
6. **Influenced by place** -Business Environment differs from place to place, region to region and country to country. Political conditions in India differ from those in Pakistan. Taste and values cherished by people in India and China vary considerably

5. Importance of Business Environment

There is a close and continuous interaction between the business and its environment. This interaction helps in strengthening the business firm and using its resources more effectively. Business environment is multifaceted, complex, and dynamic in nature and has a far-reaching impact on the survival and growth of the business. To be more specific, proper understanding of the social, political, legal and economic environment helps the business in the following ways:

(a) Determining Opportunities and Threats: The interaction between the business and its environment would identify opportunities for and threats to the business. It helps the business enterprises for meeting the challenges successfully. Analyzing of the environment over the period of the time help multinational companies to gain over the coming opportunities and get prepare to face threats

(b) Giving Direction for Growth: The interaction with the environment leads to opening up new frontiers of growth for the business firms. It enables the business to identify the areas for growth and expansion of their activities.

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

(d) Image Building: Environmental understanding helps the business organizations in improving their image by showing their sensitivity to the environment within which they are working. For example, in view of the shortage of power, many companies have set up Captive Power Plants (CPP) in their factories to meet their own requirement of power.

(e) Meeting Competition: It helps the firms to analyse the competitors' strategies and formulate their own strategies accordingly.

(f) Identifying Firm's Strength and Weakness: Business environment helps to identify the individual strengths and weaknesses in view of the technological and global developments



Figure 2: Importance of Business Environment

6. Impact of Environment on Business

The modern business manager operates in a most dynamic environment. The change in the environment has been rapid and unpredictable. These days' consumers and clients have been showing complex behaviors both in local and international markets. The most dramatic change has been that exhibited by competitive pressures. Competitors have been applying one strategy or the others to adapt to the dynamic and unpredictable nature of the business environment.

To understand the impact of environment on business **PESTEL** analysis takes place:- PESTEL analysis stands for "Political, Economic, Social, and Technological, Environmental and Legal analysis". It is a part of the external analysis when conducting a strategic analysis or doing market research and gives a certain overview of the different macro environmental factors that the company has to take into consideration.

- **Political Factors**

Political factors, identify how and to what degree a government intervenes in the economy. Specifically, political factors include areas such as tax policy, labour law, environmental law, trade restrictions, tariffs, and political stability. Political factors may also include goods and services which the government wants to provide or be provided (merit goods) and those that the government does not want to be provided (demerit goods or merit bads). Furthermore, governments have great influence on the health, education, and infrastructure of a nation.

- **Economic Factors**

Economic factors include economic growth, interest rates, exchange rates and the inflation rate. These factors have major impacts on how businesses operate and make 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

- **Social Factors**

Social factors include the cultural aspects and include health consciousness, population growth rate, age distribution, career attitudes and emphasis on safety. Trends in social factors affect the demand for a company's products and how that company operates. For example, an ageing population may imply a smaller and less-willing workforce (thus increasing the cost of labor). Furthermore, companies may change various management strategies to adapt to these social trends (such as recruiting older workers).

- **Technological Factors**

Technological factors include ecological and environmental aspects, such as R&D activity, automation, technology incentives and the rate of technological change.

They can determine barriers to entry, minimum efficient production level and influence outsourcing decisions. Furthermore, technological shifts can affect costs, quality, and lead to innovation.

- **Environmental Factors**

Environmental factors include weather, climate, and climate change, which may especially affect industries such as tourism, farming, and insurance. Furthermore, 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.

- **Legal Factor**

Legal factors include discrimination law, consumer law, antitrust law, employment law, and health and safety law. These factors can affect how a company operates, its costs, and the demand for its products.

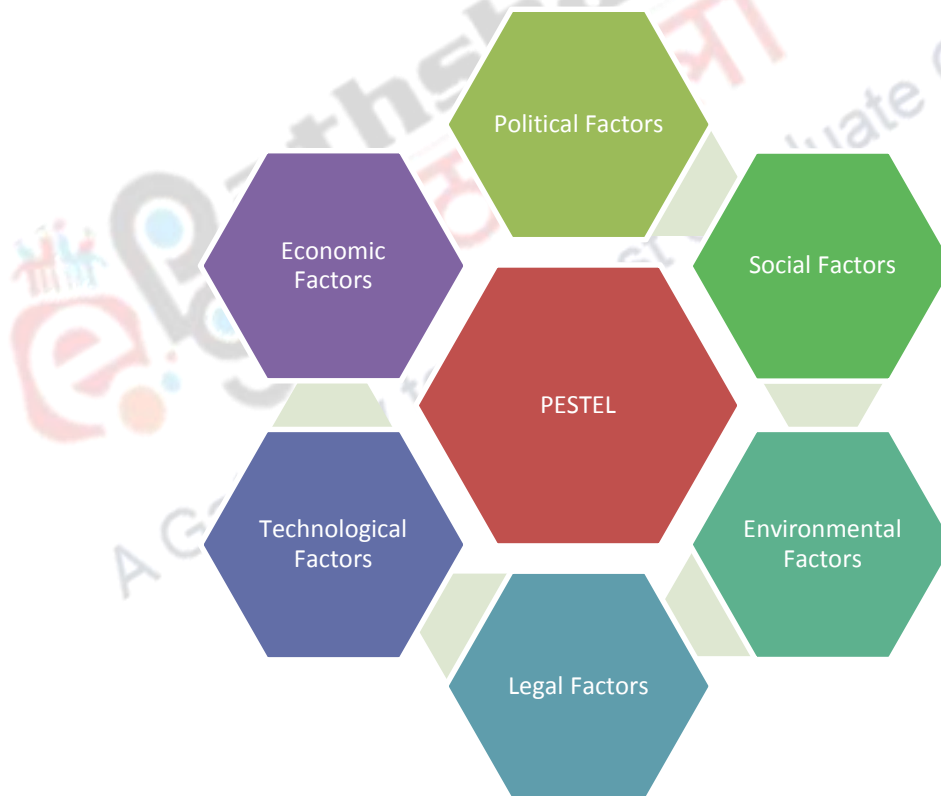


Figure 3: PESTEL Model

7. Impact of Business on Environment

Business decisions influence employees, customers, suppliers and competitors, while company operations affect communities, governments and the environment. To evaluate the impact of these decisions and activities, you have to divide their effects into categories.

- **Economic**

Your business has an economic impact on society through the wages you pay your employees, the materials you buy from your suppliers, and the prices you charge your customers. You have a positive social impact on your employees if you pay them a living wage and benefits to reduce the stress of unexpected events. You have a positive effect on your suppliers if you pay them fairly and on time for their supplies. Your effect on customers is positive if you give them good value for the price they pay for your products and services.

- **Governance**

The social impact of corporate governance contributes to the ethical climate of society. If businesses offer bribes to secure work or other benefits, engage in accounting fraud, or break regulatory and legal constraints on their operations, the ethics of society suffer. In addition to a deteriorating ethical environment, such corruption may raise the price of goods for consumers, such as happens when companies engage in price fixing.

- **Privacy**

To process orders and deliver services, companies have to collect personal information on their customers. Some information may be sensitive, such as when companies deliver medical services and have medical histories on file. Businesses have a negative impact on society if consumers find out that companies are not keeping such information secure or are selling it to third parties. The lack of trust inhibits the free exchange of personal and private information that facilitates carrying on business efficiently.

- **Intellectual Property**

Respect of patents and copyrights is both a social and ethical issue. Businesses own intellectual property and they use that of others. They have to operate with a balance that protects their own interests in a responsible way while avoiding infringing patents and copyrights. If businesses either act excessively in protecting their intellectual property or actively use that of others without permission, they risk alienating their customers and hurting their public image.

- **Environment**

A key area of business influence on society is environmental protection. Companies make a substantial direct contribution to greenhouse gases and the production of waste. Businesses that implement environmental policies to use energy more efficiently, reduce waste, and in general lighten their environmental footprint can reduce their internal costs and promote a positive image of their company. The environmental initiatives of a market leader often force competitors to take similar action for an increased beneficial effect on the environment.

8. Summary

- Business environment is basically combination of internal and external factors that influence a company's operating situation. The business environment can include factors such as: clients and suppliers; its competition and owners; improvement in technology; laws and government activities; and market, social and economic trends
- The nature of business environment is very much dynamic, it keeps on changing over the period of time. The changes in business environment are unpredictable. It is very difficult to predict the exact nature of future happenings and the changes in economic and social environment. .
- Business environment helps the business in determining opportunities, threats & growth direction over the period of time.
- PESTEL is a part of the external analysis when conducting a strategic analysis or doing market research and gives a certain overview of the different macro environmental factors that the company has to take into consideration.