



CHAPTER 3

BUSINESS ENVIROMENT
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SYLLABUS

Concept	After going through this unit, the student/ learner would be able to:
Business Environment- concept and importance	• Understand the concept of 'Business Environment'. • Describe the importance of business environment
Dimensions of Business Environment- Economic, Social, Technological, Political and Legal Demonetization - concept and features	• Describe the various dimensions of 'Business Environment'. • Understand the concept of demonetization
Impact of Government policy changes on business with special reference to liberalization, privatization and globalization in India	• Examine the impact of government policy changes on business in India with reference to liberalization, privatization and globalization since 1991. • Discuss the managerial response to changes in business environment.

Meaning

- ✚ Environment refers to the surroundings in which a person or organization operates.
- ✚ The term 'business environment' means aggregate of all conditions, events and influences that are outside the control of a business enterprise but that may affect its performance.
- ✚ Thus, the economic, social, political, technological and other forces which operate outside a business enterprise are part of its environment.
- ✚ The individual consumers or competing enterprises as well as the governments, consumer groups, competitors, courts, media and other institutions working outside an enterprise constitute its environment.
- ✚ These individuals, institutions and forces are likely to influence the performance of a business enterprise although they happen to exist outside its boundaries.



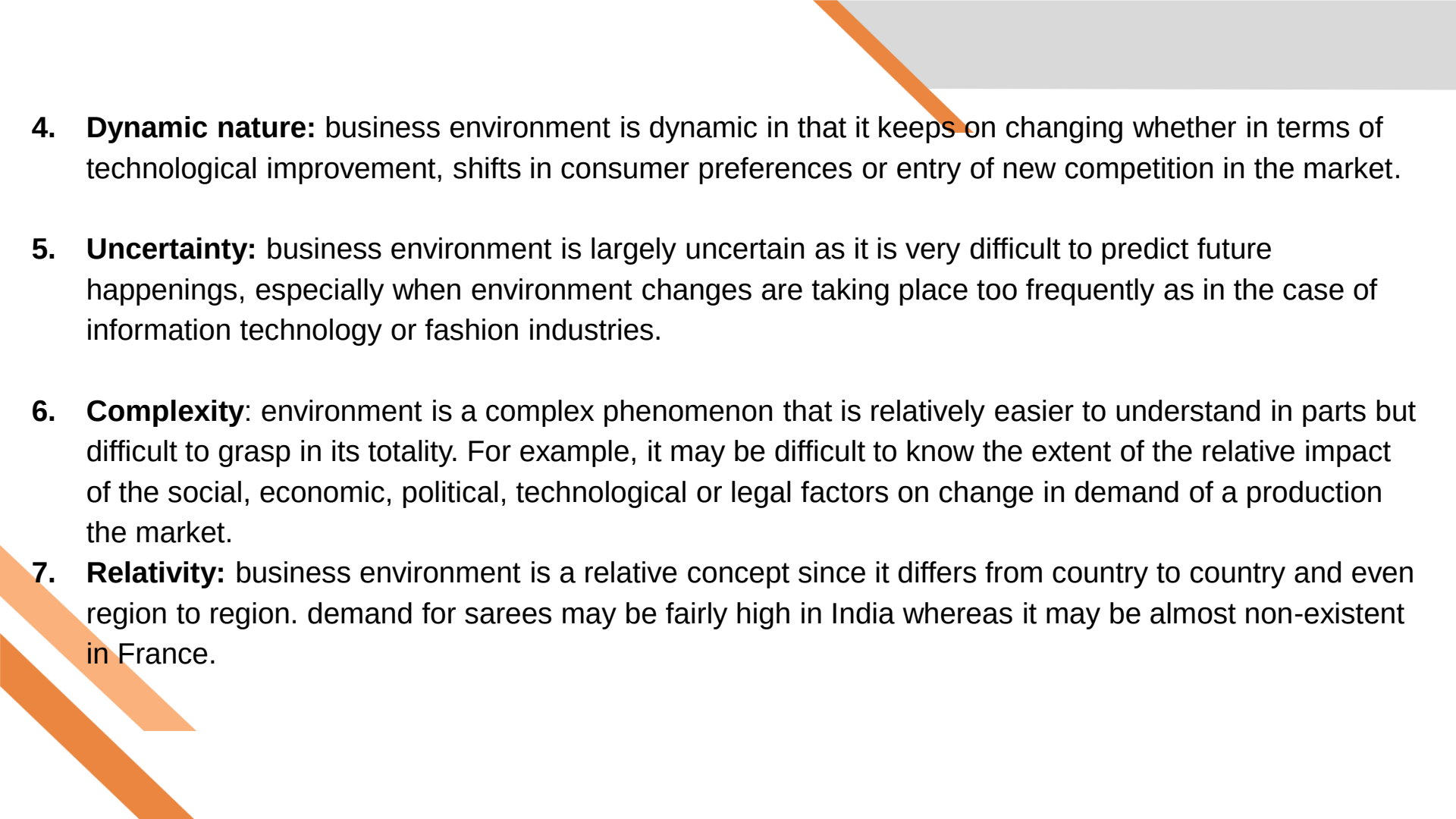
- ✚ For example, changes in government's economic policies, rapid technological developments, political uncertainty, and changes in fashions and tastes of consumers and increased competition in the market - all influence the working of a business enterprise in important ways.
- ✚ Increase in taxes by government can make things expensive to buy. Technological improvements may render existing products obsolete. Political uncertainty may create fearing the minds of investors. Changes in fashions and tastes of consumers may shift demand in the market from existing products to new ones. Increased competition in the market may reduce profit margins of firms.



How COVID-19 Has Impacted The Business Environment In India?

Features Of Business Environment

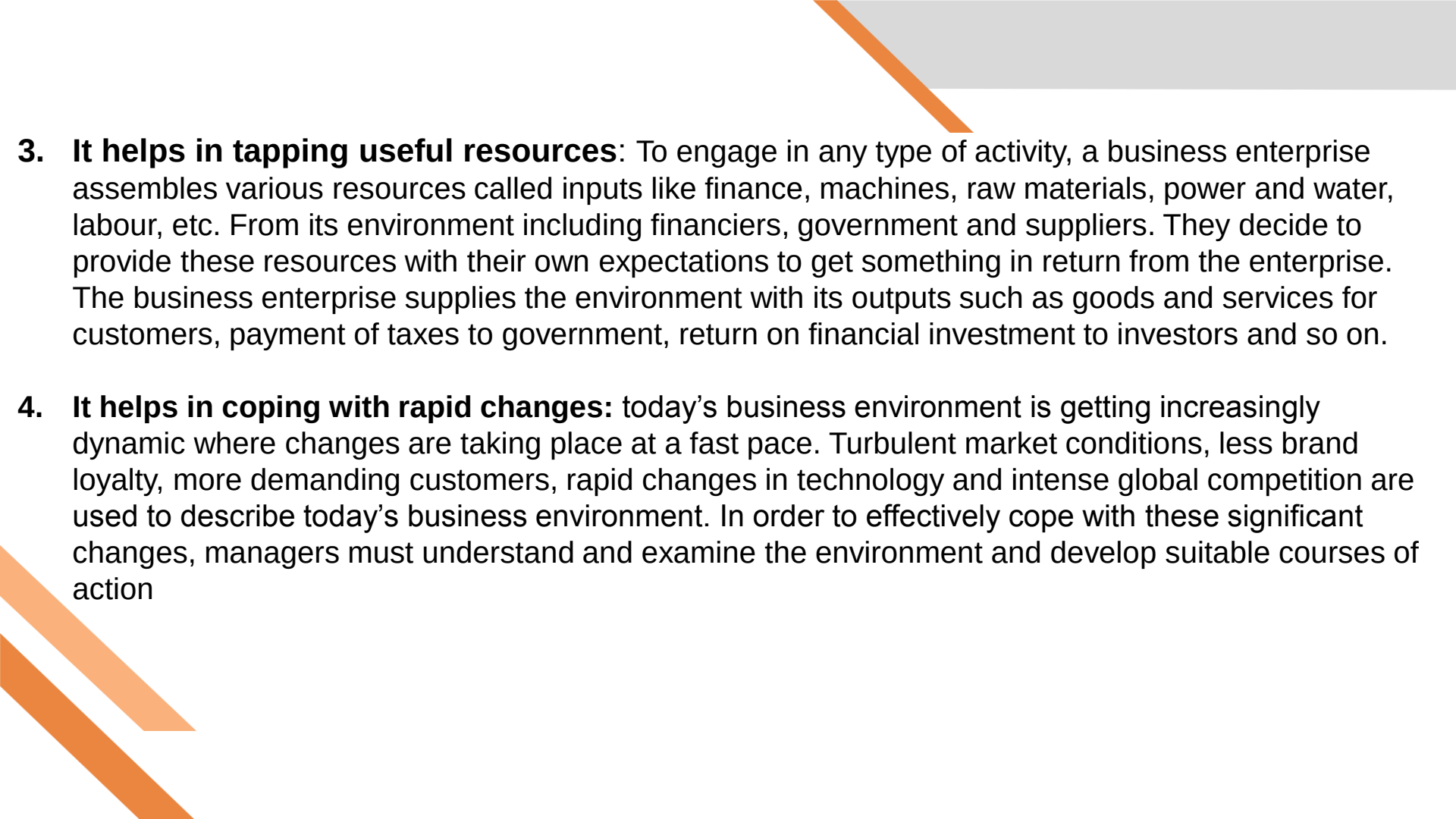
1. **Totality of external forces:** business environment is the sum total of all things external to business firms and, as such, is aggregative in nature.
2. **Specific and general forces:** business environment includes both specific and general forces. Specific forces (such as investors, customers, competitors and suppliers) affect individual enterprises directly and immediately in their day-to-day working. General forces (such as social, political, legal and technological conditions) have impact on all business enterprises and thus may affect an individual firm only indirectly.
3. **Inter-relatedness:** different elements or parts of business environment are closely interrelated. For example, increased life expectancy of people and increased awareness for healthcare has increased the demand for many health products and services like soft drinks, fat-free cooking oil, and health resorts.

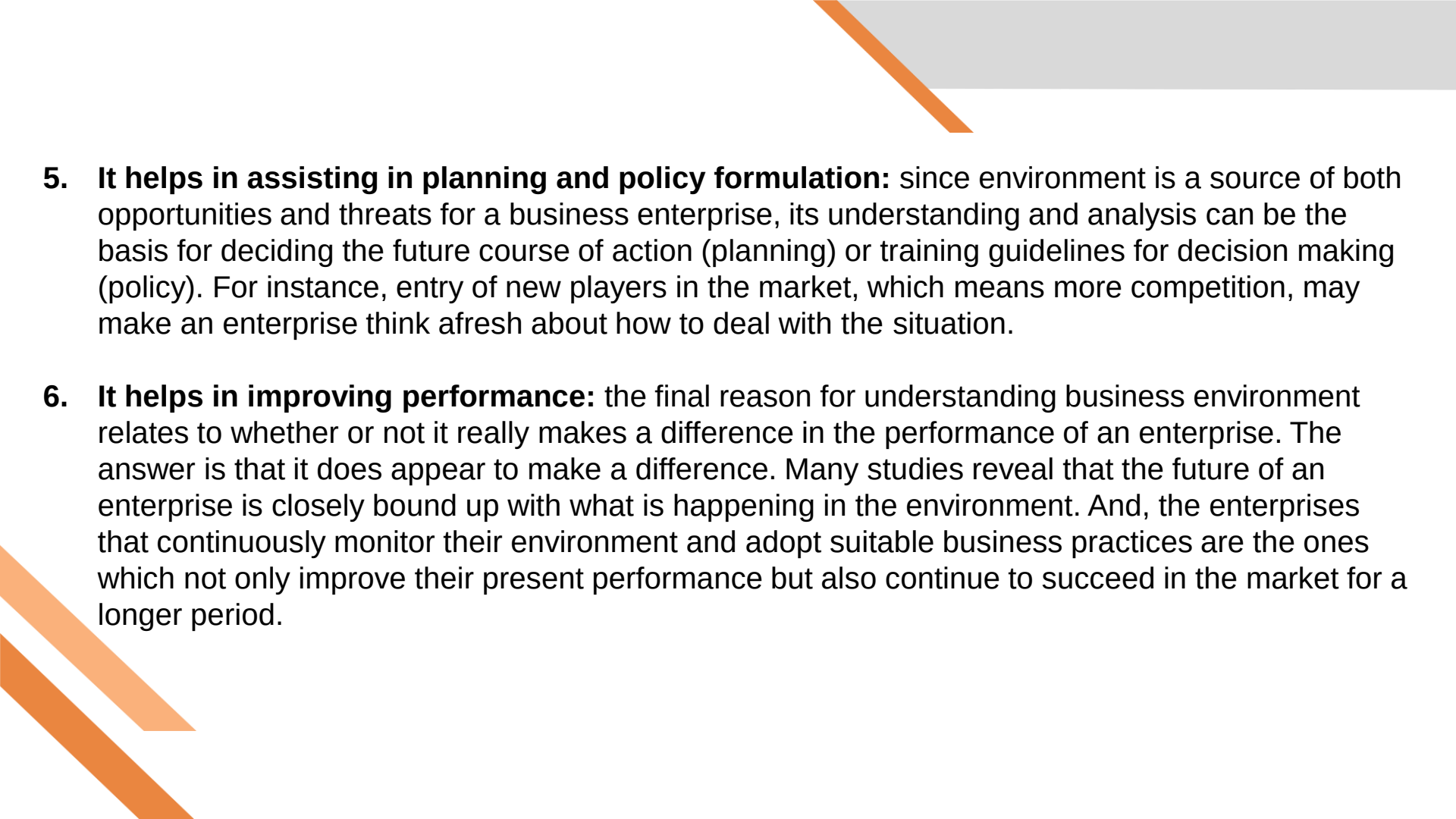
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4. **Dynamic nature:** business environment is dynamic in that it keeps on changing whether in terms of technological improvement, shifts in consumer preferences or entry of new competition in the market.
 5. **Uncertainty:** business environment is largely uncertain as it is very difficult to predict future happenings, especially when environment changes are taking place too frequently as in the case of information technology or fashion industries.
 6. **Complexity:** environment is a complex phenomenon that is relatively easier to understand in parts but difficult to grasp in its totality. For example, it may be difficult to know the extent of the relative impact of the social, economic, political, technological or legal factors on change in demand of a production the market.
 7. **Relativity:** business environment is a relative concept since it differs from country to country and even region to region. demand for sarees may be fairly high in India whereas it may be almost non-existent in France.

Importance of Business Environment

- ✚ Modern business world is a world of competitions. Those who are incompetent to face this competition will be out of the field. For this it is vital to adapt things according to the environment.
- ✚ For adjusting the operations of an organization according to the environment, environment scanning is essential. Environment scanning means monitoring the environment of each organization and identifying the constraints and opportunities before them.

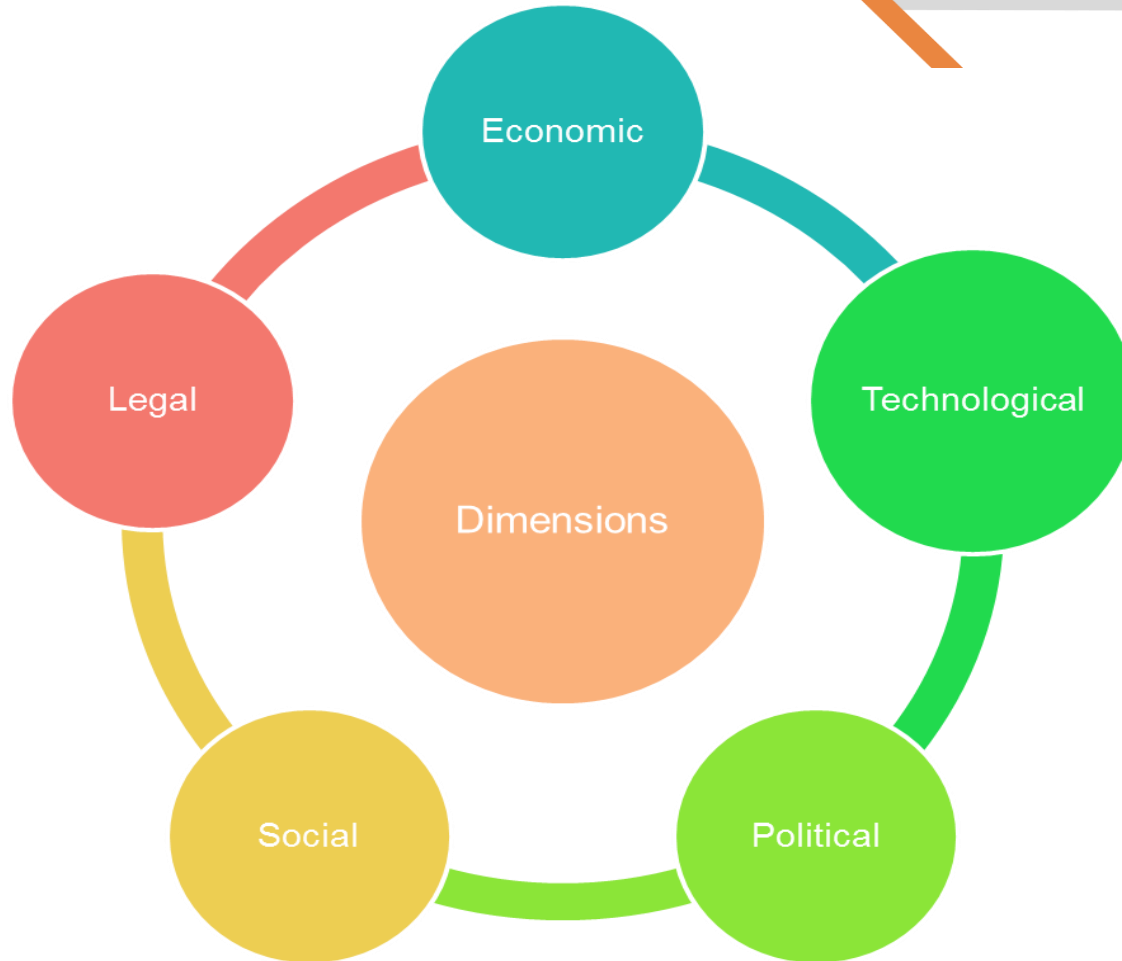
- 1. It enables the firm to identify opportunities and getting the first mover advantage:** opportunities refer to the positive external trends or changes that will help a firm to improve its performance. Environment provides numerous opportunities for business success. Early identification of opportunities helps an enterprise to be the first to exploit them instead of losing them to competitors. For example, maruti udyog became the leader in the small car market because it was the first to recognize the need for small cars in an environment of rising petroleum prices and large middle class population in India
- 2. It helps the firm to identify threats and early warning signals:** threats refer to the external environment trends and changes that will hinder a firm's performance. Besides opportunities, environment happens to be the source of many threats. Environmental awareness can help managers to identify various threats on time and serve as an early warning signal. For example, if an Indian firm finds that a foreign multinational is entering the Indian market with new substitutes, it should act as a warning signal. On the basis of this information, the Indian firms can prepare themselves to meet the threat by adopting such measures as improving the quality of the product, reducing cost of the production, engaging in aggressive advertising, and so on

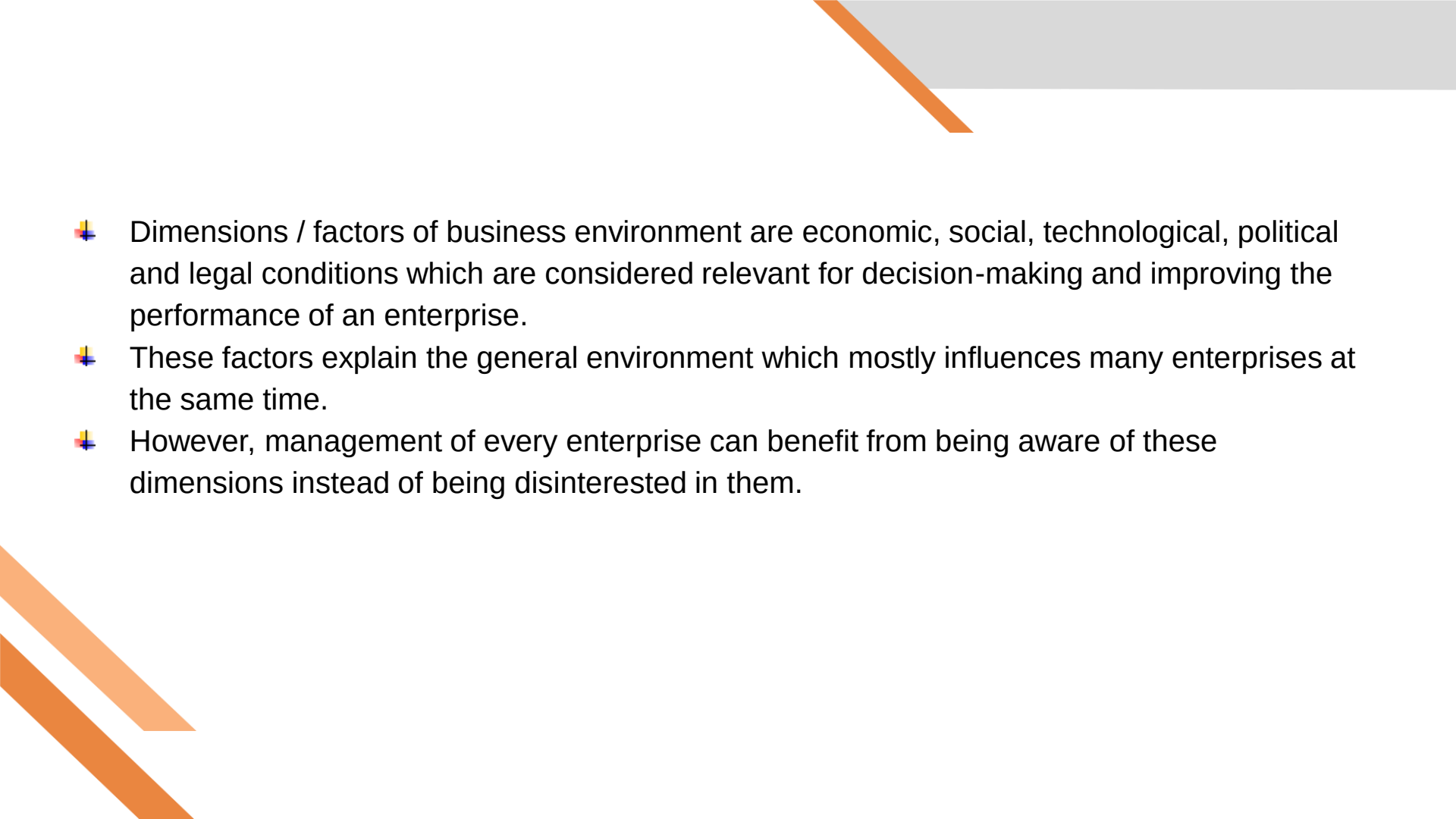
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- 3. It helps in tapping useful resources:** To engage in any type of activity, a business enterprise assembles various resources called inputs like finance, machines, raw materials, power and water, labour, etc. From its environment including financiers, government and suppliers. They decide to provide these resources with their own expectations to get something in return from the enterprise. The business enterprise supplies the environment with its outputs such as goods and services for customers, payment of taxes to government, return on financial investment to investors and so on.
 - 4. It helps in coping with rapid changes:** today's business environment is getting increasingly dynamic where changes are taking place at a fast pace. Turbulent market conditions, less brand loyalty, more demanding customers, rapid changes in technology and intense global competition are used to describe today's business environment. In order to effectively cope with these significant changes, managers must understand and examine the environment and develop suitable courses of action

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5. **It helps in assisting in planning and policy formulation:** since environment is a source of both opportunities and threats for a business enterprise, its understanding and analysis can be the basis for deciding the future course of action (planning) or training guidelines for decision making (policy). For instance, entry of new players in the market, which means more competition, may make an enterprise think afresh about how to deal with the situation.
 6. **It helps in improving performance:** the final reason for understanding business environment relates to whether or not it really makes a difference in the performance of an enterprise. The answer is that it does appear to make a difference. Many studies reveal that the future of an enterprise is closely bound up with what is happening in the environment. And, the enterprises that continuously monitor their environment and adopt suitable business practices are the ones which not only improve their present performance but also continue to succeed in the market for a longer period.

Dimensions of Business Environment

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- ✚ Dimensions / factors of business environment are economic, social, technological, political and legal conditions which are considered relevant for decision-making and improving the performance of an enterprise.
 - ✚ These factors explain the general environment which mostly influences many enterprises at the same time.
 - ✚ However, management of every enterprise can benefit from being aware of these dimensions instead of being disinterested in them.

Economic environment

- ❑ Interest rates, inflation rates, changes in disposable income of people, stock market indices and the value of rupee are some of the economic factors that can affect management practices in a business enterprise.
- ❑ For example, in case of construction companies and automobile manufacturers, low longer-term rates are beneficial because they result in increased spending by consumers for buying homes and cars on borrowed money.
- ❑ High inflation rates generally result in constraints on business enterprises as they increase the various costs of business such as the purchase of raw materials or machinery and payment of wages and salaries to employees.

Components of Economic Environment

1. Existing structure of the economy in terms of relative role of private and public sectors
2. The rates of growth of GNP and per capita income at current and constant prices
3. Rates of saving and investment
4. Volume of imports and exports of different items
5. Balance of payments and changes in foreign exchange reserves
6. Agricultural and industrial production trends
7. Expansion of transportation and communication facilities
8. Money supply in the economy
9. Public debt (internal and external)
10. Planned outlay in private and public sectors

Social environment

- ❑ The social environment of business include the social forces like customs and traditions, values, social trends, society's expectations from business, etc.
- ❑ Traditions define social practices that have lasted for decades or even centuries. For example, the celebration of diwali, eid, christmas, and guru purnima in india provides significant financial opportunities for greetings card companies, sweets or confectionery manufacturers, tailoring outlets and much other related business.
- ❑ Social trends present various opportunities and threats to business enterprises. For example, the health-and-fitness trend has become popular among large number of urban dwellers.
- ❑ This has created demand for products like organic food, gyms, and bottled (mineral) water and food supplements.

Major Elements of Social Environment

1. Attitudes towards product innovations, lifestyles, occupational distribution and consumer preferences
2. Concern with quality of life
3. Life expectancy
4. Expectations from the workforce
5. Shifts in the presence of women in the workforce
6. Birth and death rates
7. Population shifts
8. Educational system and literacy rates
9. Consumption habits
10. Composition of family

- ❖ Technological environment includes forces relating to scientific improvements and innovations which provide new ways of producing goods and services and new methods and techniques of operating business.
- ❖ For example, it is common now to see computerised information kiosks, and worldwide web multimedia pages highlighting the virtues of products.
- ❖ Similarly, retailers have direct links with supplier's who replenish stocks when needed. Manufacturers have flexible manufacturing systems.
- ❖ Airline companies have internet and world wide web pages where customers can look for flight times, destinations and fares and book their tickets online.
- ❖ In addition, continuing innovations in different scientific and engineering fields such as lasers, robotics, biotechnology, food preservatives, medicine, telecommunication and synthetic fuels have provided numerous opportunities and threats for many different enterprises.

Political Environment

- ❑ Political environment includes political conditions such as general stability and peace in the country and specific attitudes that elected government representatives hold towards business.
- ❑ Political stability, thus, builds up confidence among businesspeople to invest in the long term projects for the growth of the economy.
- ❑ Political instability can shake that confidence. Similarly, the attitudes of government officials towards business may have either positive or negative impact upon business.
- ❑ For example, even after opening up of our economy in 1991, foreign companies found it extremely difficult to cut through the bureaucratic red tape to get permits for doing business in India.
- ❑ Sometimes, it took months to process even their application for the purpose. As a result these companies were discouraged from investing in our country.
- ❑ The situation has improved over time

Major Elements of the Political Environment

1. Prevailing political system
2. The degree of politicisation of business and economic issues
3. Dominant ideologies and values of major political parties
4. The nature and profile of political leadership and thinking of political personalities
5. The level of political morality
6. Political institutions like the government and allied agencies
7. Political ideology and practices of the ruling party
8. The extent and nature of government intervention in business
9. The nature of relationship of our country with foreign countries.



Legal Environment

- ❖ Legal environment includes various legislations passed by the government administrative orders issued by government authorities, court judgments as well as the decisions rendered by various commissions and agencies at every level of the government—centre, state or local.
- ❖ An adequate knowledge of rules and regulations framed by the government is a pre-requisite for better business performance. Non-compliance of laws can land the business enterprise into legal problems.

1. **Trade Mark Act – 1969,**
2. **Essential Commodities Act – 1955,**
3. **Consumer Protection Act – 1986,**
4. **The Contract Act,**
5. **Companies Act – 1956,**
6. **Factories Act,**
7. **Industrial Disputes Act,**
8. **Workers Compensation Act,**
9. **Minimum Wages Act,**
10. **Income Tax Act – 1961,**
11. **Sales Tax Act etc.**



Economic Environment in India

✚ The economic environment in India consists of various macro level factors related to the means of production and distribution of wealth which have an impact on business and industry. These include:

1. Stage of economic development of the country.
2. The economic structure in the form of mixed economy which recognises the role of both public and private sectors
3. Economic policies of the government, including industrial, monetary and fiscal policies.
4. Economic planning, including five year plans, annual budgets, and so on.
5. Economic indices, like national income, distribution of income, rate and growth of GNP, per capita income, disposal personal income, rate of savings and investments, value of exports and imports, balance of payments, and so on.
6. Infrastructural factors, such as, financial institutions, banks, modes of transportation communication facilities.

✚ Business enterprises in India do realise the importance and impact of the economic environment on their working. Almost all annual company reports presented by their chairpersons devote considerable attention to the general economic environment prevailing in the country and an assessment of its impact on their companies.

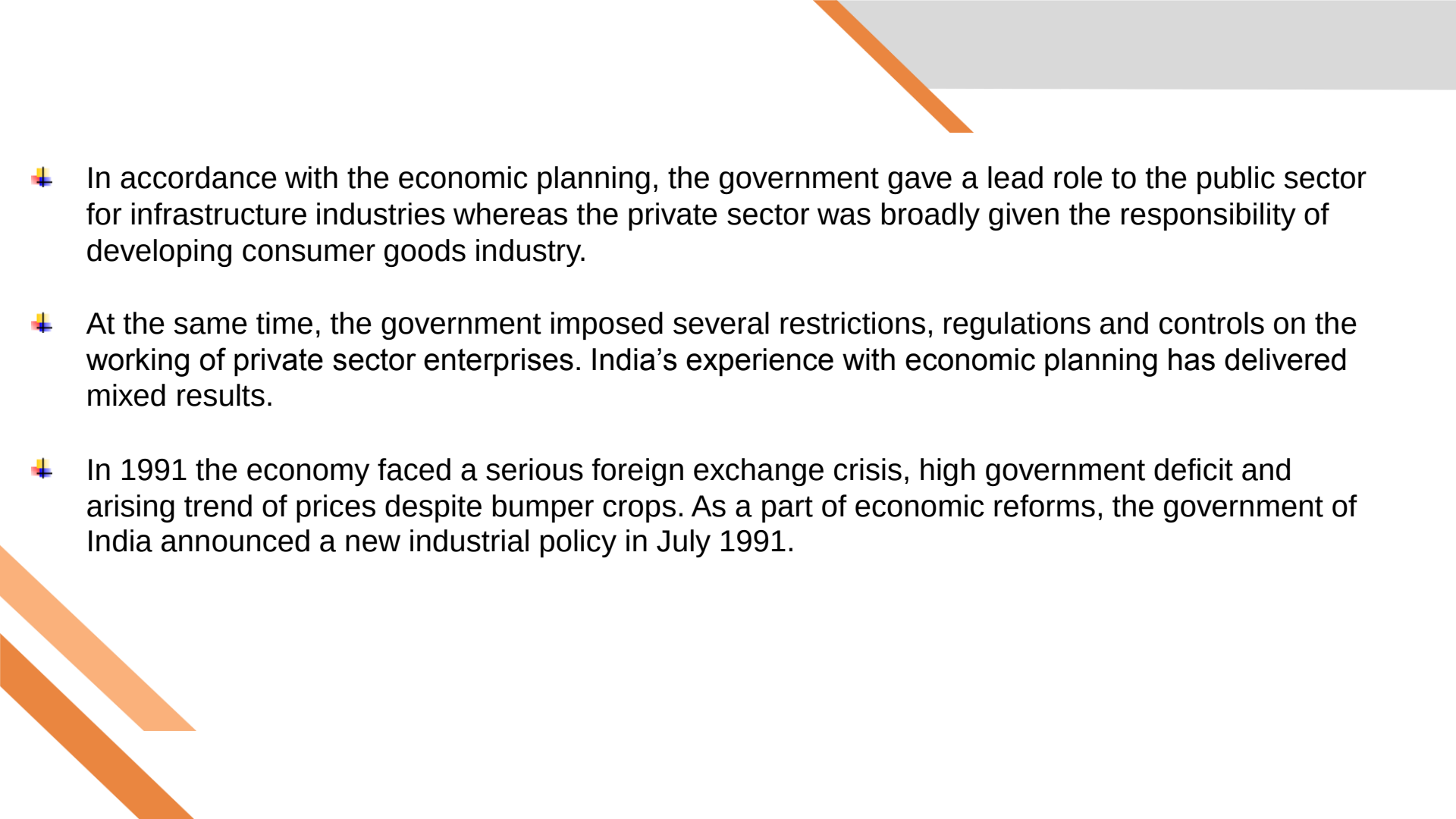
At the time of independence :-

- (a) The Indian economy was mainly agricultural and rural in character;
- (b) About 70% of the working population was employed in agriculture;
- (c) About 85% of the population was living in the villages;
- (d) Production was carried out using irrational, low productivity technology;
- (e) Communicable diseases were widespread, mortality rates were high. There was no good public health system

 In order to solve economic problems of our country, the government took several steps including control by the state of certain industries, central planning and reduced importance of the private sector.

 The main objectives of India's development plans were:

- (a) Initiate rapid economic growth to raise the standard of living, reduce unemployment and poverty;
- (b) Become self-reliant and set up a strong industrial base with emphasis on heavy and basic industries;
- (c) Reduce inequalities of income and wealth;
- (d) Adopt a socialist pattern of development — based on equality and prevent exploitation of man by man.

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- ✚ In accordance with the economic planning, the government gave a lead role to the public sector for infrastructure industries whereas the private sector was broadly given the responsibility of developing consumer goods industry.
 - ✚ At the same time, the government imposed several restrictions, regulations and controls on the working of private sector enterprises. India's experience with economic planning has delivered mixed results.
 - ✚ In 1991 the economy faced a serious foreign exchange crisis, high government deficit and arising trend of prices despite bumper crops. As a part of economic reforms, the government of India announced a new industrial policy in July 1991.

Features of New Industrial Policy 1991

- (a) The government reduced the number of industries under compulsory licensing to six.
- (b) Many of the industries reserved for the public sector under the earlier policy, were de reserved. The role of the public sector was limited only to four industries of strategic importance.
- (c) Disinvestment was carried out in case of many public sector industrial enterprises.
- (d) Policy towards foreign capital was liberalised. The share of foreign equity participation was increased and in many activities 100 percent foreign direct investment (FDI) was permitted.
- (e) Automatic permission was now granted for technology agreements with foreign companies.
- (f) Foreign investment promotion board (FIPB) was set up to promote and channelize foreign investment in India.



✚ Appropriate measures were taken to remove obstacles in the way of growth and expansion of industrial units of large industrial houses. Small-scale sector was assured all help and accorded due recognition.

✚ This policy has sought:-

1. To liberate industry from the shackles of the licensing system (liberalisation),
 2. Reduce the role of the public sector (privatisation)
 3. Encourage foreign private participation in India's industrial development (globalisation).
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THE MAJOR PROGRAMS OF THIS NEW POLICY

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Liberalization means liberating the economy from the regulations and restrictions on economic growth. These reforms were aimed at liberalising the Indian business and industry from all unnecessary controls and restrictions. They signalled the end of the licence-permit-quota raj.

Liberalisation of the Indian industry has taken place with respect to:

1. Abolishing licensing requirement in most of the industries except a short list,
2. Freedom in deciding the scale of business activities i.e., no restrictions on expansion or contraction of business activities,
3. Removal of restrictions on the movement of goods and services,
4. Freedom in fixing the prices of goods services,
5. Reduction in tax rates and lifting of unnecessary controls over the economy,
6. Simplifying procedures for imports and exports, and
7. Making it easier to attract foreign capital and technology to India.

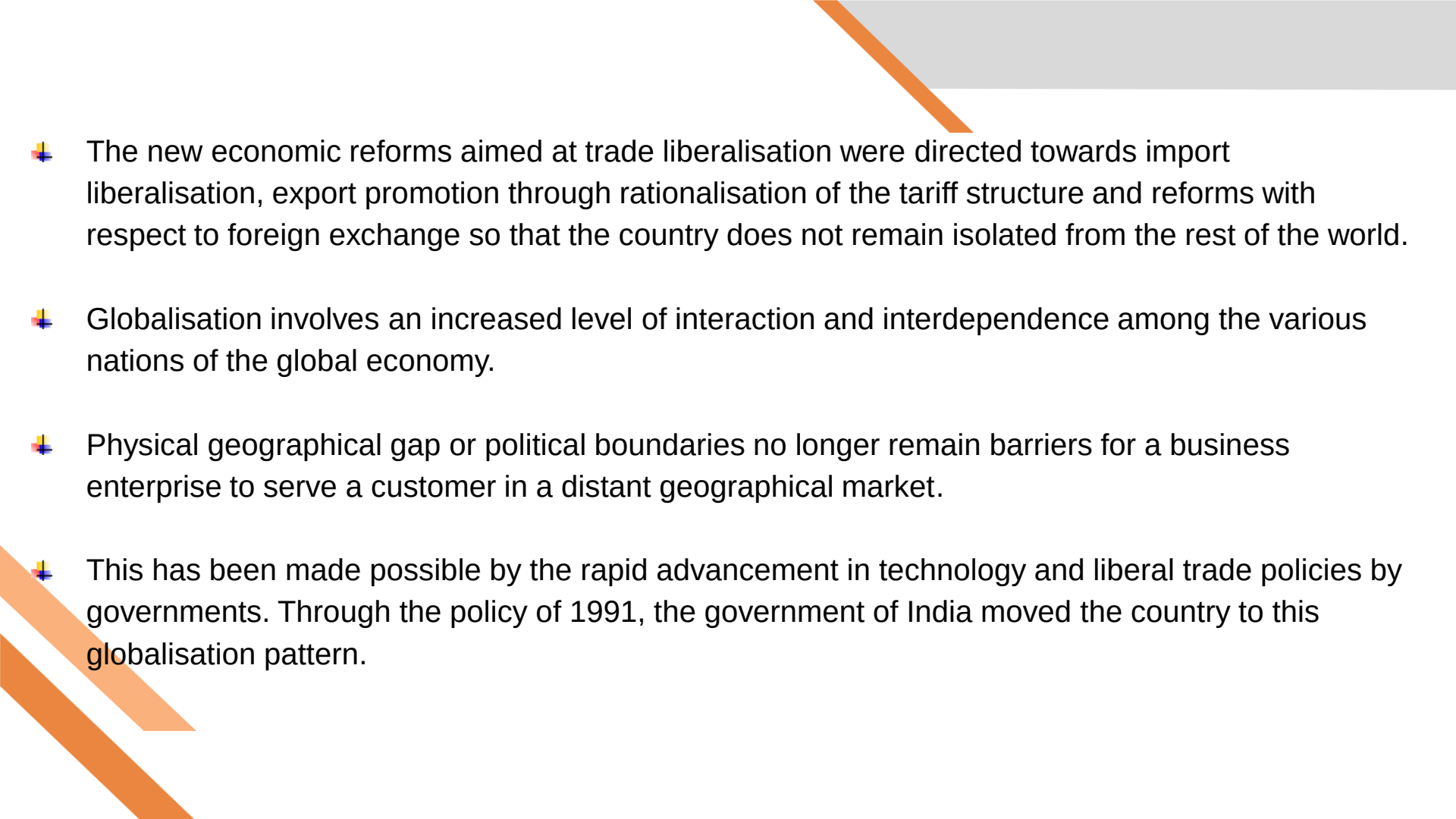
The term disinvestments used here means transfer in the public sector enterprises to the private sector. It results in dilution of stake of the government in the public enterprise.

- ✚ These new set of economic reforms were aimed at giving greater role to the private sector in the nation building process and a reduced role to the public sector.
- ✚ This was a reversal of the development strategy pursued so far by Indian planners.
- ✚ To achieve this, the government redefined the role of the public sector in the new industrial policy of 1991, adopted the policy of planned disinvestments of the public sector and decided to refer the loss making and sick enterprises to the board of industrial and financial reconstruction.

The main features of privatization are as follows:

1. **Disinvestment** of a part of the shares held by the government in public sector undertakings (PSU'S). This results in passing of ownership, control and management of PSU's to the private sector.
2. **De-reservation** of areas formerly reserved for the public sector. This allows the private sector to enter into new areas.

- ❑ Globalization means free movement of goods, capital and labour across the globe. It is the integration of the various economies of the world leading towards the emergence of a cohesive global economy.
- ❑ Till 1991, the government of India had followed a policy of strictly regulating imports in value and volume terms. These regulations were with respect to
 - (a) Licensing of imports,
 - (b) Tariff restrictions and
 - (c) Quantitative restrictions.

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- ✚ The new economic reforms aimed at trade liberalisation were directed towards import liberalisation, export promotion through rationalisation of the tariff structure and reforms with respect to foreign exchange so that the country does not remain isolated from the rest of the world.
 - ✚ Globalisation involves an increased level of interaction and interdependence among the various nations of the global economy.
 - ✚ Physical geographical gap or political boundaries no longer remain barriers for a business enterprise to serve a customer in a distant geographical market.
 - ✚ This has been made possible by the rapid advancement in technology and liberal trade policies by governments. Through the policy of 1991, the government of India moved the country to this globalisation pattern.

Demonetisation

- ✚ The government of India made an announcement on November 8, 2016 with profound implications for the Indian economy.
- ✚ The two largest denomination notes 500 and 1000 were 'demonetised' with immediate effect, ceasing to be legal tender except for a few specified purposes such as paying utility bills.
- ✚ This led to eighty six per cent of the money in circulation invalid. The people of India had to deposit the invalid currency in the banks which came along with the restrictions placed on cash withdrawals.
- ✚ In other words, restrictions were placed on the convertibility of domestic money and bank deposits.
- ✚ The aim of demonetization was to curb corruption, fake notes, use of currency for illegal activities like terrorism, accumulation of black money generated by income that has not been declared to the tax authorities

Features

1. **A tax administration tool** – demonetisation is viewed as a tax administration measure. Cash holdings arising from declared income was readily deposited in banks and exchanged for new notes. But those with black money had to declare their unaccounted wealth and pay taxes at a penalty rate
2. **To stop tax evasion** – demonetisation is also interpreted as a shift on the part of the government indicating that tax evasion will no longer be tolerated or accepted.
3. **To channelize the savings** – demonetisation also led to tax administration channelizing savings into the formal financial system. Though, much of the cash that has been deposited in the banking system is bound to be withdrawn but some of the new deposits schemes offered by the banks will continue to provide base loans, at lower interest rates.
4. **Cash less economy** – demonetisation is to create a less-cash or cash-lite economy, i.e., channelling more savings through the formal financial system and improving tax compliance. Though there are arguments against this as digital transactions require use of cell phones for customers and point-of-sale (POS) machines for merchants, which will only work if there is internet connectivity.

Impact of Demonetisation

1. Money/interest rates

1. Decline in cash transactions
2. Bank deposits increased
3. Increase in financial savings

2. Private wealth

1. Declined since some high demonetised notes were not returned and real estate prices fell

3. Public sector wealth

1. No effect

4. Digitisation

1. Digital transactions amongst new users (RUPAY/AEPS) increased

5. Real estate

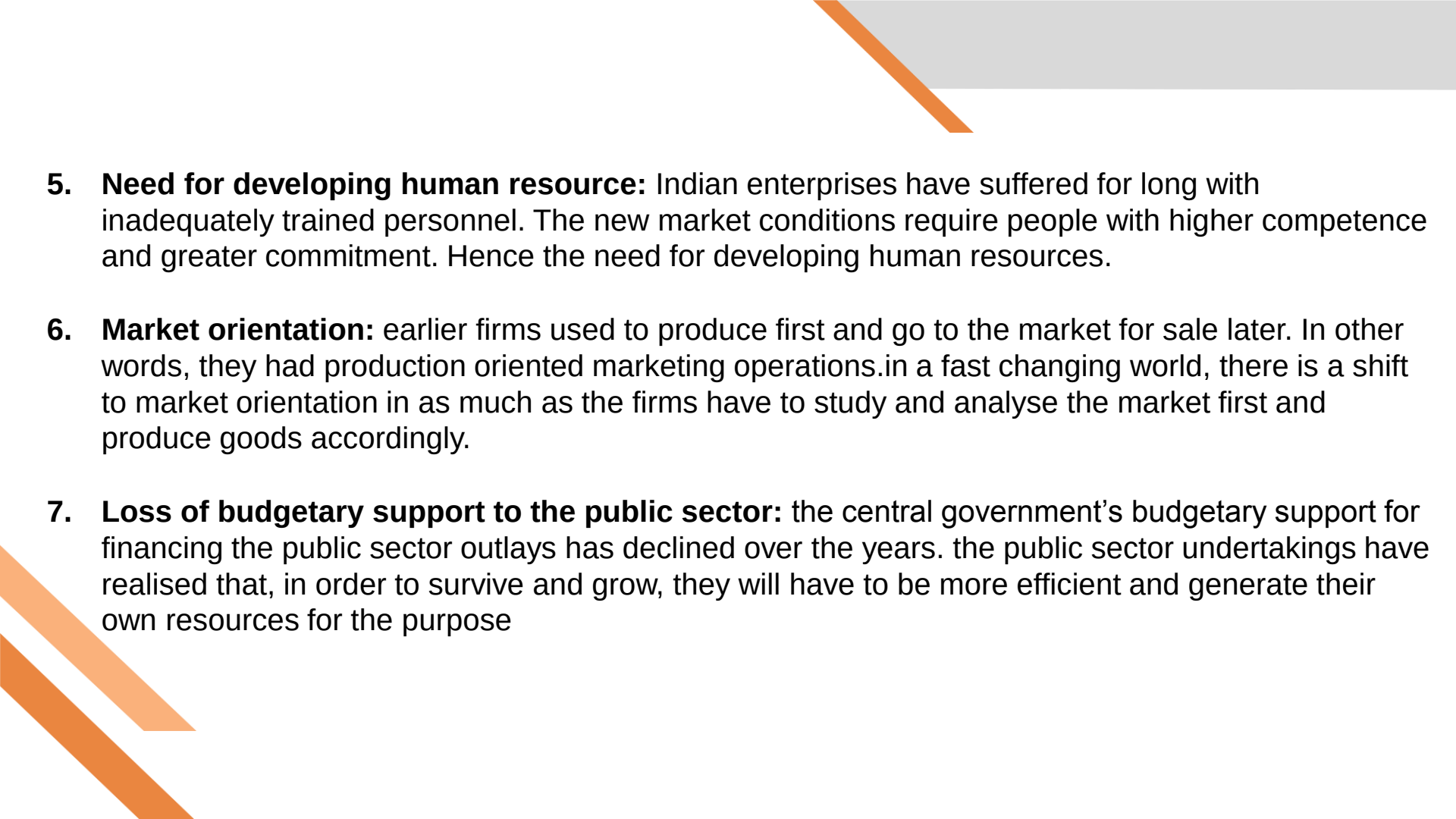
1. Prices declined

6. Tax collection

1. Rise in income tax collection because of increased disclosure

Impact of Changes in Government Policy on Business and Industry

1. **Increasing competition:** as a result of changes in the rules of industrial licensing and entry of foreign firms, competition for Indian firms has increased especially in service industries like telecommunications, airlines, banking, insurance, etc. Which were earlier in the public sector
2. **More demanding customers:** customers today have become more demanding because they are well-informed. Increased competition in the market gives the customers wider choice in purchasing better quality of goods and services.
3. **Rapidly changing technological environment:** increased competition forces the firms to develop new ways to survive and grow in the market. New technologies make it possible to improve machines, process, products and services. the rapidly changing technological environment creates tough challenges before smaller firms
4. **Necessity for change:** in a regulated environment of pre-1991 era, the firms could have relatively stable policies and practices. After 1991, the market forces have become turbulent as a result of which the enterprises have to continuously modify their operations.

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5. **Need for developing human resource:** Indian enterprises have suffered for long with inadequately trained personnel. The new market conditions require people with higher competence and greater commitment. Hence the need for developing human resources.
 6. **Market orientation:** earlier firms used to produce first and go to the market for sale later. In other words, they had production oriented marketing operations. In a fast changing world, there is a shift to market orientation in as much as the firms have to study and analyse the market first and produce goods accordingly.
 7. **Loss of budgetary support to the public sector:** the central government's budgetary support for financing the public sector outlays has declined over the years. The public sector undertakings have realised that, in order to survive and grow, they will have to be more efficient and generate their own resources for the purpose.

Crisis Of June 1991

Major elements of the crisis situation which led the government of India to announce economic reform were:

1. A serious fiscal crisis in which the fiscal deficit reached the level of 6.6 percent of GDP in 1990-91.
2. Heavy internal debt which rose to about 50 per cent of GDP with interest payments draining about 39 per cent of total revenue collections of the central government.
3. Low GNP growth rate which fell to 1.4 per cent from the peak level of 10.5 per cent in 1988-89 (at 1980-81 prices).
4. Low overall agricultural production, food grain production and industrial production showed negative growth rates of -2.8 per cent, -5.3 per cent and -0.1 per cent respectively.
5. Soaring inflation rate based both on wholesale price index and consumer price index (for industrial workers) at 13-14 per cent.
6. Shrinkage of foreign trade, imports (in \$ terms) fell by 19.4 per cent and exports by 1.5 per cent.

Crisis Of June 1991

7. Depreciation of rupee by 26.7 per cent vis-à-vis us dollars.
8. Fall of foreign exchange reserves to such a low level that they were barely adequate to meet the import requirements of a few weeks. Non-resident Indians were withdrawing their deposits at an alarmingly high rate.
9. The confidence of the international financial institutions was badly shaken and in just over a year its creditworthiness rating fell from AAA to BB+ (put on credit watch).
10. The country was on the verge of defaulting on international financial obligations and the situation warranted immediate policy action to save the situation.
11. In May 1991, the government had to lease 20 tons of gold out of its stock to the state bank of India to enable it to sell the gold with repurchase option after six months.
12. In addition, reserve bank of India was allowed to pledge 47 tons of gold to the bank of England to raise a loan of \$600 million.

Digitalisation Has Broadly Impacted Three Sections Of Society

1. The poor, who are largely outside the digital economy.
2. The less affluent, who are becoming part of the digital economy who have been covered under *jan dhan* accounts and *rupay* cards.
3. The affluent, who are fully conversant with digital transactions.



Thanks !

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