

BUSINESS STUDIES

Chapter 3: Business Environment



Business Environment

Meaning of Business Environment:

Business environment refers to all the factors that are outside the control of the business enterprise but may equally affect the performance of the business. The social, political, economic, technological factors that operate outside a business forms a part of the business environment.



Features of Business Environment:

1. **Totality of external forces:** Includes every external or outside force that could impact a business organisation such as government, competitors, etc.
2. **Specific and general forces:** Specific forces are the forces which directly affect a specific business organisation. General forces are those forces which pose a direct impact on the overall industry, but pose an indirect effect on a business enterprise.
3. **Inter-relatedness:** The changes in general forces may result in changes in specific forces. For example, a change in the government (a political force) may lead to a change in tax rates, import-export rates (an economic force)
4. **Dynamic nature:** The external forces keep changing due to constant change in technology, consumer preferences, availability of different types of raw material etc.
5. **Uncertainty:** Constant changes in environment makes it difficult to predict changes in the external environment.
6. **Complexity:** The interrelated and dynamic nature of external forces makes it difficult to prepare one single strategy to handle all the changes.
7. **Relativity:** The impact of changes depends on business to business country to country region to region etc.

Importance of Business Environment:

1. Environment Provides Numerous Opportunities for Business Success It enables the firm to identify opportunities and getting the first mover advantage.
2. Threats and Early Warning Signals Environmental awareness can help managers to identify various threats on time and serve as an early warning signal.
3. It Helps in Tapping Useful Resources Environment is a source of various resources for running a business. Like as finance, machines, raw materials etc.
4. It Helps in Coping with Rapid Changes Knowledge of environmental changes sensitises the management to make new strategy to copy with the emerging problems of changes.
5. It Helps in Assisting in Planning and Policy Formulation Its understanding and analysis can be the basis for deciding the future course of action or training guidelines for decision making.
6. It helps in Improving Performance With continuous scan of business environment, companies can easily improve their performance.

Dimensions in Business Environment:



1. **Economic Environment:** It refers to all those factors and forces that have an economic impact on the business activities. Key economic factors include inflation, money supply, price level, etc. For example, increase in inflation rates result in fall in disposable incomes and as a result the demand for products falls.
2. **Social Environment:** Social environment represents the customs and traditions, values, culture, social trends, beliefs, ethics of society in which business operate. For example,

with greater awareness among consumers about their rights, businesses are more concerned about the quality of goods they sell.

3. **Political Environment:** It includes political stability such as political leadership, political stability, practices of the ruling party, etc. For example, change in government, or unstable government.
4. **Legal Environment:** It includes all the legislations passed, administrative orders issued, court judgements or decisions taken by government or its related offices. For example, all cigarette packets must carry a warning 'smoking is injurious to health'.
5. **Technological Environment:** It consists of forces relating to scientific improvements and innovations, which lead to better production techniques and methods to produce goods. For example, shift from books to e-books, telephones to touch screen mobile phones.
6. After demonetisation, cash is deposited into banks for exchanging with new notes which makes the payment of tax compulsory with penalty rate.
7. Government introduced demonetisation to reduce tax evasion.
8. Demonetisation reduces the cash transactions in the economy which means more savings through the financial system and improving tax payment system.
9. Demonetisation facilitates tax administration, and pave way for a cashless economy

Economic Environment In India:

Since 1991 India has been going on economic reforms. We have now adopted the policy of liberalisation, privatisation and globalisation, We have started modernising the country's industrial system. Unproductive control are being removed private investment, including foreign investment is being encouraged.

1. **Liberalisation:** It means removing unnecessary trade restrictions and making the economy more competitive like as freedom of production, expansion of industries.
2. **Privatisation:** It means removing strict control over private sector and making them free to take necessary decisions. Like as reduction in the number of reserved public sector industries, increasing the share of private sector investment.
3. **Globalisation:** Free interaction among economies of the world in the field of trade, finance, production, technologies and investment is termed as globalisation. Our new economic policy contributed towards globalisation in the following ways.
4. **Privatisation:** It refers to the shifting of the development responsibility from the public sector towards the private sector. Private sector are those where the share of government in the ownership of the enterprise is less than 51 percent.

Impact of Demonetisation:

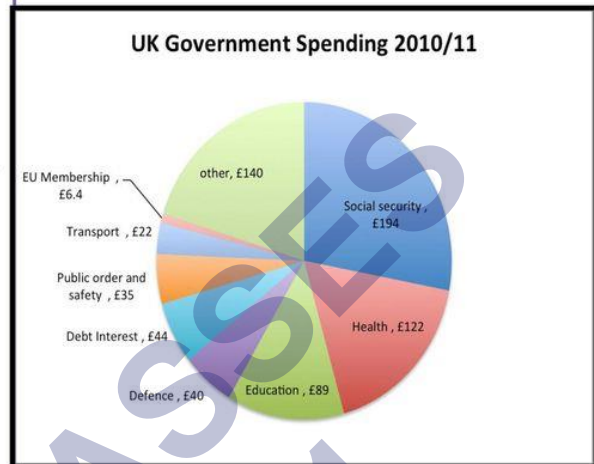
Money/Interest rates	Decrease in transactions of cash. Increase in bank deposits. Financial savings increased.
Private wealth	High demonetised notes were not returned and real estate prices also fell which lead to decrease in private wealth.
Public sector wealth	There was no effect.
Digitalisation	Increase in the digital transactions (like Rupay, AEPS) among new users.
Real estate	Decrease in the prices.
Tax collection	Due to higher disclosure there was rise in tax collection.

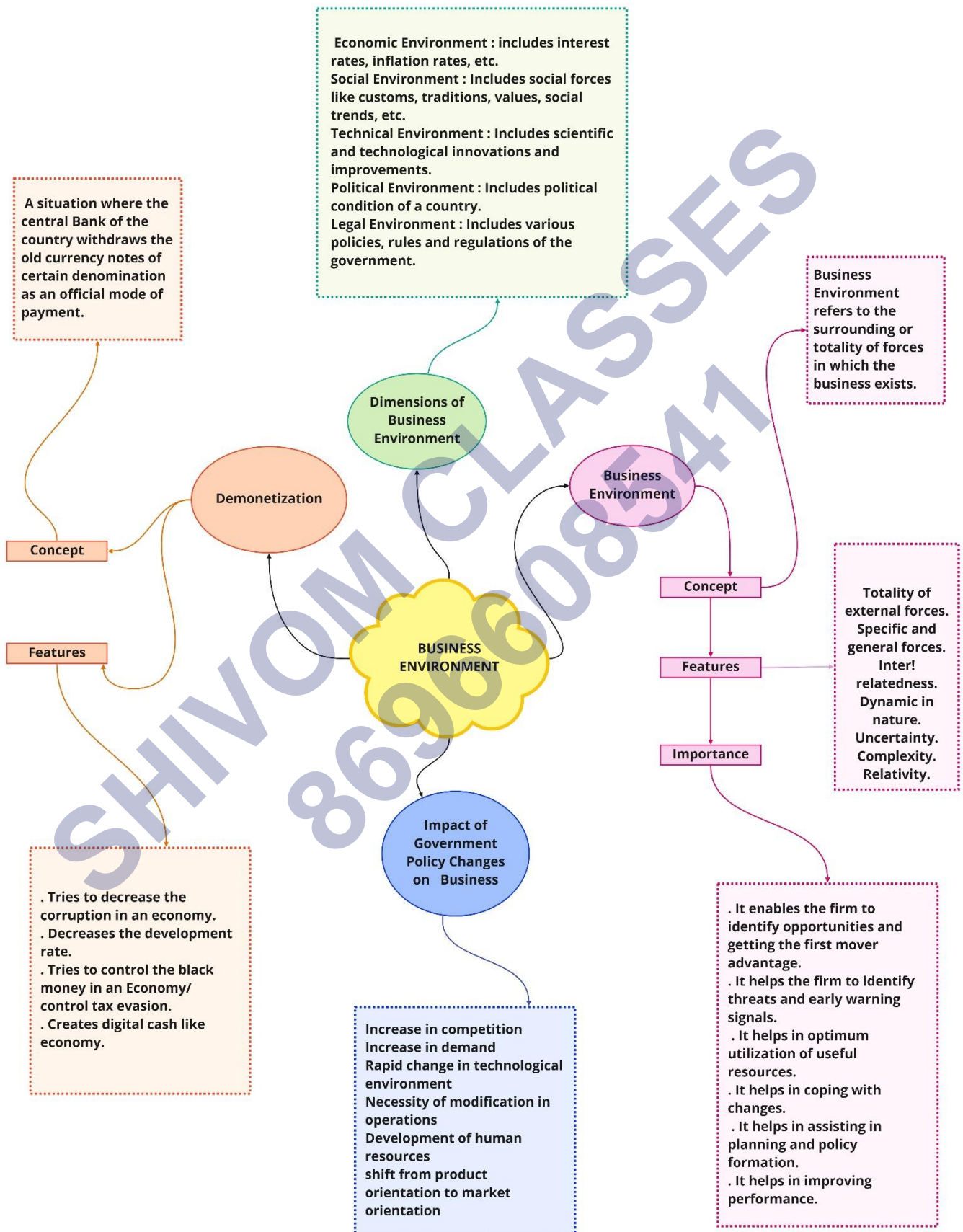
Impact of Government Policy Changes on Business and Industry:

- 1. Increasing Competition:** There is a tough competition between multinationals and there is also competitions between Indian enterprises and foreign enterprises.
- 2. More Demanding Customers:** Customers today become more demanding because they are well-informed.
- 3. World Class Technology:** Changes in government policy regarding business and industry has provided us with world class technology.
- 4. Necessity for Change:** After 1991, the market forces have become turbulent as a result of which the enterprises have to continuously modify their operations.
- 5. Need for Developing Human Resource:** The new market conditions requires people with higher competence and greater commitment.
- 6. Market Orientation:** Today firms are market oriented. They research the market, need and wants of consumers and then they produce good accordingly.
- 7. Loss of Budgetary:** Support to Public Sectors The government's budgetary support for financing the public sector has declined over the years.

Government spending and taxation

- The government can change the way businesses work and influence the economy either by passing laws, or by changing its own spending or taxes. For example:
- Extra **government spending** or lower **taxes** can result in more demand in the economy and lead to higher output and employment.
- Governments can pass **legislation** protecting consumers and workers or restricting where businesses can build new premises.





Important Questions

Multiple Choice questions-

Question 1. Relaxing the restrictions and controls imposed on Business and industry means

- (a) Liberalisation
- (b) Privatisation
- (c) Globalisation
- (d) None of the above

Question 2. Which of the following best indicates the importance of the business environment?

- (a) Coping with rapid changes
- (b) Identification
- (c) Improvement in performance
- (d) All of the above

Question 3. What will be the effect of an increase in tax by the government?

- (a) Increase in cost of production
- (b) Creates fear in the minds of investors
- (c) Increase in profit margin
- (d) None of the above

Question 4. What creates fear in the minds of investors to invest in long term projects?

- (a) Privatisation
- (b) Political Uncertainty
- (c) Liberalisation
- (d) None of the above

Question 5. Which of the following creates fear in the minds of investors?

- (a) Political uncertainty
- (b) New innovations
- (c) None of these
- (d) Technological improvements

Question 6. Celebration of Diwali is the example of:

- (a) Technological Environment
- (b) Social Environment
- (c) Political Environment
- (d) Legal Environment

Question 7. Booking of Railway tickets through internet from home or office is an example of

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- (a) Political Environment
 - (b) Technological Environment
 - (c) Economic Environment

(d) None of the above

Question 8. Export promotion is concerned with _____

- (a) Privatisation
- (b) Globalisation
- (c) Liberalisation
- (d) None of the above

Question 9. Changes in fashions and tastes of consumers will _____

- (a) Shift the market demand from an existing product to new ones
- (b) Increase the cost of production
- (c) Increase the profit
- (d) Increase the Sale

Question 10. Increased competition in the market will _____

- (a) Increase the tax
- (b) Increase the profit
- (c) Increase the cost of production
- (d) Reduce the profit margin

Question 11. Giving freedom to Indian business and industries from all unnecessary government controls and restrictions is an example of _____

- (a) Privatisation
- (b) Globalisation
- (c) Liberalisation
- (d) None of the above

Question 12. Technological improvements and innovations result in _____

- (a) Increase in tax
- (b) Render existing products obsolete
- (c) Reduction in profit margins
- (d) None of the above

Question 13. Which of the following does not explain the impact of Government policy changes on business and industry?

- (a) More demanding customers
- (b) Change in agricultural prices
- (c) Increasing competition
- (d) Market orientation

Question 14. Globalisation aims at _____

- (a) Export Promotion
- (b) Foreign exchange reforms
- (c) Import liberalization
- (d) All of the above

Question 15. When a company taken over another one and clearly becomes the new owner, the action is called

- (a) Merger
- (b) Acquisition
- (c) Strategic Alliance
- (d) None of the above

Very Short-

1. What is Business Environment?
2. How have customers benefited by increased competition after liberalization and globalization?
3. How can the firms cope up with changing technological environment?
4. What do you mean by Globalization?
5. Which policy of Indian Government has moved India towards globalization?
6. What do you mean by disinvestment?
7. Give one measure taken by Indian Government to introduce liberalization.
8. What do you mean by first mover advantage?
9. What are Values?
10. Which of the sector was given importance after independence?

Short Questions-

1. Define Business Environment. State two important concerns of business environment.
2. Explain the specific and general forces of business environment ?
3. Enumerate the benefits of understanding business environment.
4. What are the main dimensions of business environment? What does environment consist of?
5. Explain the role of political environment in shaping the business.?
6. Explain the concept of technological environment.
7. What do you understand by legal environment? Give two examples which protect consumers' interests.
8. List the various changes initiated by the Government of India since 1991.
9. List some important factors that influence the working of a business enterprises?
10. Give your views on 'Economic Environment in India.

Long Questions-

1. What do you mean by business environment? Explain the key components of business environment.

2. What do you understand by economic environment? List the main aspects of economic environment.
3. Social environment of business is important for a business enterprise".

Explain ?

4. Enumerate negative impacts of liberalization and globalization.
5. Enumerate any ten Positive impacts of liberalization and globalization.
6. Explain any five negative impacts of liberalization and globalization.

Case Study Based Question-

1. Metlapp Networks and Technologies Ltd. is a leader in technology innovation in the United States, creating products and solutions for connecting the world. It has,, a large research and development team which invented the first smart watch, named as W-7. The watch besides showing the time, also monitors few health parameters like heartbeat, blood pressure etc.

While in search of markets abroad, the company found that in India, the reform process was underway with the aim of accelerating the pace of economic growth. The company decided to take advantage of simplified export procedure and removal of quantitative as well as tariff restrictions in India. It set up its office in Jamnagar with a view to capture the Indian market. In a short span of time, the company emerged as a market leader. Success of the company attracted many other players to enter the market. Competition resulted in reduction in prices, thereby benefiting the customers.

- a. In the above paragraph, two major concepts related to government policy have been discussed. Identify and explain these concepts.
 - b. Also, explain briefly any three impacts of these concepts on Indian business and industry.
2. Naman and Govind after finishing their graduation under vocational stream decided to start their own travel agency which will book Rail Tickets and Air Tickets on commission basis. They also thought of providing tickets within ten minutes through the use of internet. They discussed the idea with their Professor Mr. Mehta who liked the idea and suggested them to first analyse the business environment which consists of investors', competitors and other forces like social, political etc. that may affect their business directly or indirectly. He further told them about the technological improvements and shifts in consumer preferences that were taking place and hence they should be aware of the environmental trends and changes which may hinder their business performance. He emphasised on making plans keeping in mind the threat posed by the competitors, so that they can deal with the situation effectively. This alignment of business operations with the business environment will result in better performance.
 - a. Identify and state the component of business environment highlighted in the above Para.

- b. State any two features of business environment as discussed by Professor Mehta with Naman and Govind.
- c. Also state two points of importance of business environment as stated by Professor Mehta in the above situation.

Assertion Reason Type Question-

1. In these questions, a statement of assertion followed by a statement of reason is given. Choose the correct answer out of the following choices.
 - a. Assertion and reason both are correct statements and reason is correct explanation for assertion.
 - b. Assertion and reason both are correct statements but reason is not correct explanation for assertion.
 - c. Assertion is correct statement but reason is wrong statement.
 - d. Assertion is wrong statement but reason is correct statement.

Assertion: Changes and fashion and tastes of consumer may shift in demand in the market from existing products to new ones.

Reason: Business environment is dynamic hence it keeps on changing in consumer preference.

2. In these questions, a statement of assertion followed by a statement of reason is given. Choose the correct answer out of the following choices.
 - a. Assertion and reason both are correct statements and reason is correct explanation for assertion.
 - b. Assertion and reason both are correct statements but reason is not correct explanation for assertion.
 - c. Assertion is correct statement but reason is wrong statement.
 - d. Assertion is wrong statement but reason is correct statement.

Assertion: The business environment helps in understanding the threats which are likely to happen in the future.

Reason: Environmental awareness can help managers to identify various threats on time and serve as an early warning signal.

MCQ Answers-

1. Answer: (a) Liberalisation
2. Answer: (d) All of the above
3. Answer: (a) Increase in cost of production
4. Answer: (b) Political Uncertainty
5. Answer: (a) Political uncertainty

6. Answer: (b) Social Environment
7. Answer: (b) Technological Environment
8. Answer: (b) Globalisation
9. Answer: (a) Shift the market demand from an existing product to new ones
10. Answer: (d) Reduce the profit margin
11. Answer: (c) Liberalisation
12. Answer: (b) Render existing products obsolete
13. Answer: (b) Change in agricultural prices
14. Answer: (d) All of the above
15. Answer: (b) Acquisition

Very Short Answers-

1. Ans. Forces affecting the performance of an organization but outside its control are called as Business Environment.
2. Ans. While purchasing they get a better quality and wider choice of goods and services.
3. Ans. They have to develop new ways.
4. Ans. When the various economies of the world integrate, it is known as Globalization.
5. Ans. The Industrial Policy of 1991.
6. Ans. When the private sector takes over public sector, it is called disinvestment.
7. Ans. Abolishing licensing requirements.
8. Ans. Early identification of opportunities.
9. Ans. Concepts held by a society in high esteem are values.
10. Ans. Public Sector.

Short Answers-

1. Ans. The sum total of all external factors which are outside the control of business enterprises is termed as Business Environment. Factors may be social, political, economic etc.
2. Ans. Business environment comprises of both specific and general forces. Specific forces refer to those forces that are having direct effect on the day to day working of the business viz. customers, competitors, investors etc. General forces refer to social, political, legal and other forces which are having an indirect effect on the operations of a business.
3. Ans. The benefits of understanding business environment are:
 - (i) Enabling the identification of opportunities and getting the first mover advantage.
 - (ii) Helping in the identification of threats and early
 - (iii) Tapping useful resources.

- (iv) Coping with the rapid changes.
- (v) Assisting in planning and policy.
- (vi) Improvement in performance.

4. Ans. The main dimensions of business environment are

- (i) Economic, (ii) Social, (iii) Technological, (iv) Political, (v) Legal Economic

environment consists of the factors having economic dimensions such as fiscal policy, monetary policy, industrial policy etc.

5. Ans. Business functions within the framework of political environment. Generally, government's policies change with the change of guard in power. Business is required to understand and follow such changes and also respect the orders that judiciary gives from time to time.

For example, after globalization, Government of India allowed many companies to enter the Indian market for giving boost to the different industries like food processing industry etc. That paved the way for entry of multinationals in India on a large scale.

6. Ans. It includes new approaches, new procedures, and new equipment's to transform inputs into outputs. It facilitates an organization's efficiency and effectiveness so that it can try to remain at par with the best in the world. Technological changes provide opportunities for some enterprises and become threats for some others.

For example, digital watches killed the business prospects of traditional watches; TV has adversely affected radio & cinema industry; mobile phones have taken over the market from landline phones.

7. Ans. Legal environment consists of rules and regulations, framed by the Parliament, under which business must operate. To exist and grow, business is required to follow all the rules and regulations that constitute this environment.

Two examples protecting consumers' interests:

- (i) Advertisement of alcoholic beverages is prohibited.
- (ii) Packets of cigarettes should mention the statutory warning 'Cigarette smoking is Injurious to health'.

8. Ans. Various changes initiated by the Government of India since 1991 are as follows:

- (i) New industrial policy
- (ii) New trade policy
- (iii) Fiscal reforms
- (iv) Monetary policy
- (v) Capital market reforms
- (vi) Phasing out of Subsidies and Price controls

9. Ans. Following are the important factors that influence the working of a business

enterprise:- (i) Changes in economic policies. (ii) Political uncertainty in the country. (iii) Increase in the rate of competition. (iv) Changes in fashion.

10. Answer: 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. These are:

1. Stage of economic development of the country.
2. The economic structure in the form of a mixed economy.
3. Economic policies of Government including industrial monetary and fiscal policy.
4. Economic planning including five-year plans etc.
5. Infrastructural factors such as financial institutions.

Long Answers-

1. Ans. Business environment is the sum total of all external factors that influence the functioning of a business enterprise. The components of general environment are:

(i) Economic environment:

Economic environment consists of factors having economic dimensions such as fiscal policy, monetary policy, industrial policy etc.

Impact: Banking sector reforms have led to attractive deposit avenues and easier credit policy. Likewise reforms in leasing & financial institutions are also catalyzing company's economic growth.

(ii) Social environment: It discriminates characteristics of the society in which an enterprise exists. It consists of literary rates, educational levels, customs and demographic distribution etc.

Impact : Equal pay for equal work for both male and female workers, reservation of jobs for minorities etc.

(iii) Political environment

It consists of the political forces responsible for the management of public affairs and their influence on business.

Impact : Government allowed Pepsi to enter Indian market again for giving boost to the food processing industry.

(iv) Technological environment

It comprises of the various processes, techniques, approaches etc. by which an organization transforms inputs into output.

Impact : Digital watches have pushed out traditional watches.

(v) Legal Environment : It characterises various governmental rules,

regulations and legislations etc. that all members of business community must follow.

Impact : Removal of control on foreign exchange and liberalization of foreign direct investments.

2. Ans. Economic environment consists of factors like inflation rates, interest rates, consumer's incomes, economic policies, market conditions etc. which affect the performance of a business firm.

Following are the main aspects of economic environment:

- (i) The role of public and private sector in the existing structure of the economy.
- (ii) The rate of increase in GNP and per capita income both at current and constant prices.
- (iii) Quantum of exports and imports of different products.
- (iv) Increase in transportation and communication facilities.
- (v) Trends in agricultural and industrial productions.
- (vi) Amount of savings and investments.

3. Ans. A business is a part of the society in which it operates. The buying and consumption habits of the people, their languages, customs, preferences, tastes etc. are the factors that influence the business. Businessmen should be alert enough to visualize the factors that directly or indirectly affect their organization. Cooperation between business and society will see business boom and will help growth of professional managers. The failure of any business organization in adapting to changes in the social environment will lead to dissatisfaction amongst its customers and rejection of its products. This shift of demand can even endanger the very survival of a business. For example, equal pay for male and female workers, demand for reservation in jobs for minorities and women etc.

4. Ans. The negative impacts of liberalization and globalization are as follows;

- (i) Threats from Multinational Companies (MNCs).
- (ii) Corporate vulnerability.
- (iii) Increased competition.
- (iv) Fast changing technology.
- (v) High obsolescence of material resources.
- (vi) High labor turnover.
- (vii) Threat to indigenous culture and values.

5. Ans. The positive impacts of liberalization and globalization are as follow:

- (i) Opportunities for new entrepreneurs.
- (ii) Latest technology becoming available.
- (iii) Opening up of foreign markets.
- (iv) Easy imports of capital goods.
- (v) Direct investment by Indian companies abroad.

- (vi) Changed attitude of labor unions,
- (viii) Easy inflow of foreign capital.
- (ix) Freedom to expand and diversify.
- (x) Restructuring of industries.
- (x) Widening of product choices for consumers.

6. Ans. Following are the negative effects of liberalization and globalization.

(i) Threats from multinational companies (MNCs)

With the arrival of multinationals it is becoming difficult for small and medium business units to even survive. The massive entry and consolidation to multinationals in the Indian markets is a challenge that has already forced some business enterprises to take the exit route.

(ii) Destabilization of protected environment

With easier entry of multi-national companies, Indian business environment is fast losing its protective shield. The new entrepreneurial freedom is creating problems for the existing players. Even manufacturers of Maruti car could not retain their market share and had to remodel their products and announce heavily price reductions from time to time.

(iii) Decline in public sector

Public sector is losing markets and their capacity utilization has declined, hampering thereby pace of country's technological and economic growth.

(iv) Sellers' market turned into buyers' market

With the entry of foreign goods and services, shortage of goods, which is boon for the sellers, has now turned into surplus. Resultantly, sales/margin to any sellers have come down substantially. Buyers are now free to buy any product of their choice at a price they can afford.

(v) Fall in the value of rupee

Indian rupee has been devaluing against DOLLAR, EURO and many other foreign currencies. This phenomenon has forced even some established exporters to encase their stake partly/fully.

Case Study Answer-

1. Answer:

- a. Liberalisation and globalisation are the two major concepts related to government policy that have been discussed.
 - Liberalisation: These economic reforms signalled the end of the licence-permit-quota raj and were aimed at liberalising the Indian business and industry from all unnecessary controls and restrictions.
 - Globalisation: Globalisation means the integration of the various economies of

the world leading towards the emergence of a cohesive global economy.

- b. The three impacts of reforms on Indian business and industry are outlined below:
- Increasing competition: The Indian firms are facing lot of competition due to changes in the rules of industrial licensing and entry of foreign firms. This change is more apparent in the sectors which were earlier reserved for private sector only like banking, insurance, telecommunications, etc.
 - More demanding customers: With the easy availability of wider choice in purchasing better quality of goods and services due to high competition consumers have become more aware and demanding. The growing expectations of the consumers has increased the pressure on the business firms.
 - Rapidly changing technological environment: With the entry of new firms which are far more superior in terms of technology the small firms are facing a lot of challenges. Moreover, the firms are constantly involved in innovating new products and upgrading present products with the help of better technologies in order to satisfy the customers demands.

2. Answer:

- a. Technological Environment is the component of business environment highlighted in the above Para. 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 a business.
- b. The two features of business environment as discussed by Professor Mehta with Naman and Govind are as follows:
- Dynamic nature: It is dynamic in nature and keeps on changing due to technological upgradations, shifts in consumer preferences or increase in competition in the market.
 - Inter-relatedness: All the elements of business environment are closely interrelated. Therefore, any change in one element may necessitate corresponding changes in the other elements as well.
- c. The two points of importance of business environment as stated by Professor Mehta in the above situation are described below:
- It enables the firm to identify opportunities and getting the first mover advantage: The dynamic business environment provides numerous opportunities for a business to evolve as per the changing needs. Therefore, early identification of the forthcoming opportunities helps an enterprise to be the first to exploit them instead of losing them to the competitors.
 - It helps the firm to identify threats and early warning signals: Sometimes the changes in the external environment may pose as a threat and hinder a firm's performance. An awareness about the business environment helps the managers to identify such threats on time and take necessary decisions and action.

Assertion Reason Answer-

1. a. Assertion and reason both are correct statements and reason is correct explanation for assertion.

Explanation: Business environment is dynamic, therefore it keeps on changing weather in terms of technological improvements, shifts in consumer preference or entry of new competition in the market.

2. a. Assertion and reason both are correct statements and reason is correct explanation for assertion.

Explanation: 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.

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