

Ninth Edition

THE BUSINESS ENVIRONMENT

A Global Perspective

Ed Thompson
Ian Worthington
Chris Britton



The Business Environment



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The Business Environment: A Global Perspective

Ninth edition

Ed Thompson, Ian Worthington and Chris Britton

De Montfort University, Leicester



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For Lindsey, Tom and Georgina, for Rachael, Philip,
Nick and Megan, and for Ramanjeet, Darshan, Sandra
and David – with our love



Brief contents

Contributors	xix
Preface to the Ninth Edition	xx
Publisher's Acknowledgements	xxii
Guided tour	xxiv
Part One INTRODUCTION	1
1 Business organisations: the external environment	3
2 Business organisations: the internal environment	17
3 The global context of business	39
4 De-globalising factors: sovereignty, conflicts and political priorities	55
Part Two CONTEXTS	69
5 The political environment (P)	71
6 The macroeconomic environment (E)	103
7 The demographic, social and cultural context of business (S)	141
8 The resource context: people, technology and natural resources (T)	163
9 The legal environment (L)	189
10 The ethical and ecological environment (E)	215
Part Three FIRMS	233
11 Legal structures	235
12 Size structure of firms	261
13 Industrial structure	285
14 Government and business	307
Part Four MARKETS	325
15 The market system	327
16 Market structure	351
17 International markets and trade	373
18 Pandemics and Covid-19	399
19 Governments and markets	419
Part Five CONCLUSION	441
20 Strategy and the changing environment	443
Glossary	469
Index	489



Contents

Contributors	xix
Preface to the Ninth Edition	xx
Publisher's Acknowledgements	xxii
Guided tour	xxiv

Part One INTRODUCTION

1 Business organisations: the external environment	3
Learning outcomes and key terms	3
Introduction	4
The business organisation and its environment	4
The general or contextual environment	7
<i>Mini case: The impact of regional economic conditions</i>	8
The immediate or operational environment	9
Analysing the business environment	10
<i>Mini case: Fresh but not so easy</i>	10
Central themes	12
Synopsis	14
Summary of key points	14
<i>Case study: Facing the unexpected</i>	14
Review and discussion questions	15
Assignments	16
Further reading	16
2 Business organisations: the internal environment	17
Learning outcomes and key terms	17
Introduction	18
The concept of the organisation: an initial comment	18
Understanding the nature of organisations: theories of organisation and management	19
Other theoretical approaches	23
Organisational structures	23
<i>Mini case: 'Into the Dragon's Den'</i>	24
<i>Mini case: Mergers and competition</i>	27
The virtual organisation	29
Structural change	30
Aspects of functional management	30
Synopsis	35
Summary of key points	35

Case study: Reshuffle at Microsoft	36
Case study: Thomas Cook expansion	37
Review and discussion questions	37
Assignments	38
Further reading	38
3 The global context of business	39
Learning outcomes and key terms	39
Introduction	40
Globalisation versus internationalisation	40
The role of multinational enterprises	43
Mini case: Transfer pricing	44
Globalisation and business	46
Mini case: Currency crisis in emerging markets	47
Globalisation and the small and medium-sized firm	48
Synopsis	49
Summary of key points	49
Case study: Global financial markets – too big to fail	50
Case study: FDI flows	51
Review and discussion questions	52
Assignments	53
Further reading	53
4 De-globalising factors: sovereignty, conflicts and political priorities	55
Learning outcomes and key terms	55
Introduction	56
What is globalisation?	57
Bretton Woods System (or the ‘New World Order’)	58
The 1970s to the present	59
Isolationism	59
International conflicts	62
Sanctions	63
Case study: Local solutions to global problems	65
Environmentalism	65
Summary of key points	66
Case study: Weetabix – local solutions to global problems	67
Assignments	68
Further reading	68

Part Two CONTEXTS

5 The political environment (P)	71
Learning outcomes and key terms	71
Introduction	72
Political systems	74

Government in democratic states	76
<i>Mini case: Brought to book</i>	79
The three branches or functions of government	82
<i>Mini case: The power of the purse</i>	83
Checks and balances in democracies	87
A model of the policy process	87
Synopsis	89
Summary of key points	89
Appendix 5.1: A democratic political system in action: UK national government	90
The executive branch of government	92
The judicial branch of government	97
Appendix 5.2: Subnational government: UK local authorities	97
Appendix 5.3: Other levels of government	99
<i>Case study: The business of lobbying</i>	100
<i>Case study: Political campaign funding</i>	101
Review and discussion questions	102
Assignments	102
Further reading	102
6 The macroeconomic environment (E)	103
Learning outcomes and key terms	103
Introduction	104
Economic systems	105
Economies in transition	109
Politico-economic synthesis	110
The macroeconomy	111
Government and the macroeconomy: objectives	117
<i>Mini case: Digging in for the long term</i>	123
Government and the macroeconomy: policies	123
The role of financial institutions	128
<i>Mini case: A new kid on the block: the rise of the credit rating agency</i>	130
International economic institutions and organisations	131
Synopsis	134
Summary of key points	135
<i>Case study: Austerity</i>	136
<i>Case study: Quantitative easing (QE)</i>	136
Review and discussion questions	138
Assignments	138
Further reading	139
7 The demographic, social and cultural context of business (S)	141
Learning outcomes and key terms	141
Introduction	142

The demographic environment of business	142
The social context	147
<i>Mini case: A new class structure?</i>	148
Lifestyles	151
The cultural environment	153
<i>Mini case: National cultures</i>	155
Application: market segmentation	156
Synopsis	158
Summary of key points	158
<i>Case study: An invitation to ‘tweet’</i>	159
<i>Case study: Supply and demands – a changing workforce</i>	160
Review and discussion questions	160
Assignments	161
Further reading	161
8 The resource context: people, technology and natural resources (T)	163
Learning outcomes and key terms	163
Introduction	164
People	164
<i>Mini case: Zero-hours contracts</i>	166
Technology	173
Technological change	173
<i>Mini case: The robots are coming</i>	175
Natural resources	180
Synopsis	183
Summary of key points	183
<i>Case study: Agricultural work and Brexit</i>	184
<i>Case study: Fracking</i>	184
Review and discussion questions	186
Assignments	186
Further reading	187
9 The legal environment (L)	189
<i>Martin Morgan-Taylor</i>	
Learning outcomes and key terms	189
Introduction	190
Classification of law	190
Public and private law	190
<i>Mini case: Verity and Spindler v Lloyds Bank (1995)</i>	191
The legal system: the courts	194
<i>Mini case: Jean-Marc Bosman – a case of foul play?</i>	196
Business organisations and the law	197
Contract law: the essentials	197
Agency	201
Law and the consumer	202

Codes of practice	209
Synopsis	210
Summary of key points	210
<i>Case study</i> : The sale of goods on the Internet	211
Review and discussion questions	213
Assignments	213
Further reading	214
10 The ethical and ecological environment (E)	215
Learning outcomes and key terms	215
Introduction	216
Ethics and business	217
<i>Mini case</i> : Illegal or unethical?	218
Corporate social responsibility	219
The 'environment' as a business issue: the emergence of corporate environmentalism	220
Drivers of 'green' business	221
Why and how firms become more environmentally responsible	225
<i>Mini case</i> : Going round in circles: Desso Carpets	226
Another perspective: the 'outside-in' view	227
Summary of key points	228
<i>Case study</i> : Doing well by doing good	228
Review and discussion questions	229
Assignments	230
Further reading	230

Part Three FIRMS

11 Legal structures	235
Learning outcomes and key terms	235
Introduction	236
Private sector organisations in the UK	236
<i>Mini case</i> : Companies under pressure	242
Social enterprises	245
Public sector business organisations in the UK	246
Legal structure: some implications	249
Franchising, licensing and joint ventures	254
<i>Mini case</i> : Cross-national joint ventures	256
Synopsis	257
Summary of key points	258
<i>Case study</i> : Uber	258
Review and discussion questions	259
Assignments	259
Further reading	260

12 Size structure of firms	261
Learning outcomes and key terms	261
Introduction	262
The size structure of UK industry	262
Organisational growth	263
Methods of growth	264
<i>Mini case</i> : The story of a failed merger	267
Finance for growth	268
Small firms	273
<i>Mini case</i> : ‘Olderpreneurs’ and small firms	274
Multinationals	281
Synopsis	282
Summary of key points	282
<i>Case study</i> : The Scottish National Investment Bank	283
Review and discussion questions	283
Assignments	284
Further reading	284
13 Industrial structure	285
Learning outcomes and key terms	285
Introduction	286
The structure of industry	286
<i>Mini case</i> : The end of manufacturing?	290
<i>Mini case</i> : The life cycle model	295
Deindustrialisation	297
Synopsis	300
Summary of key points	301
Appendix 13.1: The Standard Industrial Classification (SIC), 2007	301
<i>Case study</i> : The rise of the public service companies	302
Review and discussion questions	304
Assignments	305
Further reading	305
14 Government and business	307
Learning outcomes and key terms	307
Introduction	308
Government and business: an overview	308
Selected urban policy instruments	309
Developments in urban policy: 1997–2010	312
Urban and industrial policy developments in the UK since 2010	313
Local government and business in the UK	315
Business as an influence on government	320
<i>Mini case</i> : A taxing issue	321
Synopsis	322
Summary of key points	322

<i>Case study</i> : Public sector procurement – the Royal Navy	323
Review and discussion questions	324
Assignments	324
Further reading	324

Part Four MARKETS

15 The market system	327
Learning outcomes and key terms	327
Introduction	328
The market mechanism	328
Demand	328
Supply	331
Shifts in demand and supply	335
<i>Mini case</i> : The effect of a factory fire on the market for microchips	336
Price controls	337
<i>Mini case</i> : The price of toilet rolls in Venezuela	339
Elasticity of demand	340
Cross-price elasticity of demand	343
Elasticity of supply	343
The importance of the market to business	344
Synopsis	345
Summary of key points	345
<i>Case study</i> : The housing market in the UK	346
Review and discussion questions	348
Assignments	348
Further reading	349
16 Market structure	351
Learning outcomes and key terms	351
Introduction	352
Market structures – in theory and practice	353
Porter's five-forces model	360
<i>Mini case</i> : Open Skies and contestability	363
<i>Mini case</i> : Blizzard, Activision and Microsoft	365
Measuring the degree of actual competition in the market	366
Synopsis	368
Summary of key points	368
<i>Case study</i> : A Porter's five-forces analysis of the cigarette industry in the UK	369
Review and discussion questions	371
Assignments	372
Further reading	372

17 International markets and trade	373
Learning outcomes and key terms	373
Introduction	374
International trade – why it takes place	374
Restrictions to international trade	375
<i>Mini case: The cotton dispute</i>	376
The establishment and growth of the European Union	377
‘Brexit’ and Euroscepticism	379
The balance of payments	380
The history of the balance of payments in the UK	383
<i>Mini case: The current account of the balance of payments</i>	385
Exchange rates	388
Exchange rates and business	394
Synopsis	394
Summary of key points	394
<i>Case study: Post-Brexit trade</i>	395
Review and discussion questions	396
Assignments	397
Further reading	397
18 Pandemics and Covid-19	399
Learning outcomes and key terms	399
Introduction	400
Pandemics	400
Pandemics in history	403
Global spread	406
Prevention	407
<i>Case study: Covid-19</i>	408
<i>Mini case: FFP2/N95 respirators and surgical masks</i>	408
<i>Mini case: Peloton bikes</i>	409
UK government support measures	411
The future	416
Returning to normal	417
Synopsis	417
Assignments	418
Further reading	418
19 Governments and markets	419
Learning outcomes and key terms	419
Introduction	420
Privatisation policy in the UK	420
<i>Mini case: Government to the rescue</i>	426
Competition policy	429
<i>Mini case: Accusations of price fixing</i>	431
Government and the labour market	432
Synopsis	436
Summary of key points	436

<i>Case study: Who leads who?</i>	437
<i>Case study: 'What a fine mess you've got me into'</i>	438
Review and discussion questions	439
Assignments	439
Further reading	439

Part Five CONCLUSION

20 Strategy and the changing environment	443
<i>David Orton</i>	
Learning outcomes and key terms	443
Introduction	444
The need to monitor environmental change	445
Analysing the business environment: broad approaches	446
<i>Mini case: Multinational inward investment: a PESTLE analysis</i>	447
Techniques	450
Limitations to environmental analysis	455
Sources of information	455
Synopsis	463
Summary of key points	463
<i>Case study: Scenario planning at Shell</i>	464
Review and discussion questions	466
Assignments	466
Further reading	467
Glossary	469
Index	489

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Preface to the Ninth Edition

Why study the business environment?

The business environment is our environment, it is the world we live in and all aspects of the business environment should be viewed in terms of people. Business ethics is about fairness in how a business operates; a business environmental policy is about how we pollute or preserve our own world; employment and unemployment are about people's ability to house and feed themselves. This is a book about all of us and how we interface with the world and each other, because businesses are just organisations of people and material things.

In reading about the business environment you are reading about your world. You are reading about why the prices of the things you buy might go up or down, or why at any given time it might be harder or easier for you to get a job. By understanding the things in this book that make up your world you will better understand how the world works, what changes mean and the implications they might have on your organisations (whether they are organisations that we work for, or the organisations that we have at home). In my own life, understanding the business environment has helped me make decisions about when and where and how to buy a home, and what and what not to invest in. Understanding the world allows us to make informed decisions.

Despite the global pandemic, Brexit, the Russian invasion of Ukraine and increased international trade tensions, the world keeps on turning. People continue to learn at home and at universities – and people continue to graduate and find jobs. It will be sensible for somebody going for an interview to carry out some research on the potential employer and understand how they might be affected by their business environment.

The first aim of this book is to set out the way things are in the world today. It will do this by breaking down everything outside of a business (and cover a little bit inside as well) into chapters organised in a logical way. In effect, what we mean by external and internal environments in a global context in which business operates today. The second part will cover aspects of the business environment as you might find them in a PESTLE analysis (Political, Economic, Social, Technological, Legal, Ethical/Ecological). The third part will cover firms and industries, as well as how government regulates business. The fourth part will consider the importance of markets as a concept, nationally and internationally. Finally, we will consider how the business environment feeds into strategy making for organisations.

The second aim of the book is to offer you examples and opportunities to apply what you have learned. The biggest change in this edition of the book has been the inclusion of specific chapters on the biggest contemporary events – namely the global Covid-19 pandemic and the retreat of some aspects of globalisation, including Brexit. These new chapters apply some of the content which are introduced elsewhere to give an all-round perspective on how factors influence one another, and convey the complexity of the business environment.

The context

With this edition, like the last, I feel I have to introduce some caveats at this point. A 600-page textbook takes a while to update. As I write this (in early 2022) the terms of Brexit arrangements are finalised, but the implications are still being worked out – particularly at the Irish/Northern Irish border. The tide appears to be turning with respect to Covid-19, with several viable vaccines, countries making progress with their distribution, and plans for how the developing world will be supported to ensure global protection. However, things change quickly. While I will address Brexit and Covid-19, the concepts set out here can be applied to many different contexts; the specific situations will change over the next two to five years but the concepts will persist. Further afield, when I started the last edition Russia was considered a friendly nation to Europe; when I started this edition things were a bit more icy between the two nations. Now things are very different and Ukraine has been invaded – with things in Ukraine looking increasingly like a proxy war. . . at any rate, the most significant conflict in Europe for 20 or more years.

The second caveat is with respect to data. I have updated data wherever possible – but in some circumstances there are simply no more updates. Sometimes data are reported in a different way, so continuity could not be maintained if the datasets were any more up to date, and in a few cases data had been collected by agencies which have changed or been disbanded. As a result, some of the datasets are not as up to date as I would have preferred, but they are sufficient to illustrate the points made in the book.

My authorship

This book is now in its ninth edition. Ian Worthington approached me to author this title in a more stable world (2015), a time when pandemic flu was hypothetical and before Brexit; a time when writing a book on the business environment seemed like a less troublesome undertaking!

I have quite a broad background in terms of my experience with the business environment, having worked for large and small private and public sector organisations. My first degree in business studies equipped me with most of my foundational business environment knowledge. Subsequently, I gained a master's degree in project management, and a doctorate in organisational behaviour. In most of my organisational work I have applied an actor–network theory perspective to how the world works. Actor–network theory considers all things related, nothing existing in isolation. This has proven a logical approach writing this book too; the environment is a world of many connections, some obvious and others less so. I hope through reading this book that you will come to understand the world in a similar way.

Thanks on behalf of Ian, Chris and myself to a dedicated team from Pearson for their work on this edition, particularly Archana Makhija, Supervising Producer for UK and Canada, for her support and encouragement through the development of this edition. And on behalf of myself, a big thanks to Ian and Chris, who handed over the updating of the title in the 8th edition. This remains their creation, but as the person responsible for updates I must insist that errors are *my* own.

Finally, take it from someone with a British PhD in Organisational Behavior: organisation is spelled with a Z in *English* English (it's in the *OED*). However, to appease my publishers, it will appear as *organisation* hereafter.

Ed Thompson



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Guided tour

Learning outcomes highlight core coverage in terms of expected learning outcomes after completing each chapter, to help students focus their learning and evaluate their progress.

Learning outcomes

Having read this chapter you should be able to:

- indicate the basic features of business activity
- portray the business organisation as a system interacting with its environment
- demonstrate the range and complexity of the external influences on business activity
- identify the central themes inherent in the study of the business environment

Key terms are drawn out at the start of every chapter and are emboldened the first time they appear in the text to enable students to locate information quickly. A full Glossary appears at the end of the book.

Key terms

Bureaucracy	Human relations approach	Project team
Classical theories of organisation	Human resource management	Public sector
Contingency approach	Management	Re-engineering
Divisional structure	Marketing	Scientific management
Downsizing	Marketing concept	Sub-systems
Formal structures	Marketing mix	Systems approach
Functional organisation	Matrix structure	Theory X and Theory Y
Functional specialisation	Organisation chart	Theory Z
Hierarchy of needs	Private sector	Virtual organisation
Holding company	Profit centre	Voluntary (or third) sector

Lecturer resources tailored to support the use of this textbook in teaching is available at go.pearson.com/uk/he/resources.

Case studies of varying complexity relate the theory represented in the chapter to real-life situations in a range of diverse organisations.

case study

The sale of goods on the Internet

The sale of consumer goods on the Internet (particularly those between European member states) raises a number of legal issues. And these issues are now complicated by the fact that the UK has left Europe, but not stopped trading with EU member states. First, there is the issue of trust, without which the consumer will not buy; they will need assurance that the seller is genuine, and that they will get the goods that they have ordered. Second, there is the issue of consumer rights with respect to the goods in question: what rights exist and do they vary across Europe? Last, the issue of enforcement: what happens should anything go wrong?

cancellation available under Article 9, where the buyer has a right to cancel the contract for 14 days starting on the day the consumer receives the goods or services (this was seven days under the Distance Selling Directive). This 'cooling-off' period is intended to place the consumer in the position as if they had seen the goods in store. Failure to inform the consumer of this right automatically extends the period to a year and 14 days. Whilst the seller can place the cost of returning goods on the buyer, the seller must refund the standard rate outgoing postage. The seller is not entitled to deduct any costs as a restocking fee. All of this places a considerable

Summary of key points provides the student with a useful revision aid.

Summary of key points

- The legal rules within which businesses exist and operate are an important part of the external environment of business organisations.
- Laws affecting businesses derive from a variety of sources, including custom, the decisions of the courts and legislation.
- Laws are sometimes made at international and supranational level (including Europe).
- Contract, agency and consumer protection are three key areas governing the day-to-day work of businesses.
- Offer, acceptance, consideration, intention to create legal relations and capacity are central elements of contract law.

Questions and **assignments** provide engaging activities for students and lecturers in and out of the classroom situation. Further questions on the website help to evaluate their progress.

Review and discussion questions

- 1 Numerically, the sole proprietorship is the most popular form of business organisation throughout Europe. How would you account for this?
- 2 To what extent is corporate status an asset to a business organisation? Does it have any disadvantages?
- 3 Examine the implications of privatising a public sector business organisation.
- 4 Discuss how the legal status of a business affects its objectives, its methods of finance and its stakeholders.
- 5 How would you explain the rise in the popularity of franchising in recent years?

Assignments

- 1 You have recently been made redundant and decide to set up your own small business, possibly with a friend. Assuming that you have £25,000 to invest in your new venture, draft a business plan which is to be presented to your bank manager in the hope of gaining financial support. Your plan should include a clear rationale for the legal form you wish your business to take, your chosen product(s) or service(s), evidence of market research, an indication of anticipated competition and supporting financial information.
- 2 You work in a local authority business advice centre. One of your clients wishes to start a business in some aspect of catering. Advise your client on the advantages and disadvantages of the various legal forms the proposed enterprise could take.



Part One

INTRODUCTION

- 1 Business organisations: the external environment
- 2 Business organisations: the internal environment
- 3 The global context of business
- 4 De-globalising factors: sovereignty, conflicts and political priorities



1

Business organisations: the external environment

Business organisations differ in many ways, but they also have a common feature: the transformation of inputs into outputs; it is through this process that the value is created. This transformation process takes place against a background of external influences which affect the firm and its activities. This external environment is complex, volatile and interactive, but it cannot be ignored in any meaningful analysis of business activity.

Learning outcomes

Having read this chapter you should be able to:

- indicate the basic features of business activity
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Key terms

Environmental change
External environment
General (or contextual)
environment

Immediate (or operational)
environment
Inputs
Open system

Outputs
PESTLE analysis
Transformation system

Introduction

Business activity is a fundamental and universal feature of human existence and yet the concept of ‘business’ is difficult to define with any degree of precision. Dictionary definitions tend to describe it as being concerned with buying and selling, or with trade and commerce, or the concern of profit-making organisations, and clearly all of these would come within the accepted view of business. Such a restricted view, however, would exclude large parts of the work of government and its agencies and the activities of non-profit-making organisations – a perspective it would be hard to sustain in a climate in which business methods, skills, attitudes and objectives have been vigorously adopted by these organisations. It is this broader view of business and its activities that is adopted below and that forms the focus of an investigation into the business environment.

The business organisation and its environment

A model of business activity

Most business activity takes place within an organisational context and even a cursory investigation of the business world reveals the wide variety of organisations involved, ranging from the small local supplier of a single good or service to the multi-billion-dollar international or multinational corporation producing and trading on a global scale. Given this rich organisational diversity, most observers of the business scene tend to differentiate between organisations in terms of their size, type of product and/or market, methods of finance, scale of operations, legal status, and so on. Nissan, for example, would be characterised as a major multinational car producer and distributor trading on world markets, while a local builder is likely to be seen as a small business operating at a local level with a limited market and relatively restricted turnover.

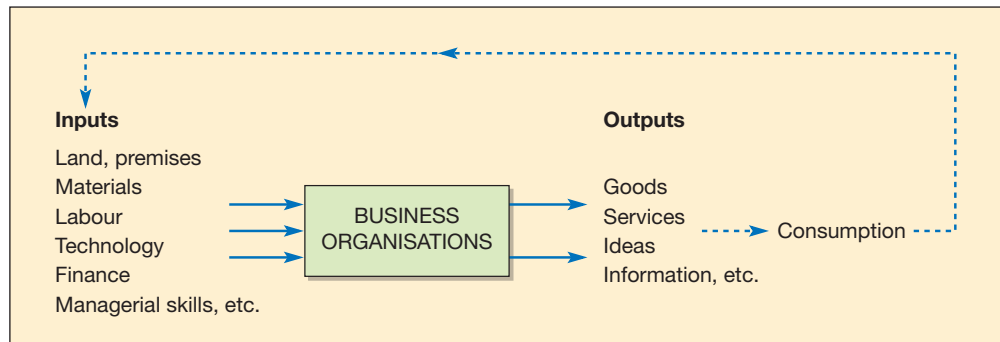


Further information on Nissan is available at www.nissan-global.com
The Nissan UK website address is www.nissan.co.uk

While such distinctions are both legitimate and informative, they can conceal the fact that all business organisations are ultimately involved in the same basic activity, namely the transformation of **inputs** (resources) into **outputs** (goods or services). This process is illustrated in Figure 1.1.

In essence, all organisations acquire resources – including labour, premises, technology, finance, materials – and transform these resources into the goods or services required by their customers. While the type, amount and combination of resources will vary according to the needs of each organisation and may also vary over time, the simple process described above is common to all types of business organisation and provides a useful starting point for investigating business activity and the environment in which it takes place.

A more detailed analysis of business resources and those internal aspects of organisations which help to transform inputs into output can be found in Chapters 2 and 8. The need, here, is simply to appreciate the idea of the firm as a **transformation system** and to recognise that in producing and selling output, most organisations hope to earn

Figure 1.1 The business organisation as a transformation system

sufficient revenue to allow them to maintain and replenish their resources, thus permitting them to produce further output which in turn produces further inputs. In short, inputs help to create output and output creates inputs. Moreover, the output of one organisation may represent an input for another, as in the case of the firm producing machinery, basic materials, information or ideas. This interrelationship between business organisations is just one example of the complex and integrated nature of business activity and it helps to highlight the fact that the fortunes of any single business organisation are invariably linked with those of another or others – a point clearly illustrated in many of the examples cited in the text.

The firm in its environment

The simple model of business activity described above is based on the systems approach to management (see Chapter 2). One of the benefits of this approach is that it stresses that organisations are entities made up of interrelated parts which are intertwined with the outside world – the **external environment** in systems language. This environment comprises a wide range of influences – economic, demographic, social, political, legal, technological, etc. – which affects business activity in a variety of ways and which can impinge not only on the transformation process itself, but also on the process of resource acquisition and on the creation and consumption of output. This idea of the firm in its environment is illustrated in Figure 1.2.

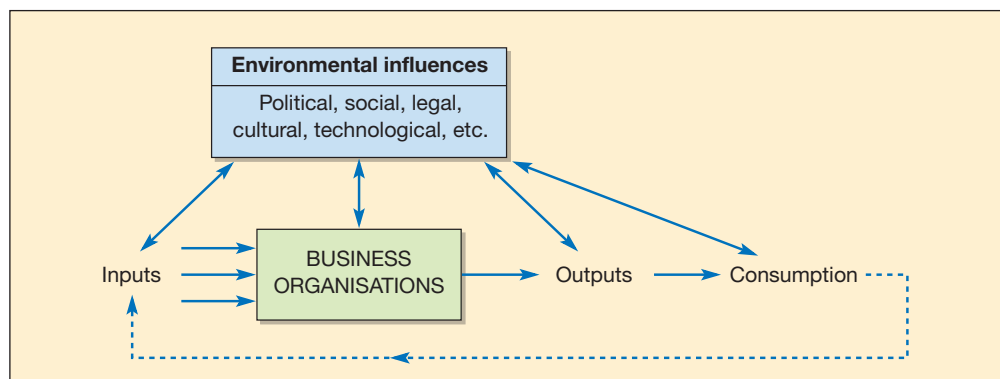
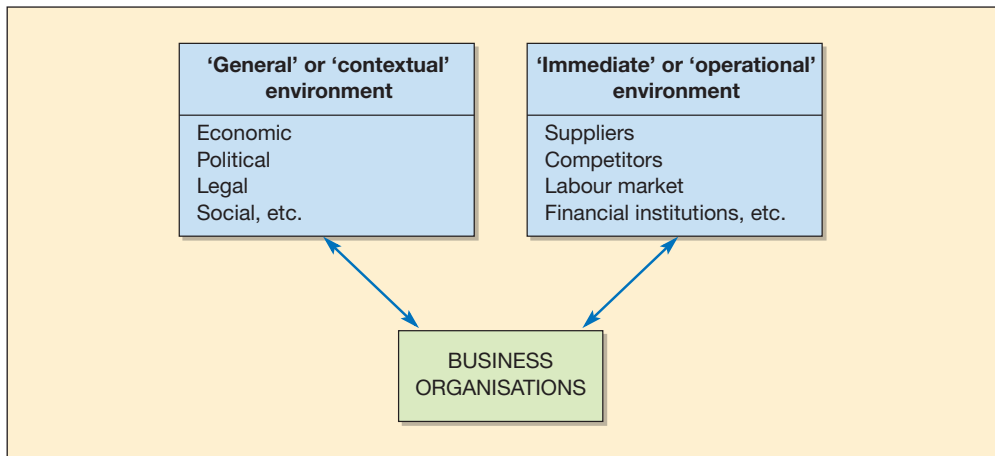
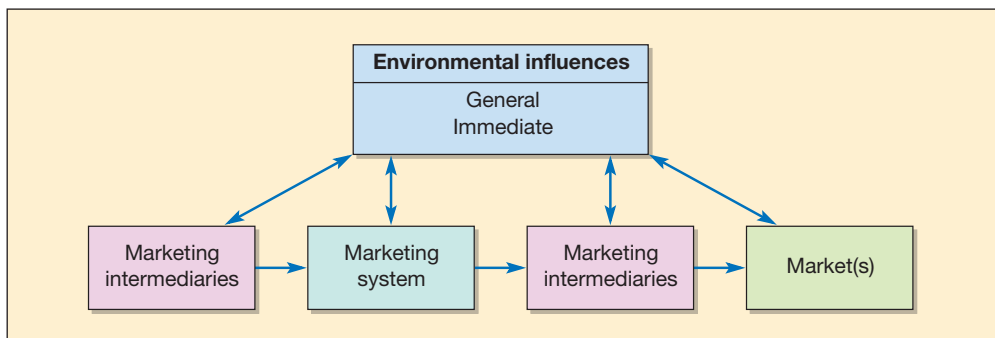
Figure 1.2 The firm in its environment

Figure 1.3 Two levels of environment

In examining the business environment, a useful distinction can be made between those external factors that tend to have a more immediate effect on the day-to-day operations of a firm and those that tend to have a more general influence. Figure 1.3 makes this distinction.

The **immediate (or operational) environment** for most firms includes suppliers, competitors, labour markets, financial institutions and customers, and may also include trade associations, trade unions and possibly a parent company. In contrast, the **general (or contextual) environment** comprises those macroenvironmental factors such as economic, political, socio-cultural, technological, legal and ethical influences on business which affect a wide variety of businesses and which can emanate not only from local and national sources, but also from international and supranational developments. Macro-environmental factors might be thought of as factors so large that the business cannot change them.

This type of analysis can also be extended to the different functional areas of an organisation's activities, such as marketing or personnel or production or finance, as illustrated in Figure 1.4. Such an analysis can be seen to be useful in at least two ways. First, it emphasises the influence of external factors on specific activities within the firm and in doing so underlines the importance of the interface between the internal and external

Figure 1.4 Environmental influences on a firm's marketing system

environments. Second, by drawing attention to this interface, it highlights the fact that, while business organisations are often able to exercise some degree of control over their internal activities and processes, it is often very difficult, if not impossible, to control the external environment in which they operate.

The general or contextual environment

While the external factors referred to above form the subject matter of the rest of the book, it is useful at this point to gain an overview of the business environment by highlighting some of the key environmental influences on business activity. In keeping with the distinction made between general and more immediate influences, these are discussed separately below. In this section we examine what are frequently referred to as the 'PESTLE' factors (i.e. Political, Economic, Socio cultural, Technological, Legal and Ethical influences). A **PESTLE analysis** (or PEST analysis) can be used to analyse a firm's current and future environment as part of the strategic management process (see Chapter 19).

PESTLE examines factors external to the firm; these might represent opportunities or threats and later can be used in a SWOT analysis (whereas strengths and weaknesses are internal factors).

The political environment

A number of aspects of the political environment clearly impinge on business activity. These range from general questions concerning the nature of the political system and its institutions and processes (Chapter 5) to the more specific questions relating to government involvement in the working of the economy (Chapter 6) and its attempts to influence market structure and behaviour (Chapters 12, 16, 18).

Government activities, both directly and indirectly, influence business activity, and government can be seen as the biggest business enterprise at national or local level (Chapter 14). Given the trend towards the globalisation of markets (Chapters 4 and 17) and the existence of international trading organisations and blocs, international politico-economic influences on business activity represent one key feature of the business environment (Chapters 5, 8 and 17). Another is the influence of public, as well as political, opinion in areas such as environmental policy and corporate responsibility (Chapter 10).

The economic environment

The distinction made between the political and economic environment – and, for that matter, the legal environment – is somewhat arbitrary. Government, as indicated above, plays a major role in the economy at both national and local level (Chapters 6 and 14) and its activities help to influence both the demand and supply side (e.g. see Chapter 15). Nevertheless there are a number of other economic aspects related to business activity which are worthy of consideration. These include various structural aspects of both firms and markets (Chapters 11, 12, 13 and 16) and a comparison of economic theory and practice (e.g. Chapters 15, 16 and 17).

mini case**The impact of regional economic conditions**

For a company that trades in different markets across the world, macroeconomic conditions (see Chapter 6) in a particular part of its overall market can play a key role in determining its corporate sales and profitability. French carmaker PSA Peugeot Citroën, for instance, experienced a significant decline in sales in 2012 as demand fell in Southern Europe on the back of the recession in the eurozone. In response to the problem, the company announced significant job cuts aimed at reducing costs and looked to the French government for a series of multi-billion-euro loans to keep it afloat until trading conditions improved.

As the global economy slowed, steel industries have been heavily affected. After a period of rapid expansion (driven mostly by the growth of Chinese infrastructure and social development), China's economy has now started to slow as demand from more developed countries who consume Chinese-made products has fallen. This has led to a dramatic drop in the price of steel as it is no longer

needed for building more factories and infrastructure. To support its own steel industry China has been selling steel at less than the cost European steelmakers can produce it. This is an example of the slowdown in European and American economies causing Chinese businesses to act more aggressively, which has eventually led to the collapse of large parts of the British steel industry such as the (Indian-owned) Tata steel works at Port Talbot near Cardiff in 2016.

Since market conditions can vary substantially in different locations, some businesses can experience significant variations in performance in different parts of their operations. US car giant Ford, for example, announced significant losses in Europe in 2012 alongside 'spectacular' results in its North American division. Like Chrysler and other competitors including GM, Ford was able to offset its European losses with stronger sales in the United States. It also posted pre-tax profits in its South American and Asian markets.



Further information on the organisations mentioned in this mini case is available at www.psa-peugeot-citroen.com; www.tatasteel.com; www.ford.com; www.chrysler.com; www.gm.com

The social, cultural and demographic environment

Both demand and supply are influenced by social, cultural and demographic factors. Cultural factors, for example, may affect the type of products being produced or sold, the markets they are sold in, the price at which they are sold and a range of other variables. People are a key organisational resource and a fundamental part of the market for goods and services. Accordingly, socio-cultural influences and developments have an important effect on business operations, as do demographic changes (Chapters 7 and 8).

The technological environment

Technology is both an input and an output of business organisations as well as being an environmental influence on them. Investment in technology and innovation is frequently seen as a key to the success of an enterprise and has been used to explain differences in the relative competitiveness of different countries (Chapter 8). It has also been responsible for significant developments in the internal organisation of businesses in the markets for economic resources.

The legal environment

Businesses operate within a framework of law, which has a significant impact on various aspects of their existence. Laws usually govern, among other things, the status of the organisation (Chapter 11), its relationship with its customers and suppliers and certain internal procedures and activities (Chapter 9). They may also influence market structures and behaviour (e.g. Chapters 16 and 19). Since laws emanate from government (including supranational governments) and from the judgments of the courts, some understanding of the relevant institutions and processes is desirable (e.g. Chapters 5 and 9).

The ethical and ecological environment

Ethical considerations have become an increasingly important influence on business behaviour, particularly among the larger, more high-profile companies. One area where this has been manifest is in the demand for firms to act in a more socially responsible way and to consider the impact they might have on people, their communities and the natural environment (Chapter 10).

The immediate or operational environment

Resources and resource markets

An organisation's need for resources makes it dependent to a large degree on the suppliers of those resources, some of which operate in markets that are structured to a considerable extent (e.g. Chapter 8). Some aspects of the operation of resource markets or indeed the activities of an individual supplier can have a fundamental impact on an organisation's success and on the way in which it structures its internal procedures and processes. By the same token, the success of suppliers is often intimately connected with the decisions and/or fortunes of their customers. While some organisations may seek to gain an advantage in price, quality or delivery by purchasing resources from overseas, such a decision can engender a degree of uncertainty, particularly where exchange rates are free rather than fixed (Chapter 17). Equally, organisations may face uncertainty and change in the domestic markets for resources as a result of factors as varied as technological change, government intervention or public opinion (e.g. conservation issues).

Customers

Customers are vital to all organisations and the ability both to identify and to meet consumer needs is seen as one of the keys to organisational survival and prosperity – a point not overlooked by politicians, who are increasingly using business techniques to attract the support of the electorate. This idea of consumer sovereignty – where resources are allocated to produce output to satisfy customer demands – is a central tenet of the market economy (Chapter 6) and is part of a capitalist ideology whose influence has become all-pervasive in recent years, the idea being that companies competing is the most efficient way to organise society. Understanding the many factors affecting both individual