Environment literally means the surroundings external objects, influences or overall circumstances under which someone or something exists.

In Business the environment in which an organization exists could be broadly divided into two parts:

A) The Internal environment (Related the factors such as its personnel, physical facilities, organization and functional means, which are generally controllable.
B) The External environment (Related the factors such as economic, socio cultural, Government and legal, demographic, geo – physical – by and large beyond the control.

The External environment includes all the factors outside the organization, which provide opportunities or pose threats to the organization.

The internal environment refers to all the factors within an organization which imparts strengths or cause weaknesses of a strategic nature. The environment in which an organization exists can, therefore, be described in terms of the opportunities and threats operating in the external environment apart from the strength and weaknesses existing in the internal environment.

INTERNAL ENVIRONMENT:

There are a number of internal factors which influence the strategy and other decisions. An outline of the important internal factors is given below:
**Value system:** The value system of the founders and those at the helm of affairs has important bearing on the choice of business, the mission and objectives of the organization, business policies and practices. It is a widely acknowledges fact that the extent to which the value system is shared by all in the organization is an important factor contributing to success.

**Mission and Objectives:** The business domain of the company, priorities, direction of development, business philosophy, business policy etc. is guided by the mission and objectives of the company.

**Management Structure and Nature:** the organizational structure, the composition of the board of directors, extent of professionalisation of management etc. are important factors influencing business decisions.

**Internal Power Relationship:** Factors like the amount of support the top management enjoys from lower levels and workers, share holders and board of directors have important influence on the decisions and their implementation. The relationship between the members of the Board of directors is also a critical factor.

**Human Resources:** The characteristics of the human resources like skill, quality, morale, commitment, attitudes, etc. could contribute to the strength or weakness of an organization. Sometimes, organizations find it difficulties to carry out restructuring or modernization because of resistance by employees whereas they are smoothly one in some others.

The involvement, initiative etc. of people at different levels may vary from organization to organization. The organizational culture and overall environment have bearing on them. John Towers, MD, Rover group, observes that a Japanese company of 30,000 employees is 30,000 process improvers. In a western company, it is 2,000 process improvers and 28,000 workers. And in an Indian company …………..?

**Company Image and Brand Equity:** The image of the company matters while raising finance, forming joint ventures or other alliances, soliciting marketing intermediaries, entering purchase or sale contracts, launching new products etc. Brand equity is also relevant in several of these cases.

However, there are a number of other internal factors which contribute to business success/ failure or influences the decision making. These are:

- **Physical Assets and facilities** like the production Capacity, technology, and efficiency of the productive apparatus, logistics etc. are among the factors which influence the competitiveness
- **R & D and technological capabilities**, among other things, determine the ability to innovate and compete.
- **Marketing resources** like the organization for marketing, quality of the marketing men, brand equity; distribution network etc. has direct bearing on the marketing efficiency. They are important also for brand extension, new product introduction etc.
• **Financial Factors** like financial policies, financial position, and capital structure are also important internal environment affecting business performance, strategies and decisions.

**EXTERNAL ENVIRONMENT:**
The external environment consists of two types of environment, viz micro environment and macro environment. Recently the International environment comes under mega environment.

**Micro Environment:**
The Micro environment consists of the actors in the company’s immediate environment, that affect the performance of the company. These include –

- **Suppliers** – those who supply the inputs like raw materials
- **Marketing intermediaries** – which are ‘firms that aid the company in promoting, selling and distributing its goods to final buyers’
- **Competitors** – not only other firms of similar products but also all those who compete for the discretionary income of the consumers.
- **Customers** – Business is a create of customer; therefore monitoring the customer sensitivity is a prerequisite for the business success.
- **Publics** – is any group that has an actual or potential interest in or impact on an organization’s ability to achieve its interests. Media publics, citizen’s action publics and local publics are some examples.

**Macro Environment:**
The Macro environment consists of the larger societal forces that affect all the actors in the company’s micro environment – namely:

- **Demographic** – population growth rate, age composition, sex composition, education level, caste and creed, religion etc. All factors which relevant to business.
- **Economic** - economic condition, economic policies and the economic system are the important external factors that constitute the economic environment of a business
- **Natural** – geographical, and ecological factors, such as natural resources endowments, weather and climatic conditions, topographic factors, location aspects in the global context, or facilities, etc., are all relevant to business
- **Technological** – the fast changing technologies also create problems for enterprises as they render plants and products obsolete quickly. Product – market – matrix generally has a much shorter life today than in the past. It is particularly so in the international marketing context.
- **Political** – Political and Government environment has close relationship with the economic system and economic policy. For example, the communist countries had a centrally planed economic system. In most countries, apart from those laws that control investment and related matters, there are a number of laws which regulate the conduct of business. These laws cover such matters as standards of product, packaging, promotions etc.
- **Socio – Cultural**: socio – cultural fabric is an important environment factor that should be analyzed while formulating the business strategies. The cost of ignoring the customs, traditions, taboos, tastes and preferences etc. of a people could be very high. The buying and consumption habits of the people, their languages, beliefs, and values, customs and traditions, tastes and performances, education are all factors that affect business.

The micro environment is also known as task environment and operating environment.

**Mega Environment:**

Mega environment mainly consist of International Environment which is very important from the point of certain categories of business.

**A. Import and export dependency:**
- Industries directly depends on Imports or exports
- Import – competing Industries.
- A boom in the export market or a relaxation of the protectionist policies may help the export oriented industries.

- A liberalization of imports may help some industries which use imported items, but may adversely affect important – competing industries.

**B. World trade linkage:**
- Oil price hikes have seriously affected a number of economics. These hikes have increased the cost of production and the prices of certain
products like fertilizers, synthetic fabrics, etc. The high oil price has led to an increase in the demand for automobile models that economizes energy consumption.

- The oil crisis led to a reorientation of the government of India’s energy policy. Such development affects the demand, consumption and investment pattern.

**Environmental Scanning – factors and approaches**

Before start the strategy formulation, in any organization, it must to do the scan the external environment to identify the possible opportunities and threats and its internal environment for strength and weaknesses.

In his book, “Essential of strategic management“, **J.David Hunger** pointed out that *Environmental scanning* is the monitoring, evaluating and disseminating of information from the external and internal environments to key people within the corporation. It is a tool that a corporation uses to avoid strategic surprise and to ensure long – term health.

Azhar Kazmi, quoted in his book – “Business Policy and strategic management that – the process by which organizations monitor their relevant environment to identify opportunities and threats defecting their business is known as environmental scanning.

Factors to be consider for environmental scanning:

1. **Events** are important and specific occurrences taking place in different environmental sectors.
2. **Trends** are the general tendencies or the courses of action along which events take place.
3. **Issues** are the current concerns that arise in response to events and treats.
4. **Expectations** are the demands made by interested groups in the light of their concern for issues.

**Example: Gas leakage accident at the Union Carbide Factory at Bhopal in Dec. 1984.**

<table>
<thead>
<tr>
<th>Event</th>
<th>The accident and the resulting holocaust</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trend</td>
<td>The authorities and Organizations to be conscious about safety from hazardous exposure to chemicals</td>
</tr>
<tr>
<td>Issue</td>
<td>A rising concern about environmental pollution</td>
</tr>
<tr>
<td>Expectation</td>
<td>To legislate changes in rules and regulations pertaining to safety measures and stricter enforcement through various mechanism</td>
</tr>
</tbody>
</table>
By monitoring the environment through environmental scanning, an organization can consider the impact of the different events, trends, issues, and expectations on its strategic management process. Since the environment facing any organization is complex and its scanning is absolutely essential, strategists (who, as individuals or in groups – internal or external; are concerned with and play a role in strategic management) have to deal cautiously with the process of environmental scanning.

**Objectives:**

- To make efforts to deal with it in such a manner that unnecessary time and effort is not expended, while important factors are not ignored.
- To enable this it is important to devise an approach, or a combination of approaches to environmental scanning.

Approaches to environmental scanning:

Kubr has suggested three approaches, which could be adopted for sorting out information for environmental scanning.

1. **Systematic approach:** Gathering information for environmental scanning which have a direct impact on organizations activities, Govt. policy statements pertaining to an organization’s business and industry to monitor changes and take the relevant factors into account. Continuously updating such information is necessary not only for strategic management but also for operational activities.

2. **Ad Hoc approach:** Using this approach, an organization when undertake special projects, evaluate existing strategies, or devise new strategies; may conduct special survey and studies to deal with specific environmental issues periodically.

3. **Processed – form approach:** when an organization uses information supplied by Govt. or private agencies, it uses secondary sources of data and the information gathered in a processed form.

Since environmental scanning is absolutely necessary for strategy formulation of any organization, whatever approaches is adapted, DATA Collection and Processing systematically is ultimate for Strategic Management Process.

Sources of information: Strategists use different information sources depending on their needs for environmental scanning.

1. **External** (like publications – newspaper, magazines, journals, books, trade and Industry association newsletter, Govt. Publications, annual reports of competitions etc. mass media such as Radio, Television and the Internet:

   **External Agencies:** like customers, marketing intermediaries, suppliers, trade associations, Govt. agencies and so on.
2. **Internal** – (company files and documents, MIS, databases, company employees. Formal studies conducted by employees, market research agencies, consultants and educational institutions on hire.

### Methods and Techniques used for Environmental Scanning (ES):

There are wide range of methods and techniques available for ES. Strategists may choose one which suit their needs in terms of the –

- Quantity
- Quality
- Availability
- Time lines
- Relevance
- Cost of environmental information

Various authors have mentioned the methods and tech. Used for ES. Le Bell and Krasner have outlined 9 groups of techniques:

1. Single – variable extrapolation
2. Theoretical – limit envelopes
3. Dynamic modes
4. mapping
5. multivariable interaction analysis
6. unstructured expert opinion
7. structured expert opinion
8. structured in expert opinion
9. unstructured in expert speculation

But the most popular of these are:

1. The **chaos theory** by Edward Lorenz and Michael Feigenbaum. Chaos theory uses mathematical models, known as chaotic models, to interpret the process of non – linear and dynamic system.

The phenomenon of Chaos is observed in a wide variety of processes – biological, sociological, economic, and meteorological. The applications of Chaos theory in management may range from predicting market behavior, financial forecasting and anticipating competitive strategies.

**Lesion:** In a dynamic environment, it is suicidal for organizations to remain static. They have to forego keeping an internal orientation and attempt to change dynamically as the environment change.

3. **The QUEST (Quick environmental scanning techniques)** is a four step process which uses scenario – writing for scanning the environment and
identify the strategic options. The Four steps involved in applying this technique are –

1. Internal strategists will observe and identify the major events and trends in the Industry

2. Speculate on a wide range of important ISSUES that might affect the future of their organization

3. Preparing a report summarizing the major issues and their implications and 3-5 scenarios incorporating the major themes of their discussion.

4. Report and scenarios are reviewed by a group of strategists who identify feasible strategic options to deal with the evolving environment.

After the environmental scanning process is complete, the strategists start to appraise the environment - called environmental appraisal. It is structured by the preparation of the environmental threats and opportunities profile (ETOP), which involves dividing the environment into different sectors and then analyzing the impact of each sector on the organization.

**Tools for Environmental Scanning:**

The complete information positive and negative, internal and external are very important for every strategist so that they can combat the possible threats and exploit the opportunities in the right moment by preparing the right strategies.

Keeping in view them generally using the following tools for environmental scanning:

**The SWOT Analysis through SWOT Matrix:**

SWOT, is an instrumental framework in value based management and strategy formulation to give in-depth information to strength, weakness, opportunity and threats for a particular company / organization.

**Strength and Weaknesses (SW)** – Internal value – creating or destroying factor like assets, skill, resources etc. which can measured by using internal assessment or by external benchmarking.

**Opportunity and Threats (OT)** – External value – creating or destroying factors and a company can not control, but emerge from either the competitive dynamicstic of the Industry / market or from demographic, political, technical, social, and legal or cultural factors.
The relationships in a SWOT analysis are generally represented by a 2x2 matrix. The ‘Strength’ and ‘Opportunities’ are both positive considerations. ‘Weakness’ and Threats are both negative considerations. The final results of an analysis could be listed in the matrix in given below:

<table>
<thead>
<tr>
<th>Internal Factors</th>
<th>Positive</th>
<th>Negative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strength</td>
<td>• Patents</td>
<td>• Weakness</td>
</tr>
<tr>
<td></td>
<td>• Strong brand names</td>
<td>• Lack of potent protection</td>
</tr>
<tr>
<td></td>
<td>• Good Reputation</td>
<td>• A weak brand name</td>
</tr>
<tr>
<td></td>
<td>• Cost advantages from proprietary know how</td>
<td>• Poor reputation among customers</td>
</tr>
<tr>
<td></td>
<td>• Exclusive access to high grade natural resources</td>
<td>• High cost structure</td>
</tr>
<tr>
<td></td>
<td>• Favorable access to distribution networks</td>
<td>• Lack of access to the best natural resources</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Lack of access to key distribution channels</td>
</tr>
<tr>
<td>External Factors</td>
<td>Opportunities</td>
<td>Threats</td>
</tr>
<tr>
<td></td>
<td>• An unfulfilled customer need</td>
<td>• Shifts in consumer tastes away from the firm’s products</td>
</tr>
<tr>
<td></td>
<td>• Arrival of new technologies</td>
<td>• Emergence of substitute products</td>
</tr>
<tr>
<td></td>
<td>• Loosening of regulations</td>
<td>• New regulations</td>
</tr>
<tr>
<td></td>
<td>• Removal of international trade barriers</td>
<td>• Increased trade business</td>
</tr>
</tbody>
</table>

The above matrix identifies the strength, weaknesses, threats and opportunities of a business firm. This formation can be used by the company in many ways in evolving its options for the future. In general, the company should attempt to:
- Build its strength
- Reverse its weakness
- Maximize its response to opportunities
- Overcome to its threats

**PESTLE Analysis through PESTLE Matrix:**

Environmental Scanning is an important component when the business is in Competition. PESTLE analysis involves identifying the political, economic, socio-cultural, technological, legal and environmental influences of an organization or policy in the past, and how they might do so in future.

- Like the SWOT analysis, the PESTLE analysis is also simple, quick, and uses four key perspectives. PESTLE analysis, has its origins in the PEST analysis, which involves identifying the political, economic, socio-cultural and technological influences on an organization.
• The PESTLE analysis used to provide a context for the organisation's / individual's role in relation to the external environment (mainly macro and mega environment).

• Depending on which elements are included it can also be referred to as STEP, STEEP, PESTEL, PESTLE or LEPEST.

• Recently it was even further extended to STEEPLE and STEEpled, including education and demographics.

• PESTLE is useful before SWOT - not generally the other way round. It helps to identify SWOT factors.

The advantage of this tool is that it encourages management into proactive and structured thinking in its decision making.

**The PESTLE Matrix:**

<table>
<thead>
<tr>
<th>Political</th>
<th>Economic:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Current legislation</td>
<td>• Economic situation and trends</td>
</tr>
<tr>
<td>• Future legislation</td>
<td>• Taxations to products.</td>
</tr>
<tr>
<td>• Regulatory bodies and processes</td>
<td>• Market and Trade cycle</td>
</tr>
<tr>
<td>• Government policies</td>
<td>• Specific Industry factor</td>
</tr>
<tr>
<td>• Government term and changes</td>
<td>• Customer</td>
</tr>
<tr>
<td>• Trade policies</td>
<td>• Interest and exchange rates</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Social:</th>
<th>Technological:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Life style change</td>
<td>• Replacement</td>
</tr>
<tr>
<td>• Demographic</td>
<td>• Tech. solutions</td>
</tr>
<tr>
<td>• Cons. Attitudes and opinion</td>
<td>• Maturity of Technique</td>
</tr>
<tr>
<td>• Brand, competitive tech. Image</td>
<td>• Manufacturing maturity and capacity</td>
</tr>
<tr>
<td>• Consumer buying pattern</td>
<td>• Innovation potential</td>
</tr>
<tr>
<td>• Ethnic / Religious factors</td>
<td>• Technical access, licensing, patents</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Legal:</th>
<th>Environmental:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• International Law</td>
<td>• Ecological / Environmental issues</td>
</tr>
<tr>
<td>• Employment law</td>
<td>• Environmental Impact</td>
</tr>
<tr>
<td>• Competition law</td>
<td>• Environmental legislation</td>
</tr>
<tr>
<td>• Health and safety law</td>
<td>• Energy consumption</td>
</tr>
<tr>
<td>• Regional legislation law</td>
<td>• Waste disposal</td>
</tr>
</tbody>
</table>

<table>
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<th>Technological:</th>
<th>Environmental:</th>
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<td>• Technical access, licensing, patents</td>
<td></td>
</tr>
</tbody>
</table>
5 force analysis/ competitive analysis

Michael E. Porter the renowned author of competitive strategy, Competitive Advantage and Competitive Advantage of Nations, has provided a structural analysis of industries. According to this analysis, the state of competition in an industry depends on five basic competitive forces viz:

1. Rivalry among existing firms
2. Threat of new entrants
3. Threats of substitutes
4. Bargaining power of suppliers
5. Bargaining power of Buyers

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1. Rivalry among existing firms

There is competitive rivalry between firms on a continuing basis. The various players try to constantly jockey for position and try new product and process innovations in order to develop a strategic edge and hence a stronger position in the competitive space. Intense rivalry is related to a number of factors:

- competitors are large in number and of comparable sizes;
- industry growth is slow;
- the product or service has low switching costs;
- fixed costs are high;
- the product is perishable

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As the competition grows, firms require to provide more variety of products. As a result of this, there are offerings of various consumer products, more than ever before. It has become a common practice for the same company to offer different products for different market segments.

For example, between 1998-99 Hindustan Lever introduced 64 product innovations. Forty four of these were new launches and twenty were re-launches. 50 percent of its growth during this period came from these launches.

2. Threats of New Entrants

A prosperity industry often faces threat of new entrants which can alter the competitive environment. There are many entry barriers like – Government Policies, Economies of Scale, Product differentiation, Brand Identity or Monopoly elements, Capital Requirements and Cost disadvantages.

In many cases Government policy and regulation are important entry barriers. For example, prior to the economic liberalization in India, government – dictated entry barriers were rampant, like reservation of industries / industrial licensing, import restriction, restriction on foreign capital and technology etc.

3. Threats of substitutes

An important force of competition is the power of substitutes. “Substitutes limit the potential returns in an industry by placing a ceiling on the price firms in the industry can profitability charge. The more attractive the price performance alternative offered by substitutes, the firmer the lid on industry profits”

Porters explained the TOS are: Buyer propensity to substitutes, Relative Price Performance and Switching Costs

- Equally, a firm that has a product that cannot be easily substituted, either because it is unique or because it has some form of protection (e.g. a patent), is in a strong position.

- The key questions for this analysis are:
  - Whether or not the substitute poses a threat to the organization’s product or service or provides a higher perceived value or benefit.
  - What is the ease with which buyers can switch to substitutes.
  - Can the organization reduce the risk of substitution by building in switching costs?

- Each product idea is copied or improved by competition. It is not necessarily the best product idea that becomes dominant. However, improved and new product ideas have become an integral part of the game. For an example:

  Hero Honda, at one stage found it difficult to get a foot hold in the Indian market for two-wheelers. However, when most motorcycles were giving a fuel economy of 45-45 kilometers per liter, Hero Honda came out with a self designed motorcycle capable of giving 80 kilometers to a liter.
4. The bargaining power of Customers

For several industries, buyers/ customers are potential competitors – they may integrate backward. Beside, they have different degree of bargaining power. Important determinants of the buyer power, explained by Porter are:

Bargaining for higher Quality or more service, Profitability of the Buyer, Potential for backward Integration by buyer, Price sensitivity, switching costs, Extent of buyers’ information.

5. Bargaining power of suppliers

The important determinants of supplier power are the following:
Switching Costs, Differentiation of inputs, Supplier concentration, Supplier Margins, Volume Sales, Firm’s ability to forward integration.

- Suppliers can exert bargaining power in an industry by raising prices or by changing the quality of their goods and services.
- For example if a major steel producer selling to a small metal fabricator, the firm has a weak position and its ability to compete will to a large extent depend on the steel producer. If, the supplier decided to raise prices, the firm would have high switching costs and little option but to accept the raise.
- The advantage is with the supplier when:
  - it is large and dominated by a few companies;
  - its product is unique or differentiated;
  - it does not have sufficient competition;
  - it has the ability to integrate forward into the industry;
  - the industry is not an important customer;
  - The buying industry has low barriers to entry.
  - the supplier is strong

Conclusion:

Business environment is dynamic. Many elements in the environment undergo changes. Technological changes are frequent. Tastes and the preferences of the people change. The competitive situation changes.
- Demographic factors, including population size, change.
- Attitude and value systems also undergo changes.
- Economic factors like income, change continuously.
- Government policies and regulations also change to cope with the changing environment.
- All these factors indicate that a business policy should be dynamic enough to be successfully adaptable to the changing environment.

Therefore, the success of a business today, depends on its ability to foresee the environmental changes and to modify its strategies appropriately with internal and external environmental changes.