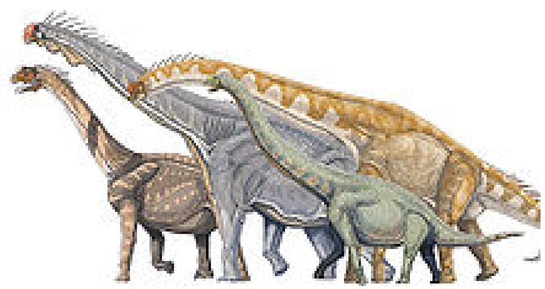
BA 291 – BUSINESS ENVIRONMENT

By Aj. Parichat Jantori

“ It’s not the strongest of the species that survives, nor the most intelligent, that survives. It is the one that is the most adaptable to change”



Which one do you prefer?

“Geologists at Ohio State University have found the largest-ever complete fossil of a cockroach, one that lived 55 million years before the first dinosaurs.”

Facts about Cockroaches

- can eat almost anything, including paper, wood, glue and rubbish.
- quite intelligent and can learn and adapt to situations amazingly fast.
- move fast from place to place. They can fly or walk. run in mazes and remember the route of the maze from day to day
- know how to become resistant to pesticides quickly and are therefore very difficult to poison
- each female cockroach can produce hundreds of eggs during her short life span. Within a year, you can have over 100,000 cockroaches from that original female.
- are infamous for their tenacity, they survive a nuclear war, can live without head for weeks.

Facts about Dinosaur

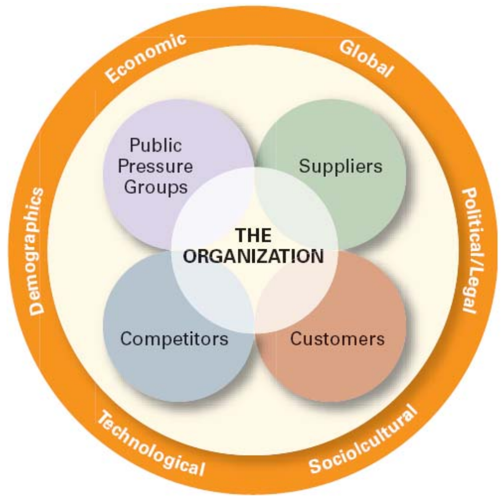
- A large collision would throw so much dust into the air that sunlight would not be able to shine and plants and animals would die. The dramatic changes in climate that resulted from this huge collision were too much for the dinosaurs. They were not able to survive.
- Dinosaurs became extinct is volcanic activity.
- Disease killed off the dinosaurs

Size, slow, food, number offspring, slow breeding …

Business Environment

The environment in which companies operate is continually changing, sometimes quite rapidly. Companies have to learn how to adjust and adapt their business to change.

Business Environment



General Environment

The general environment affects organizations indirectly. Change in general environment does not directly change day-to day operations, however, they do effect all organizations eventually.

Political Environment

Political Risk

- Political instability
- Expropriation of corporate assets without prompt and adequate compensation
- Forced sale of equity to host-country nationals, usually at or below depreciated book value
- Discriminatory treatment against foreign firms in the application of regulations or laws
- Barriers to repatriation of funds (profits or equity)
- Loss of technology or other intellectual property (such as patents, trademarks, or trade names)
- Interference in managerial decision making
- Dishonesty by government officials, including cancelling or altering contractual agreements, extortion demands, and so forth

Political Environment

Impact on Business

- Business decision, Investment decision
- Political institutions as policy maker
- Consumer confident, consume decision
- Cost of doing business – corruption
- Competitive advantage – subsidiary, discrimination

Legal Environment

Business related law

- Company law
- Product safety and liability, labeling requirement, consumer protection
- Tax law
- Competition law, anti-trust law, cartel law
- Regulations on accounting – US GAAP, IFAS, IAS, Thai GAAP
- Labor law, employee right
- Environment law

Legal Environment

Impact on business

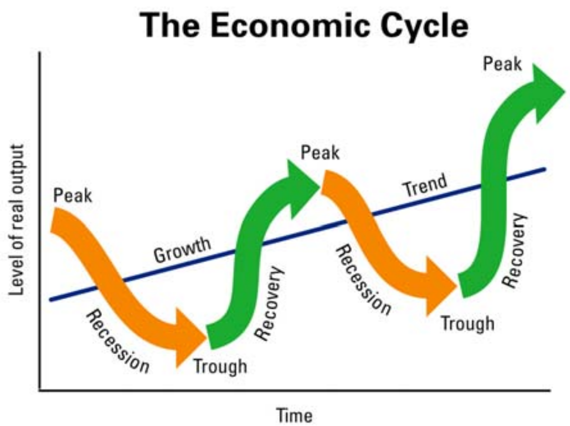
- Law as a framework
- Product liability law, consumer protection – more concern about consumer, cost when sue in the court
- Labor law – cost, benefits for employee
- Competition law – price setting, merger and acquisition other companies
- Environmental law – product design, facilities design

Legal Environment

Liebeck v. McDonald's Restaurants (McDonald's coffee case and the hot coffee lawsuit)

- a woman who was heavily burned by hot coffee purchased from fast food restaurant McDonald's was rewarded $2.86 million.
- Her attorneys argued that McDonald's coffee was "defective," claiming it was too hot and more likely to cause serious injury than coffee served at any other establishment

Economic Environment



Exchange Rate

„The euro briefly traded as low as Y108 on Monday, its weakest level since November 2001. The resulting loss of buying power among European consumers is a serious problem for Japanese exporters such as Sony, whose profit forecast for the year to March 2011 assumes an average exchange rate of Y125 to the euro. The divergence could cost the electronics group Y100bn this year." […]

The financial turmoil in Europe, which is hitting the euro, is creating additional problems for Japanese companies. Hitachi, for example, has said some of its projects are being delayed by financing issues. The weaker euro, which has lost 5.9 per cent against the yen over the past month, also makes European manufacturers more competitive. […]" (Financial Times, 8.06.2010)

Exchange Rate

Currency Exposure

- **Transaction exposure:** the extent to which the income from individual transactions is affected by fluctuations in foreign exchange values
- **Translation exposure:** the impact of currency exchange rate changes on the reported financial statements of a company
- **Economic exposure:** the extent to which a firm's future international earning power is affected by changes in exchange rates

Hedging against currency risk: Forward contract, Options, Swaps, Diversification of location

Inflation

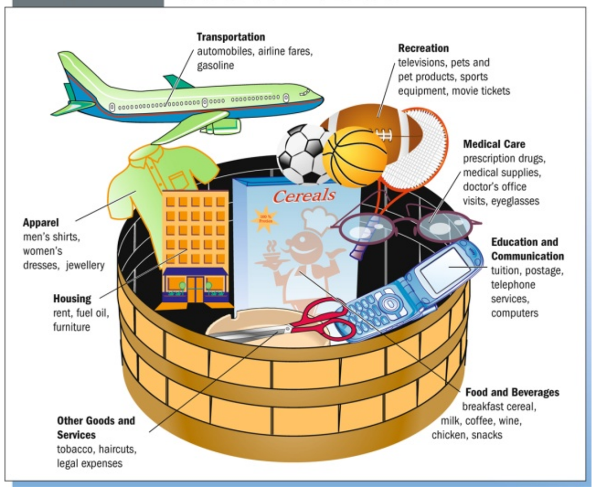
Inflation: The rate at which the general level of prices for goods and services is rising, and, subsequently, purchasing power is falling (Consumer price index)

-Core inflation: a measure of inflation which excludes certain items that face volatile price movements

-Headline inflation: measure of the total inflation within an economy

Inflation

Figure 3.5 Contents of the CPI Market Basket



Cause of Inflation

Demand-pull inflation caused by increases in aggregate demand due to increased private and government spending

Cost-push inflation, also called "supply shock inflation," is caused by a drop in aggregate supply (potential output). This may be due to natural disasters, or increased prices of inputs.

Built-In inflation is often linked to the "price/wage spiral".

Unemployment rate

1. Frictional unemployment: is the time period between jobs when a worker moves from one job to another.
2. Seasonal unemployment: Unemployment expected at a given time of year
3. Cyclical unemployment: occurs when there is not enough aggregate demand in the economy.
4. Structural unemployment: occurs when a labor market is unable to provide jobs for everyone who wants one because there is a mismatch between the skills of the unemployed workers and the skills needed for the available jobs

Demographic

- Physical characteristics of a population such as:
- Gender
- Level of education
- Geographic location, Immigration
- Income
- Family composition
- Age

Impact on business: Consumer taste and preferences, Product & Service design, New customer segments, Sophistication of product

Product for Aging Society

Infrastructure

The physical facilities that support economic activities, including railroads, highways, ports, airfields, utilities, power plants, schools, hospitals, and commercial distribution systems.

Impact on business:

- Cost
- Efficiency
- Disruption of Production
- Competitive Advantage

Social-cultural

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- The sum total of beliefs, rules, techniques, institutions, and artifacts that characterize human populations.
- Consists of learned patterns of behavior common to the members of a given society.
- The unique lifestyle of a particular group of people.

Impact on business: tastes and preferences, product design, marketing strategies, business negotiation, meeting, personal management

Technology

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- Method or technique for converting inputs to outputs in accomplishing a specific task.

Changes in the technological environment have had some of the most dramatic effects on business. A company may be thoroughly committed to a particular type of technology, and may have made major investments in equipment and training only to see a new, more innovative and cost-effective technology emerge.

Globalization/ Internationalization

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International integration arising from increasing human connectivity and interchange of worldviews, products, ideas, and other aspects of culture.

In particular, advances in transportation and telecommunications infrastructure, including the rise of the Internet, represent major driving factors in globalization and precipitate further interdependence of economic and cultural activities.

Task Environment

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The task environment include all the sectors that conduct day-to-day transactions with the organization and directly influence its basic operations and performance.

Task environment includes customers, competitor, suppliers, labor market and pressure groups.

Competition Environment

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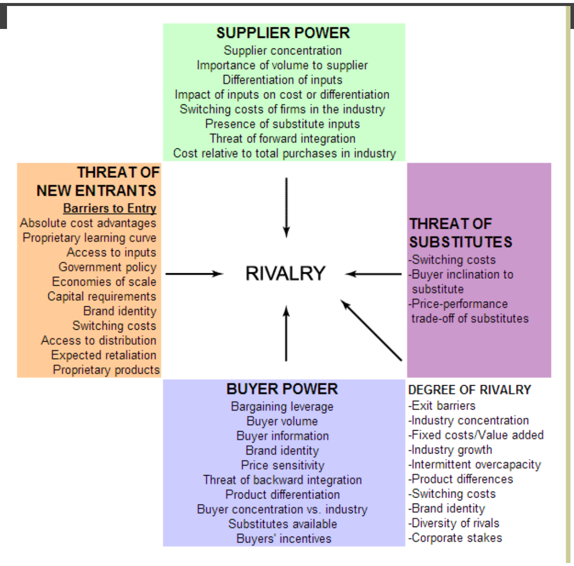

Internal Environment

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The internal environment of an organization contains the internal resources (funding, employee, skills, know-how)and possesses internal capabilities (process, management system) and core competencies. The organization needs to conduct the internal analysis figure out loopholes in resources, capabilities, and core competencies.

This enables the firm to devise suitable strategies for closing the gaps in the aforesaid internal components

Business Environment Analysis

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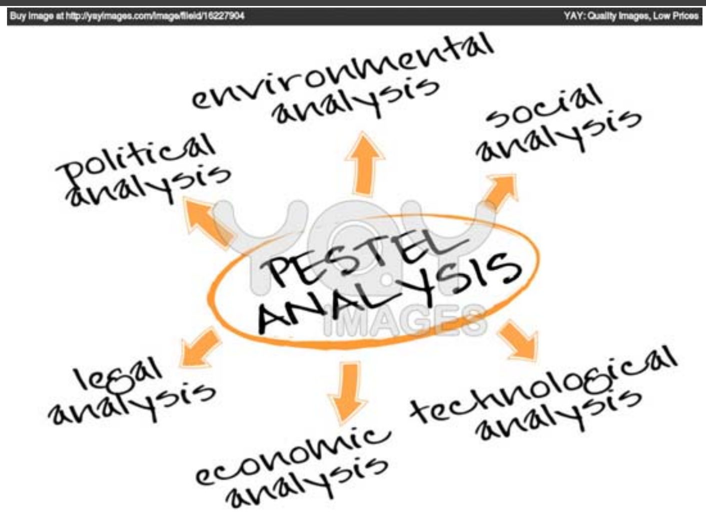

Getting involve in International Business

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Business, just like a crime has become a unified, global field.

Why doing international business? Why firms doing FDI?

Basic foreign entry decision

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- Which markets to enter
- When to enter these markets
- What is the scale of entry

Which foreign market

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Favorable

- Politically stable developed and developing nations
- Free market systems
- No dramatic upsurge in inflation or private-sector debt

Unfavorable

Politically unstable developing nations with a mixed or command economy or where speculative financial bubbles have led to excess borrowing

Cost

Benefits

Risk

Timing of entry

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Advantages in early market entry:

- First-mover advantage.
- Build sales volume.
- Move down experience curve and achieve cost advantage.
- Create switching costs.
  - Tie customers to your product.
- Establishment of entry barriers for late entrants

Disadvantages:

- First mover disadvantage - pioneering costs.
- Changes in government policy
- Opportunity to free ride on first mover investment

Scale of entry

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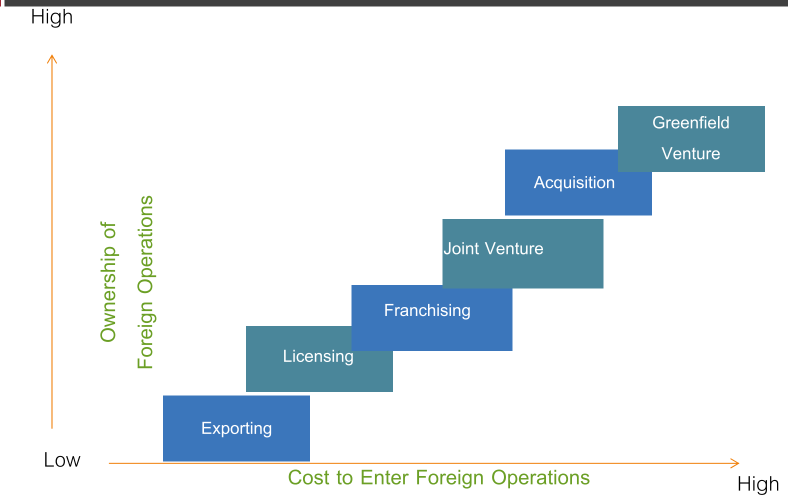
Large scale entry

- Strategic Commitments - a decision that has a long-term impact and is difficult to reverse.
- May cause rivals to rethink market entry.
- May lead to indigenous competitive response

Small scale entry

- Time to learn about market.
- Reduces exposure risk.

Strategies for entering the international business



Entry mode

- *Exporting and Importing* - The act of selling and buying goods across the countries
- *Global sourcing (offshoring)* – Purchasing materials or labor from around the world wherever it is cheapest
- *Licensing* - A trade agreement in which one company (licensor) allows another company (licensee) to use its company name, products, patents, brands, trademarks, etc. in exchange for a fee or royalty.

Entry mode

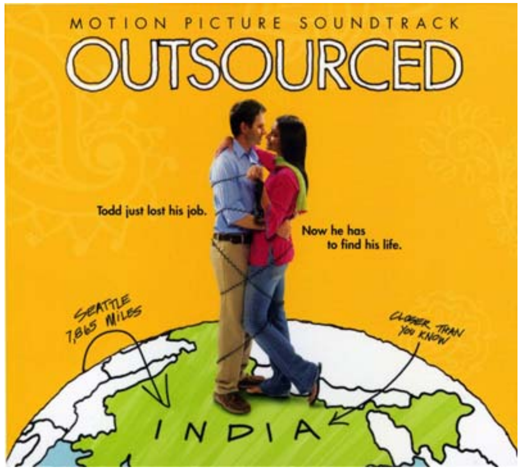
- *Franchising* - a form of licensing where a company (franchiser) agrees to provide a franchisee a name, logo, operational guidelines, products, etc, in return for a financial commitment and the agreement to conduct business in accord with the franchiser's standard of operations.
- *Joint venture* – A specific type of strategic alliance in which the partners agree to form a separate, independent organization for some business purpose.
- *Direct investment (Greenfield venture)*– Directly investing in a foreign country by setting up a separate and independent production facility or office.

Example of global sourcing

Labor-intensive manufactured products produced using low-cost Chinese labor

Call centers staffed with low-cost English speaking workers in the Philippines and India

IT work performed by low-cost programmers in India and Eastern Europe



Advantages and disadvantages of entry modes

Entry Mode	Advantages	Disadvantages
Exporting	Ability to realize location and experience curve economies	High transport costs Trade barriers Problems with local marketing agents
Turnkey contracts	Ability to earn returns from process technology skills in countries where FDI is restricted	Creating efficient competitors Lack of long-term market presence
Licensing	Low development costs and risks	Lack of control over technology Inability to realize location and experience curve economies Inability to engage in global strategic coordination
Franchising	Low development costs and risks	Lack of control over quality Inability to engage in global strategic coordination
Joint ventures	Access to local partner's knowledge Sharing development costs and risks Politically acceptable	Lack of control over technology Inability to engage in global strategic coordination Inability to realize location and experience economies
Wholly owned subsidiaries	Protection of technology Ability to engage in global strategic coordination Ability to realize location and experience economies	High costs and risks

Table 14.1

Advantages and Disadvantages of Entry Modes