



EBU5608 Product Development and Management

Topic 3 – Business Environment and Economic Environment

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Office Hours

- Any questions about the topics, groups, coursework, exam:
 - Talk to your lecture during the **Office Hours**:

Teaching Week/Date	Office Hours	Location
Week 3 – 13 th March	13:50 – 14:35	IS (International School) Building, 105-3
Week 4 – 20 th March		
Week 12 – 15 th May		
Week 13 – 22 nd May		

Today Agenda

- What is the business environment?
- External environment
- Internal environment
- What is the economic environment?
- Microeconomic environment
- Macroeconomic environment



The environment

"The best architects always design a thing by considering it in its larger context – a chair in a room, a room in a house, a house in an environment, an environment in a city plan."

– *Eliel Saarinen, Finnish architect*



Business environment

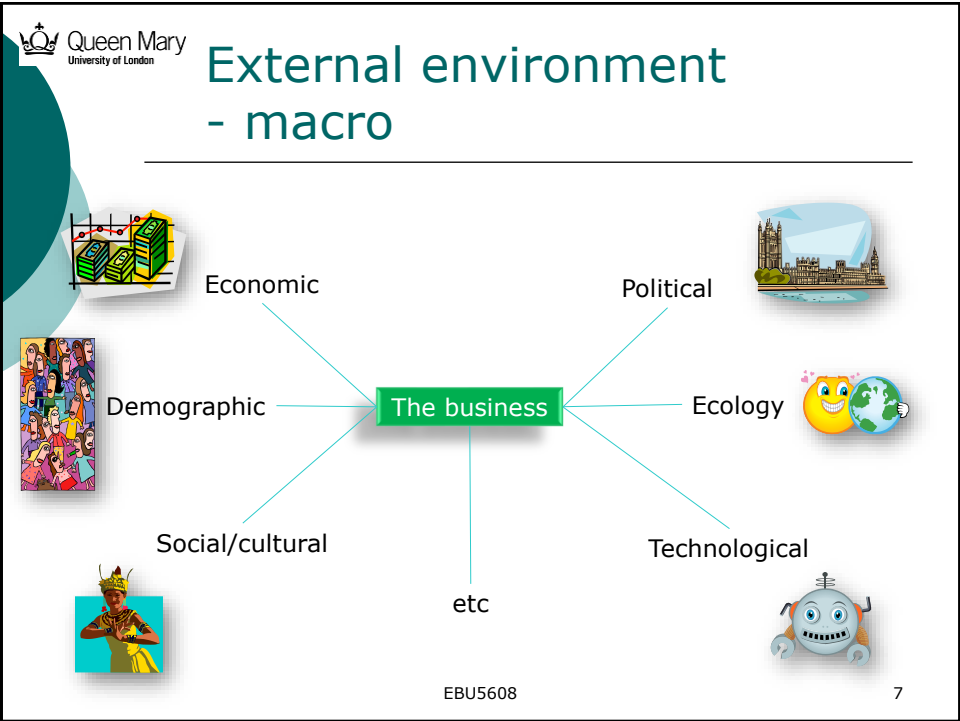
- The business environment – the environment in which the organisation is **located** which contains the **phenomena** which can influence its **behaviour** and **performance**
- “A business organisation can be seen as a system whose performance is influenced by a whole range of phenomena in its environment” [1]
- External influences can be broken into two areas
 - ‘**Macro**’ (*Palmer*), also known as ‘general’ (*Worthington*) and
 - ‘**Micro**’ (*Palmer*) also known as ‘immediate’ (*Worthington*)
- The internal environment of a business must also be considered



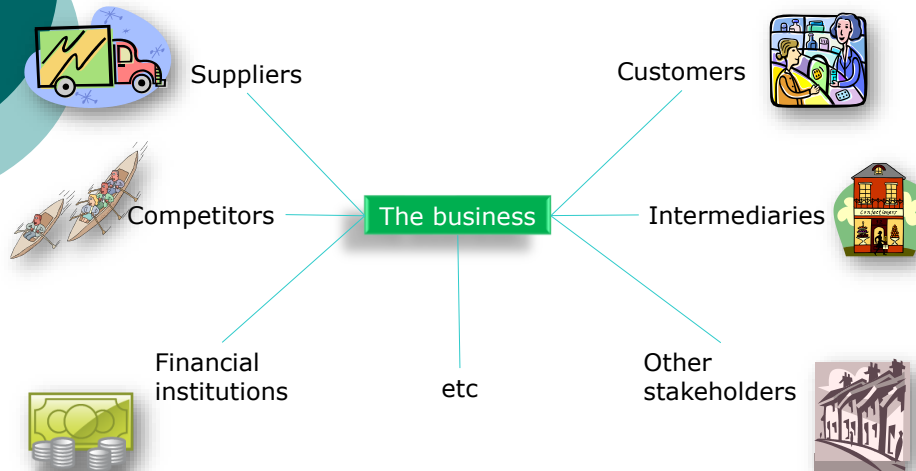
Quick questions to think about

- How would you describe 'The Business Environment' in your words?
- What do you understand by the term 'external environment' when applied to an organisation?
- What do you understand by the term 'internal environment' when applied to an organisation?





External environment - micro



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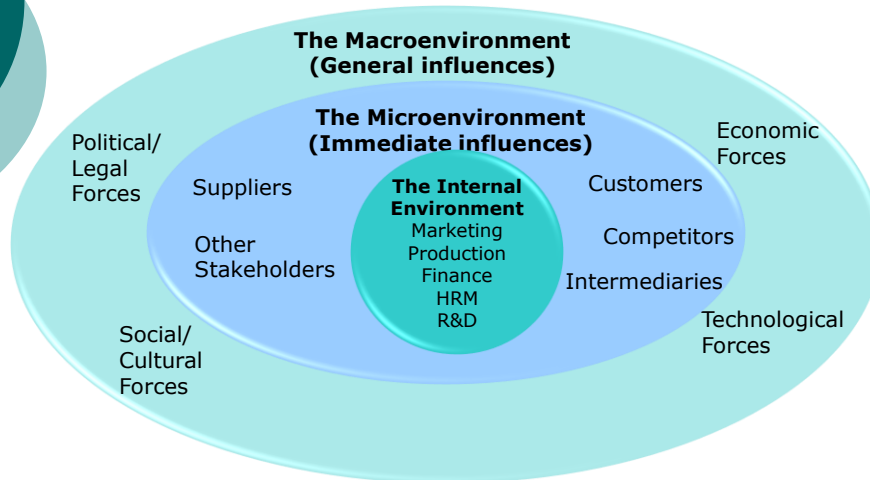
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Internal environment

- Functions that are found **within** the organisation itself
 - Marketing department
 - Production
 - Finance
 - Human Resource Management (HRM)
 - Research and Development (R&D)
 - Etc.



The business environment



[2]

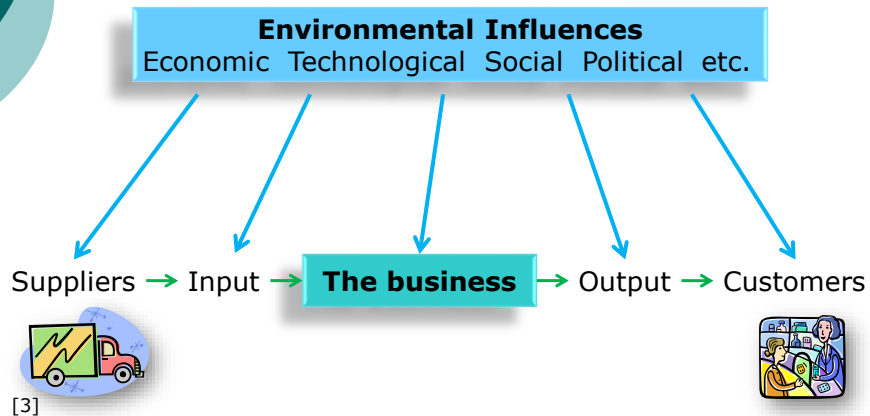
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External environment - the business role

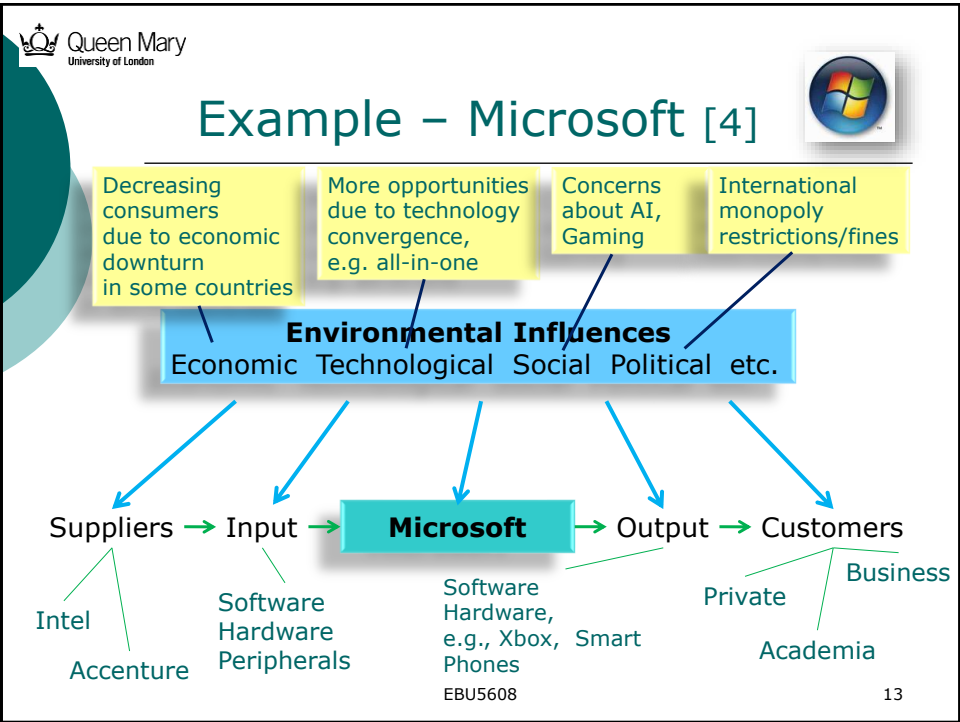
- Ultimately, the role of an organisation is to take the **inputs** from the external environment (both macro and micro) to add **value** to them (this applies to both products and services); often through a **change** process; so that **customers** will be willing to purchase them

External environment (cont.)



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External environment – macro - **Political**

- “Politicians are instrumental in shaping the **general** nature of the external environment as well as being responsible for passing legislation that affects **specific** types of organisation” (*Palmer*)
- Areas included are
 - Government involvement in the working of the **economy**
 - Governments attempt to influence **market** structure and behaviour
 - Stability of the political system can affect whether a country is **attractive** in terms of investment
 - New **legislation** can impact on the production and sales of products and services e.g. law against using a hand-held mobile phone whilst driving in the UK





External environment – macro - **Social and Cultural**

- “Culture is concerned with a set of **shared values** which are passed down between generations” (Palmer)
- With increasing **globalisation** and international business, it is vital that organisations consider the social and cultural values of the countries they do business in, especially if they are not their own
- Issues include
 - Social values regarding **work/leisure balance** which is changing rapidly in many countries
 - Cultural values regarding **religion, food**, equality, capitalism etc.
 - Increasing concern regarding the **planet** – environmental issues



External environment – macro - **Demographic**

- Prediction regarding the **age** and **size** of a population is very important for an organisation so that it can prepare for the demand in terms of its **products** and the availability of **personnel**
- A major issue internationally is the increase in **life expectancy** worldwide and reduction in the number of young people
 - This will affect the number of new **graduates** available for certain **positions**
 - Organisations will have to consider employing **older people**
 - Demand for certain **products** e.g. those aimed at a 'younger' market will reduce, where as those aimed at the 'older' market, often referred to as the 'grey' market will increase
- **Plans** need to reflect these demographic changes





External environment – macro - **Technological**

- Organisations must be aware of the **technological** changes that could impact on their business
- Palmer identifies **four areas** which can be impacted
 - New technology can allow products and services to be **delivered** in new ways, e.g. via the Internet – e-Business/e-Commerce
 - New ways of **distributing** goods and services, e.g. Dell – direct selling and delivery to the consumer
 - The internet has allowed many products to be sold much **more cheaply**, e.g. budget airlines, as the intermediaries are removed and therefore the overheads reduced
 - New **marketing opportunities** have arisen with the increase in the use of the Internet – ‘pop-ups’, banners etc.



External environment – macro - **Ecological/Environmental**

- Growing public concern over the state of the **environment** and the **implications** of this
- Global **warming** and the use of fossil **fuels**
- Increase in the demand for **environmentally friendly** products that do not overuse fossil-fuels in their production or impact on the environment
- **Genetically modified** foods not sold in the UK
- **Organic** goods market continually growing in the UK
- Demand for **locally sourced** products to reduce distribution impact – i.e. reduces the use of oil, petrol etc.
- New European Union laws regarding the **reuse** and **disposal** of electrical equipment and components – WEEE 2006





External environment – macro – **Economic**

- “Businesses need to keep an eye on indications of a nation’s prosperity e.g. on Gross Domestic Product (GDP) and household disposable income” (*Palmer*)
 - **GDP** – “a measure of the value of goods and services produced in an economy during a specified period” (*Palmer*)
 - **Household disposable income** – “It consists of **earnings** from work, **property income** such as interest and dividends, and **pensions** and other social security benefits; income taxes and social security contributions paid by households are **deducted**” [4]



External environment – micro

- The Micro external environment is made up of groups that are more **immediate** to the organisation
- These are often called **Stakeholders**
 - Can be defined as:
 - “**any person** with an interest in the activities of an organisation (e.g. customers, employees, government agencies and local communities)” (*Palmer*)
 - “anyone with an interest in an organisation and who is affected by and can affect performance” (*Worthington*)
 - These groups can **influence** and **impact** the plans of an organisation
 - Consideration of these groups is key to **success**

External environment – micro - **Customers**



- Business must be aware of the changing **demands** and **needs** of customers,
 - (see slides about *Economic Environment*)
- 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,
- No customers = no business.



External environment – micro - **Suppliers**

- “Suppliers provide an organisation with goods and services that are **transformed** by the organisation into value-added products for customers” (*Palmer*)
- “Often suppliers are **crucial** to an organisation’s marketing success” (*Palmer*)





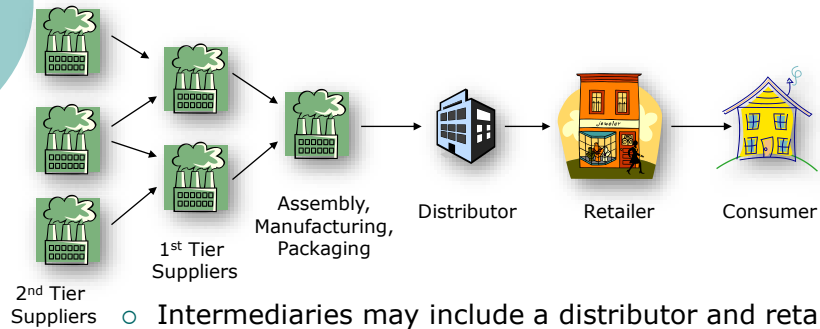
External environment – micro - **Intermediaries**

- “Individuals or organisations who are involved in **transferring** goods and services from the producer to the final consumer” (*Palmer*)
- Examples include **supermarkets** who are the intermediaries between food producers and end consumers
- Traditionally, more intermediaries involved in the channel of **distribution**



Traditional distribution

- Traditional distribution:

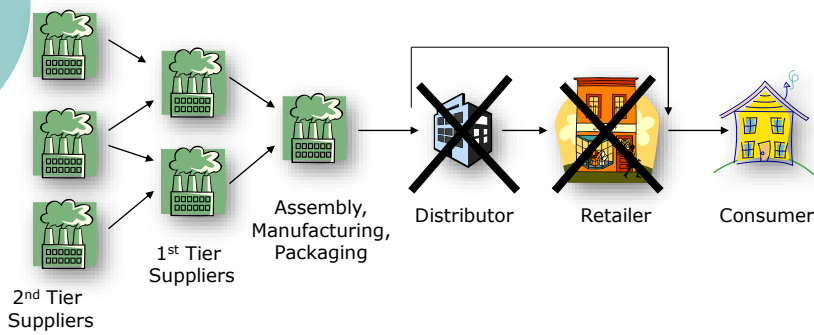


- Intermediaries may include a distributor and retailer
- Organisations that use this structure e.g. Microsoft, Nokia, Apple

[5]

Disintermediated distribution

- Disintermediated distribution



- [6]
- Intermediaries have been removed from the distribution channel, e.g. Dell

External environment – micro - **Competitors**

- All organisations need to be aware of their competitors
- Particularly important in **highly competitive** industries,
 - e.g. mobile phone manufacturers, digital music providers etc.
- Organisations need to be aware of what their competitors **next move** may be so that it doesn't impact on their own business
- Many organisations want to be the **first** to launch **new products** to the market place





External environment – micro - **Financial Community**

- The **majority** of organisations are funded by the financial community
- Can be **banks** who provide loans, banking services, guidance or overdraft facilities to small or privately owned businesses
- May be **shareholders** (private or institutional) who provide investment in PLCs etc
- Investors need to be considered when making organisational **plans**
 - If investors do not agree with the plans they may remove their financial support



External environment – micro – **Local Community**

- This is an external group that is often **overlooked**
- Local communities can have an impact on organisations plans
 - for example many local communities in the UK have stopped mobile phone antennas/**masts** being located near their homes and schools
- More recently plans for '**wind farms**' to provide renewable energy have been blocked by local communities



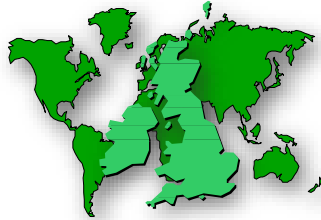


External environment – micro – **Pressure groups**

- Another group often overlooked by organisations
- Can have a huge amount of influence over **image** and ultimately success of an organisation
- Can **you** think of any examples of when pressure groups have impacted on an organisation?
- Can you think of any in **technology** based industries?



Economic Environment



- **Macroeconomics** deals with the way the economy works at international or national level

- **Microeconomics** deals with individual organisations and their customers and suppliers



Microeconomics – formal definitions

Definition:

- “the branch of economics that studies **individual units** e.g. households, firms and industries. It studies the **interrelationships** between these units in determining the pattern of production and distribution of goods and services” [3]
- “the study of an organisation and its customers/suppliers in isolation from the rest of the economy” [Palmer]

Key aspects of microeconomics

Key aspects we need to understand are:

- **Competition**
 - Perfect
 - Imperfect
 - Oligopoly
 - Monopoly
- **Demand & Supply**
- **Price determination**
- **Elasticity**

We will define
these terms
later

Competition

- Competition exists for most organisations operating in a commercial environment
- Ultimately organisations want to **attract customers** away from their competitors
- This is done in a number of ways, including
 - **better products** (differentiation – see Marketing lecture) and
 - **pricing** (see Marketing lecture)
- Competition can also arise between organisations when resources are scarce

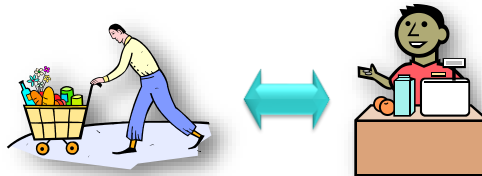


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Markets

- Economists define markets in terms of the interaction between two groups:
 - Those wanting to **buy** products
 - Those wanting to **sell** them
- When studying microeconomics it is important to remember that it is assumed that the **national economy is stable**



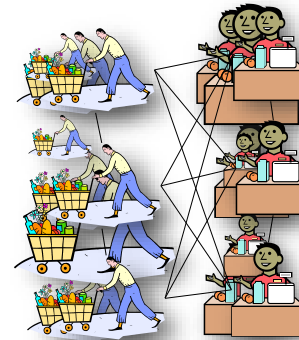
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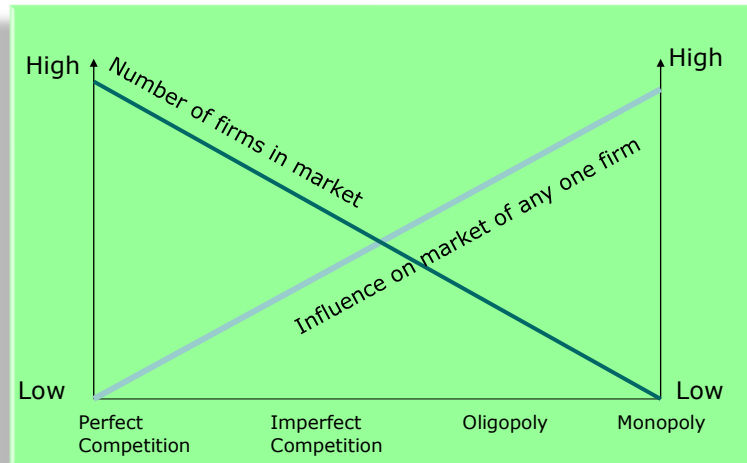
Market structure [4]

The term 'market structure' is used to describe

- The **number** of buyers and sellers operating in a market
- The extent to which the market is **concentrated** in the hands of a small number of buyers and/or sellers
- The degree of **collusion** or **competition** between buyers and/or sellers



The continuum of market structures

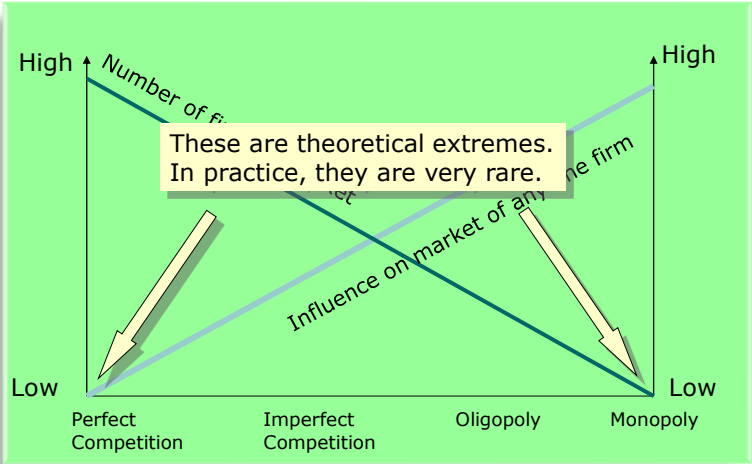


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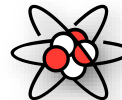
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The continuum of market structures



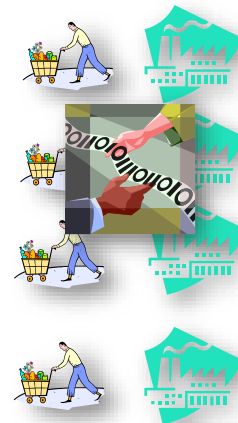
Perfect (or 'atomistic') competition

- Definition:
 - “a market structure in which there are **many firms**; where there is **freedom of entry** to the industry; where all firms produce an **identical product**; and where all firms are price takers” [6]
- **Price takers** – meaning that the only determination of price is the competitive market forces alone
 - i.e. firms are not free to set what prices they would like
- **Simplest** type of market to understand
- Very **rarely** found in practice



Characteristics of a perfect competitive market

- There are a large number of **producers**
 - Each has similar costs and an identical product
- There are also a large number of **buyers**
 - Each buying only a small percentage of the output
- Buyers and sellers are free to **enter** or **leave** the market
- There is a ready supply of **information** about market conditions



Building blocks of competition

- The building blocks of competition are:
 - Demand
 - Supply
 - Price determination

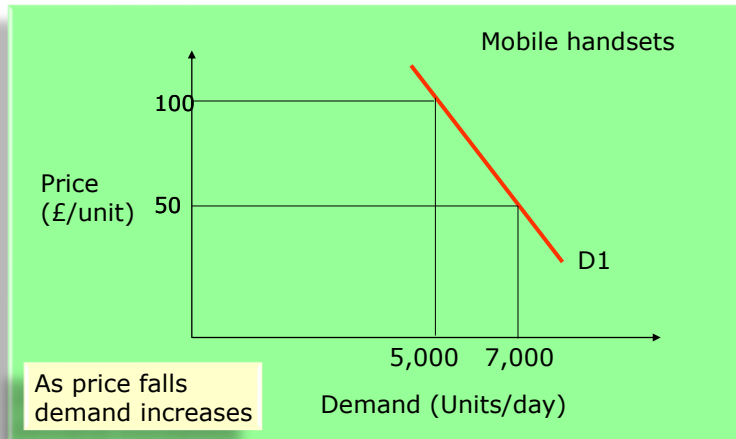
We will look at each of these

Demand

- Definition
 - “ the **quantity** of a product that consumers are willing and able to buy at a specific **price** over a given **period** of time” *Palmer*
- General rules –
 - As the price of a product or service **drops** so the demand will be expected to **increase**
 - So, if the price of a product or service **rises**, then demand is expected to **decrease**



Demand curve

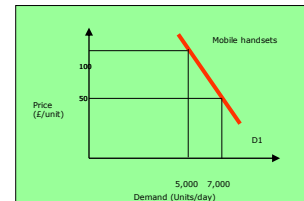


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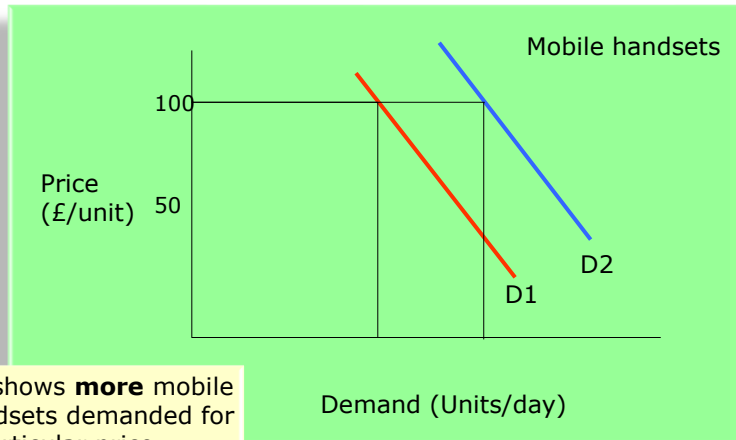
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Demand curve assumptions

- The price of **substitutes** for mobile phones (e.g. landlines, Skype, Apple Watch etc.) will not change
- Consumers will **not** suddenly decide not to buy mobile phones any more!
- When these **assumptions change**, a new demand curve is needed to explain a new relationship between price and quantity demanded



Demand curve – changing assumptions



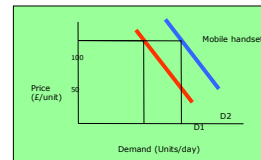
D2 shows **more** mobile handsets demanded for a particular price

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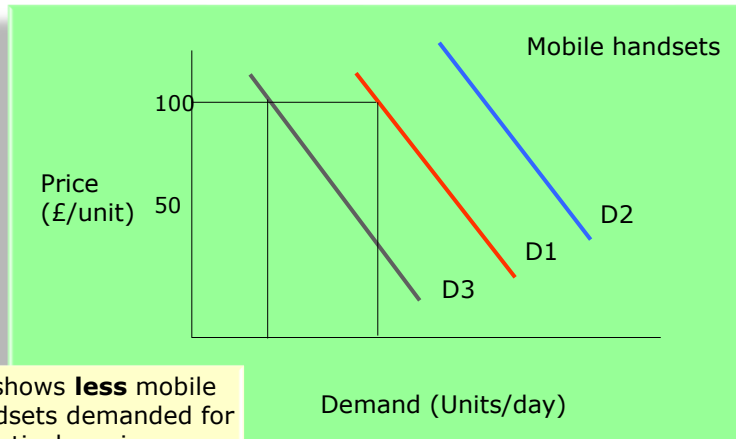
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Upward demand shift - possible causes

- Consumers could have become **wealthier**
- The price of **substitutes** (e.g. MP3 players, Apple Watches) could have increased
- Demand for **complementary goods** (e.g. music downloads, communications)
- Consumer **preferences** may change (eg Apple Watch vs smartphone)
- **Advertising** campaign may increase demand



Demand curve – changing assumptions



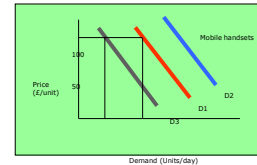
D3 shows **less** mobile handsets demanded for a particular price

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Downward demand shift - possible causes

- Consumers could have become **poorer**
- The price of **substitutes** could have reduced, making them more attractive than mobile phones
- Mobile phones become associated with **health hazards** – e.g. brain damage, especially in children
- An **advertising** campaign for substitute products



Supply

Definition

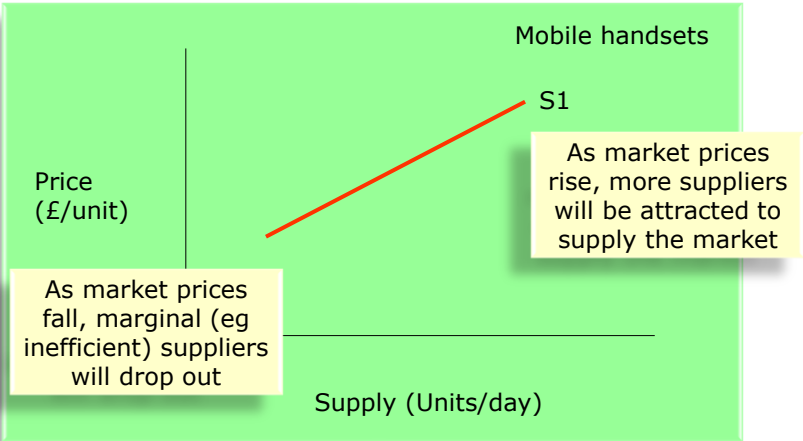
- “the **amount** of a product that producers are willing and able to make available to the market at a given price over a particular period of time” *Palmer*



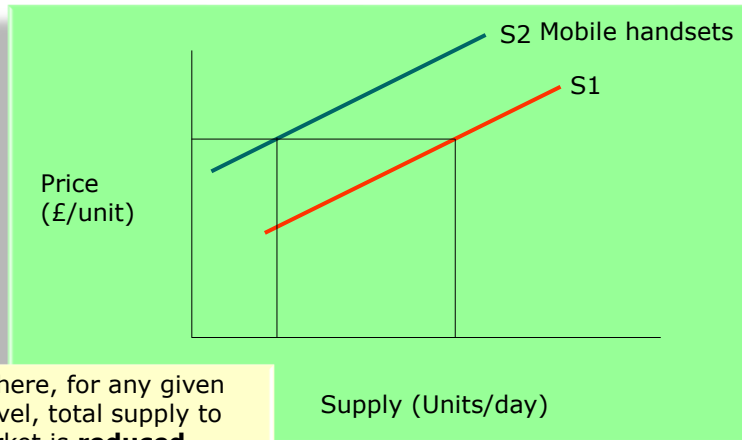
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Supply curve



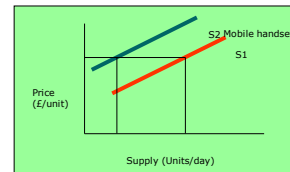
Supply curve – changing assumptions



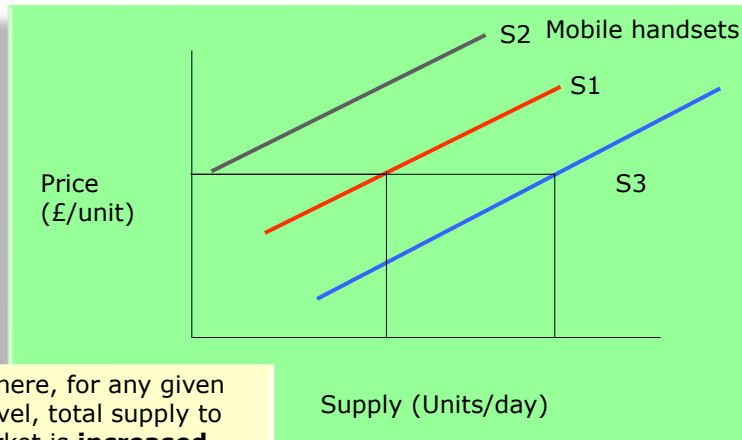
S2 is where, for any given price level, total supply to the market is **reduced**

Reduced supply – possible causes

- **Production** could become more expensive. For any given price level, fewer firms will be willing to supply to the market as they will no longer be able to cover their costs
- **Extraneous factors** (e.g. transport problems) could result in producers having difficulty in getting their produce to the market place
- Governments may impose additional **taxes** on supplies



Supply curve – changing assumptions



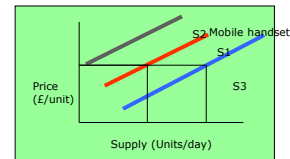
S3 is where, for any given price level, total supply to the market is **increased**

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Increased supply – possible causes

- New **production technology** could result in mobile phones being produced more efficiently
 - suppliers are then prepared to supply more handsets at any given price
- **Extraneous factors** (e.g. loss of other markets) could result in a glut of produce which must be sold and the market is therefore flooded with additional supply
- Governments may give **subsidies**, thereby increasing suppliers' willingness to supply to the market



Price determination

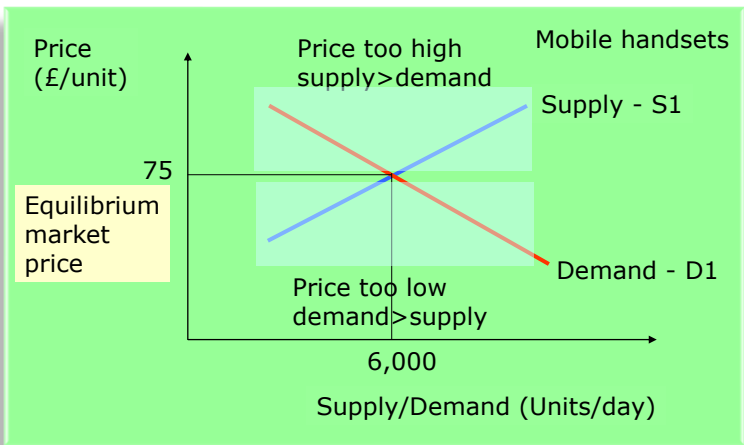
- An examination of the demand and supply graphs indicate that they share common axes
 - Vertical axes refers to the price
 - The horizontal axis refers to the quantity changing hands
- So, It is possible to redraw the original demand and supply lines on the same graph



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Equilibrium market price



Price determination

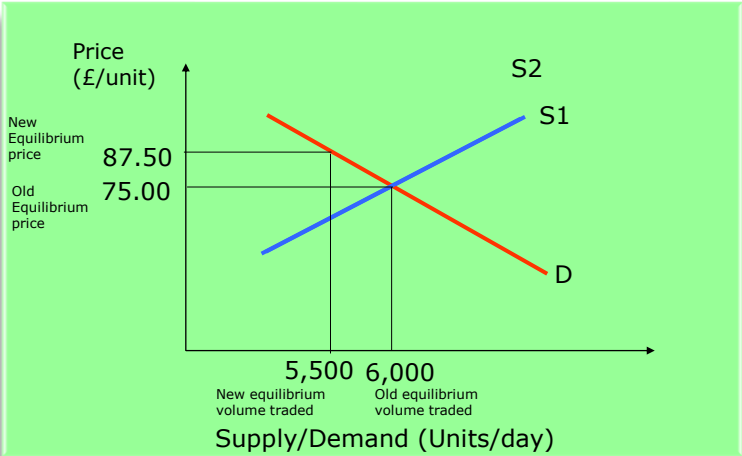
- In perfectly competitive markets, the process of achieving **equilibrium** between supply and demand happens automatically without external intervention
- The market alone determines the 'going rate' for the product – firms are 'price takers'



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Equilibrium market price – effect of decreased supply



Changes in the equilibrium price

- Remember - the market alone determines the 'going rate' for the product – firms are 'price takers'
- Changes in the equilibrium price come about for two reasons
 - Assumptions about **suppliers'** ability or willingness to supply change, resulting in a shift to a new **supply curve**
 - Assumptions change about **buyers'** ability or willingness to buy, resulting in a shift to a new **demand curve**
- New equilibrium prices and trade volumes can be found at the **intersection** of the supply and demand curves



Elasticity of demand

- Definition “the extent to which demand changes in relation to a change in price or some other variable such as income”
- **Price elasticity** of demand refers to the ratio of percentage change in demand to the percentage change in price
- Where demand is relatively **unresponsive** to price changes, demand is said to be **inelastic** with respect to price

$$\text{price elasticity of demand} = \frac{\text{change in demand (\%)}}{\text{change in price (\%)}}$$

Learn more:

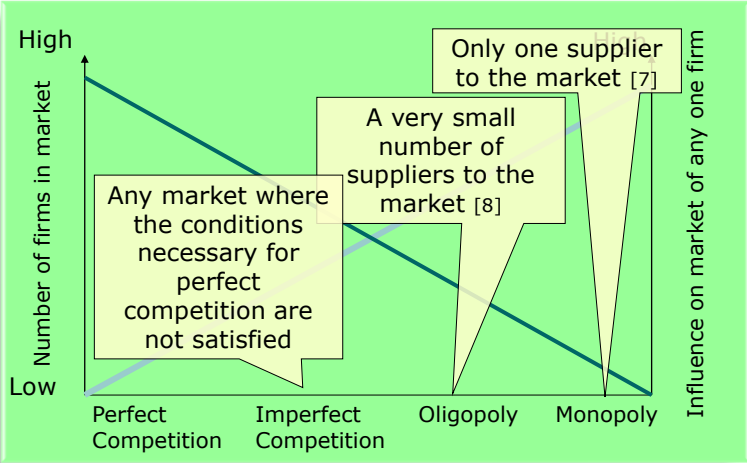
<http://www.investopedia.com/terms/p/priceelasticity.asp>

Elasticity of supply

- Definition
 - “a measure of the responsiveness of supply to changes in price” Palmer
- If suppliers are **relatively unresponsive** to an **increase** in the price of a product, the product is described as being **inelastic** with respect to price
- If producers **increase** production substantially as **prices rise**, the product is said to be **elastic**

price elasticity of supply=	change in supply(%)
	change in price(%)

Other forms of competition



Summary

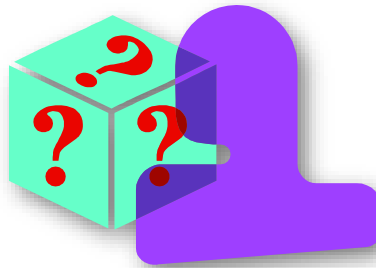
Business Environment

- External Environment
 - **Macro**
 - **Micro**

Economic Environment

- Microeconomics
 - **Competition**
 - **Market**
 - **Demand & Supply**
 - **Price determination**
 - **Elasticity**

Questions?



Go to www.menti.com to post your questions



Directed Reading

- Reading
 - ***The Business Environment, A Global Perspective***, Thompson, E., Worthington, I., Britton, C. (2023) 9th Edition, Pearson, ISBN 1292417846.

Chapters 1 and 15



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References

1. Adapted from *The Business Environment*, A. Palmer, (2009) 6th Edition, McGraw-Hill, pg.4
2. Adapted from *The Business Environment*, A. Palmer, (2009) 6th Edition, McGraw-Hill, pg.5
3. Diagram taken from Palmer, pg.4
4. <http://miranda.sourceoecd.org/vl=312866/cl=35/nw=1/rpsv/fa ctbook/10-03-02.htm>
5. Adapted from e-Business Technologies, Craig Van Slyke, France Belanger, 2003, Wiley, pg. 25
6. .. Pg. 24
7. Mintzberg, H (1989), *Mintzberg on Management*, Free Press, New York, NY.

