

Strategic Management

Unit III

External Environment Analysis

POST RAJ POKHAREL
M.Phil. (TU) 01/2010)

External Environment Analysis

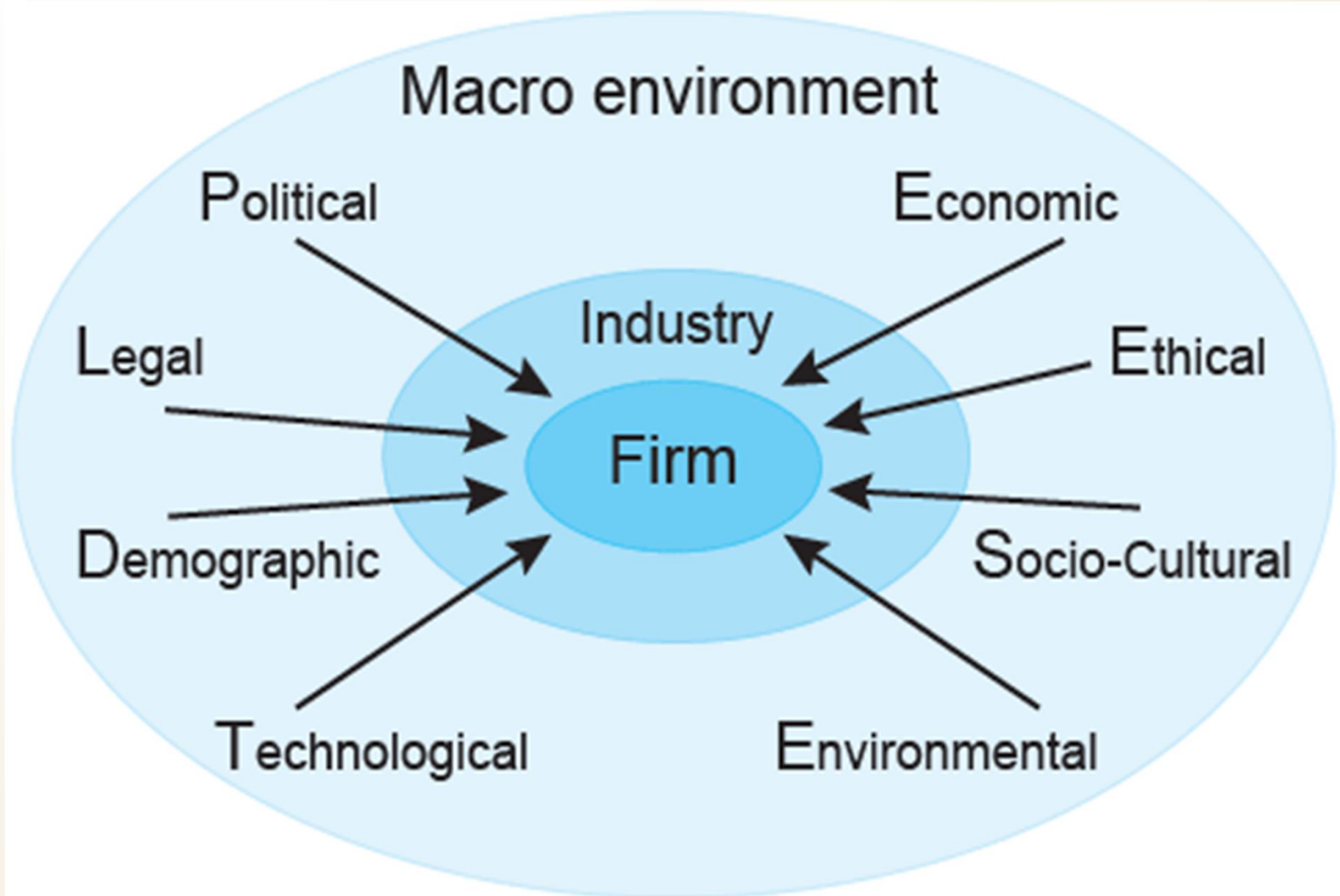
PEST analysis – an analysis of the political, economic, social and technological factors in the external environment of an organization, which can affect its activities and performance

Additional: i.e. International envt.

Strategy

PEST or PESTEL analysis is a simple and effective tool used in situation analysis to identify the key external (the macro environment level) forces that might affect an organization. These forces can create both opportunities and threats for an organization. Therefore, the **aim** of doing PEST is to find out the **current factors affecting** a company, what **changes are going to happen in the external environment** and to **exploit those changes or defend against** them better than competitors would do. The outcome of PEST is an understanding of the overall picture surrounding the company.

Macro environment forces affecting a firm (PEST including legal, environmental, ethical and demographic forces)



Political Factors

- **Political System**
- **Political philosophy**
- **Frequent changes in the government**
- **Government action plan (changes)**
- **Government stability and likely changes**
- **Bureaucracy**
- **Corruption level**
- **Tax policy (rates and incentives)**
- **Freedom of press**
- **Regulation/de-regulation**
- **Trade control**
- **Import restrictions (quality and quantity)**
- **Tariffs**
- **Competition regulation**

How do political factors influence the strategy of an organization ?

- Political parties, regard as pillars of democratic system : You can relate it connecting parties in the govt. and opposition parties too....
- .. Local government (like: municipality, metropolitan city ...) role on business growth ...
- Govt. role on strengthening private sectors

Dipesh:

Gaurav: - Current stable govt. (decision on tax rate, import tax)
- New normal business opportunities (online, e-commerce, ...)

Jenisha:

- The political factor effects on organization by 1. Impact on economy 2. Changes in regulation 3. Political stability 4. Mitigation of risk .

Jyoti:

- Upcoming govt. rules, regulations have strong impact on business
- Power in political leaders
- Govt. tax rate decision
- Political decisions on socio-cultural, use of technology

Political Factors

- Government involvement in trade unions and agreements
- Environmental Law
- Education Law
- Anti-trust law
- Discrimination law
- Copyright, patents / Intellectual property law
- Consumer protection and e-commerce
- Employment law
- Health and safety law
- Data protection law
- Laws regulating environment pollution

How do "Economic Factors" influence the strategy of an organization

- Manish
- Manisha: Lead role
- Nikita
- Narayani
- Economic system:
 - **Free market economy**: based on private sector ownership of the factor of production
 - **Centrally planned economy**: ...public..
 - **Mixed system**: co-existence of both private and public sectors
- Economic policies:
 - **Monetary policy** (money supply, interest rates, credit availability, exchange rate)
 - **Fiscal policy**: budget, taxation
 - **Industrial policy**
- **Economic condition**: GDP, Per capita income
- Growth rates
- **Inflation rate**
- **Unemployment** trends
- **Labor costs**
- **Stage of business cycle**

Economic Factors

- Credit availability
- Trade flows and patterns
- Level of consumers' disposable income
- Monetary policies
- Fiscal policies
- Price fluctuations
- Stock market trends
- Weather
- Climate change

How do "Socio-Cultural Factors" influence the strategy of an organization?

Nishal

Pawanee: Lead role

Prafullata:

Prashant

- Health consciousness
- Education level
- Attitudes toward **imported goods and services** (imported vs. local goods for eg. Apple from Mustang Vs. India)
- Attitudes toward work, leisure, career and retirement
- Attitudes toward product quality and customer service
- Attitudes toward saving and investing
- Emphasis on safety
- Lifestyles
- Buying habits

Socio-Cultural Factors

- Religion and beliefs
- Attitudes toward “green” or ecological products
- Attitudes toward and support for renewable energy
- Population growth rate
- Immigration and emigration rates
- Age distribution and life expectancy rates
- Sex distribution
- Average disposable income level
- Social classes
- Family size and structure
- Minorities

Prasiddha
Pratima
Pushpa
Rachin

Rachana
Ranju
Ravi
Ruchi

Sabina
Samikshya
Bishal (Pok & Timilsina)

Technological factors

- Basic infrastructure level
- Rate of technological change
- Spending on research & development
- Technology incentives
- Legislation regarding technology
- Technology level in your industry
- Communication infrastructure
- Access to newest technology
- Internet infrastructure and penetration

Environmental factors

- Weather
- Climate change
- Laws regulating environment pollution
- Air and water pollution
- Recycling
- Waste management
- Attitudes toward “green” or ecological products
- Endangered species
- Attitudes toward and support for renewable energy

Legal factors:

- I. Industrial laws, labor act
- II. Consumer protection and e-commerce

- III. Employment law
- IV. Health and safety law
- V. Data Protection

Technological Factors

- Basic infrastructure level
- Rate of technological change
- Spending on research & development
- Technology incentives
- Legislation regarding technology
- Technology level in your industry
- Communication infrastructure
- Access to newest technology
- Internet infrastructure and penetration

Environmental Factors

- Weather
- Climate change
- Laws regulating environment pollution
- Air and water pollution
- Recycling
- Waste management
- Attitudes toward “green” or ecological products
- Endangered species
- Attitudes toward and support for renewable energy

Legal Factors

- Anti-trust law
- Discrimination law
- Copyright, patents / Intellectual property law
- Consumer protection and e-commerce
- Employment law
- Health and safety law
- Data Protection

Ethical

- Ethical advertising and sales practices
- Accepted accounting, management and marketing standards
- Attitude towards counterfeiting and breaking patents
- Ethical recruiting practices and employment standards (not using children to produce goods)

Demographic

- Population growth rate
- Immigration and emigration rates
- Age distribution and life expectancy rates
- Sex distribution
- Average disposable income level
- Social classes
- Family size and structure
- Minorities

Individualism (Sayal and Samjhana)

- ◆ The tendency of people to look after themselves and their immediate family only
- ◆ In an individualist culture, success is measured by how far one stands out from the crowd. Eg: self-made millionaires, employees of the month, standing out...
- ◆ USA, UK, Australia with individualism philosophy

Collectivism

- ◆ refers to people regarding themselves as part of a group. Working together concept like in Japan and France
 - ◆ In a collectivist culture, success is measured by one's contributions to the group as a whole. Eg: loyalty to company or country
-

Totalitarian Vs Democracy

Democracy: (Shikshya and Shiva)

- Power is assigned on people.
- Governed by elected representative
- Multiparty system exist
- Fundamental rights are ensured
- Private sector is regarded as the crucial part of development of the country.

Totalitarian अधिनायकवादी:

- = Exercised dictatorial control over many aspects of life
- = Govt. attempts to control the whole economy.
 - communist totalitarianism
 - theocratic धर्मशासित totalitarianism
 - Tribal आदिवासी totalitarianism

Common Law Vs. Civil Law

(Shiwa and Sonu Suwas)

Common Law

- Created by Law case (i.e. **judges**) through the decision made by court.
- The courts are given the main task in creating the law.
- Dominated by judicial decisions
- A bottom-up approach to principles.
- Judges play referee role
- Lawyers debate and oppose
- US, England, India..

Civil Law

- A codified system and it is developed by **Legislator**.
- The courts should apply the law.
- Statute (act) and code are the supreme source of jurisdiction.
- A top-down approach to principles.
- Judges play director/examiner role.
- Lawyers advise and inform
- East Asian, Eastern countries

Determinants of Culture

Social Structure: Nepalese structure, American, European, Indian

Religious and Ethical System: System of shared beliefs and rituals.

Hinduism, Christianity, Buddhism, Islam

Language: Language diversity in society. English as a major language.

Language is being the expression of culture

Education: Educated and skilled manpower dictates economic performance of the country.

State of technological change

1. **Manual Technology:** Traditional technology, simple tools are used, production volume is low but overall cost of production is higher.
2. **Mechanised Technology:** Use of Machine, investment in plant and machinery, quality improves, cost becomes lower
3. **Automated Technology:** Self controlled machines, production and productivity is higher, requires few employees
4. **Computerised technology:** Used computer based sophisticated machine, Digital technology is used, few employees requires
5. **Robotized technology:** Robots in place of human being, used mostly in hazardous conditions. Productivity and quality are superior.

Impact of international factors

1. **Increased Competition** : Competition with MNCs
2. **High Complexities:** Competition at international level
3. **A global reallocation of industries:** Production and marketing in different countries using cheap factor of production.
4. **Expansion in world trade volumes:** Global trade of materials, products and services
5. **Growth in merger and acquisitions trends**
6. **Movement of capital and technology**
7. **An increased power in trade organizations:** WTO, World Bank etc. give pressure and also promote
8. **Growth of lifestyles:** western culture, fashion
9. **International cooperation:** Interdependence

Impact of Ecological Factors on Business

- **Abundance of natural resources enable business to acquire input needed**
- **More regulator compliance regarding envt. Issues**
- **Environment protection issues**
- **Energy Supply to the business**
- **Compliance of international agreement signed by the government**
- **Concern for green production**
- **Challenges of using the natural resources efficiently**

Industry and Competitive Analysis

Customer Profiles

Developing a profile of a firm's present and prospective customers improves the ability of its managers to plan strategic operations.

Suppliers: In assessing a firm's relationships with its suppliers, several factors other than the strength of that relationship should be considered.

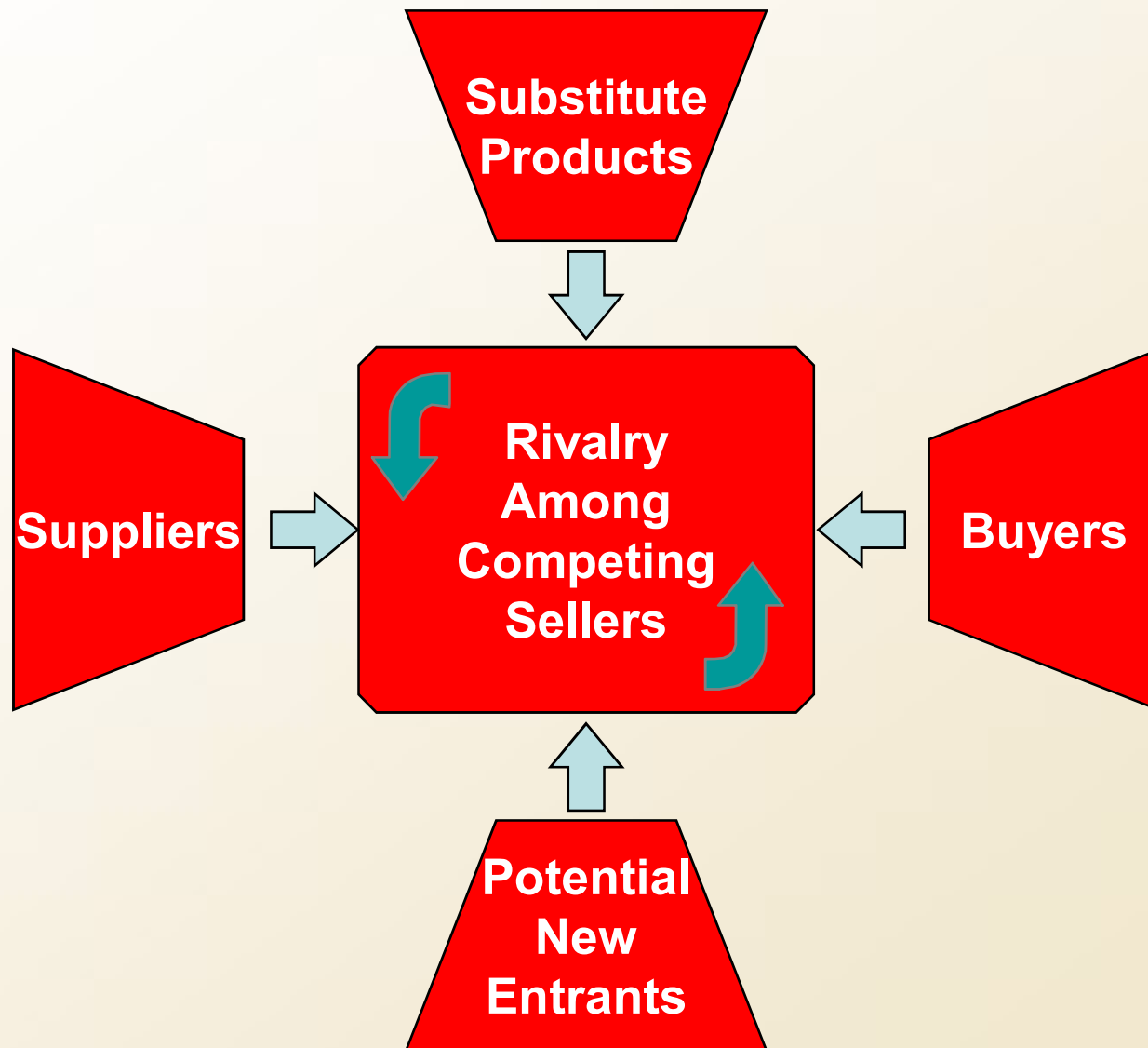
1. Are the suppliers' prices competitive?
2. Do the suppliers offer attractive quantity discounts?
3. Are the suppliers competitive in terms of production standards?

Creditors

With regard to its competitive position with its creditors, among the most important questions that the firm should address are the following:

- Do the creditors perceive the firm as having an acceptable record of past payment?
 - A strong working capital position? Little or no leverage?
 - Are the creditors' loan terms compatible with the firm's profitability objectives?
 - Are the creditors' able to expand the necessary lines of credit?
-

The Five Forces Model of Competition: A Key Analytical Tool (Vivek and Subas)



Industry and Competitive Analysis

1. THREAT OF NEW ENTRANTS : New Entrants bring new capacity, a desire to gain market share. These desires of a new entrant are threats to an established corporation. The threat of entry depends on entry barriers.

Barriers to Entry

- Absolute cost advantages
- Access to inputs
- Government policy
- Economies of scale
- Capital requirements
- Brand identity
- Switching costs
- Access to distribution
- Expected retaliation (revenge)

Industry and Competitive Analysis

2. Bargaining Power of Buyers:

Bargaining power of buyers refers to the ability of the industry's customers to **force down price, bargain for higher quality or more services** and play competitors against each other. If the customers groups are powerful, there will be buyers market and the producer's profile will suffer.

3. THREAT OF SUBSTITUTES

Substitute products or services are those which may appear to be different but can satisfy the same needs as another product.

If switching costs are low, substitute may have strong effect in the industry.

4. Bargaining Power of Suppliers:

refers to a situation where **suppliers force the firms to pay higher prices**. They affect an industry through their ability to raise price or reduce quality of purchased goods. Bargaining power of supplier be there if:

- Substitutes are not really available (electricity)
- Monopoly supplier
- The product is unique and important input to the buyer's business

5. Rivalry Among Existing Firms:

- Rivalry among existing competitors takes the similar form of jockeying for position-using tactics like price competition, **advertising battles**, **product introduction** and **increased customer service** or warranties.
- Competitive moves by one firm have noticeable effects on its competitors
- Eg. Ok soap and puja soap make rivalry through advertisement as “OK Matra le hudaina, malai safa chahiyo” and “Puja le matra kehi hudaina”

STRATEGIC IMPLICATIONS OF THE FIVE COMPETITIVE FORCES

Competitive environment is unattractive when:

- **Rivalry is very strong**
- **Entry barriers are low**
- **Competition from substitutes is strong**
- **Suppliers & customers have considerable bargaining power**

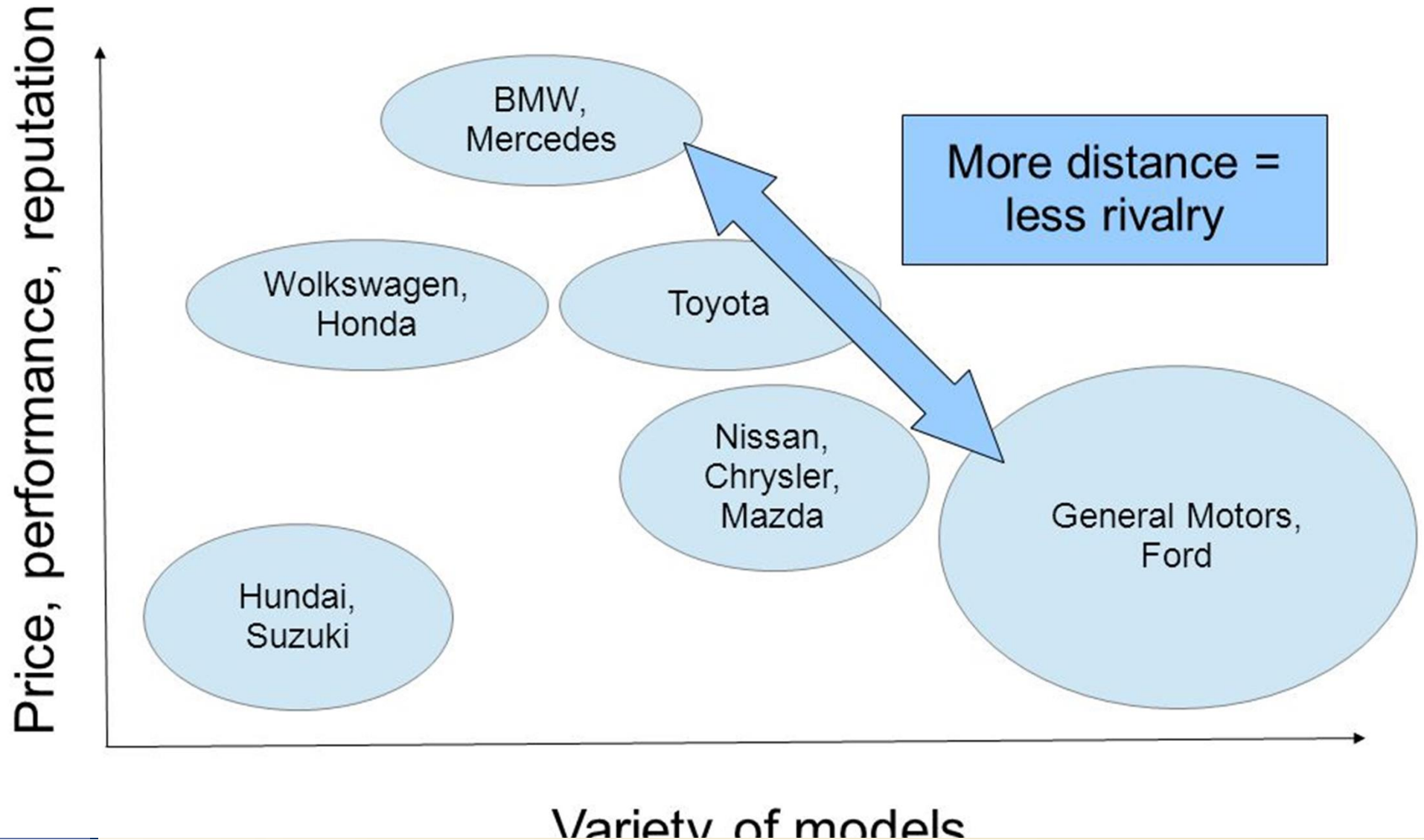
Strategic Group Map

- A strategic group consists of **rival firms** with **similar competitive strategies** and **positioning in an industry**
- A strategic group map displays **clusters of groups within an industry** based on variables that you choose for their strategic significance.

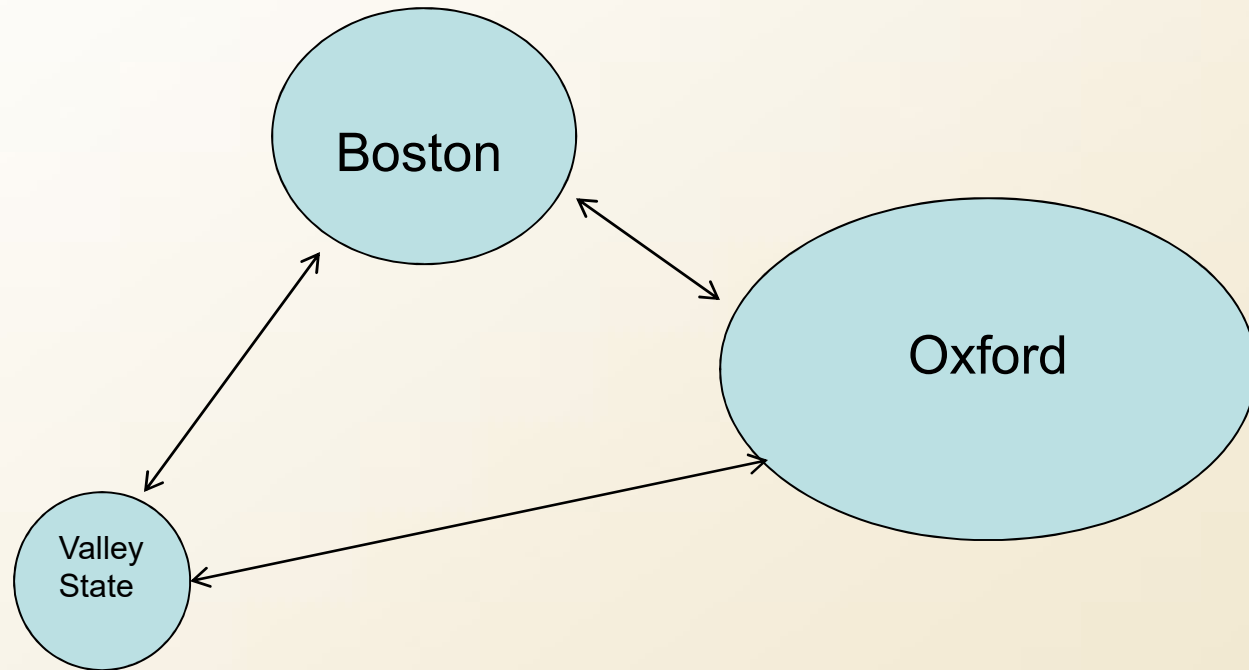
Some Strategic variables

- Specialization
- Brand identification
- Distribution channels
- Product quality
- Vertical integration
- Cost position
- Service
- Price point

Example: strategic group map of the automotive industry



Price, performance, Customer's choice



No. of Disciplines (Programs)

Monitoring competition

Why do organizations need to monitor competition ?

- Many organizations (MNCs), they do have **their own internal monitoring unit** that will be confined to monitor competition within the industry.
- Rivals... competitive moves... (always monitor).... Impact.. (short-run, long run).... Sensitivity.. (low, medium, high)
- Counter (....)
- In order to avoid the potential losses...
- To predict rivals potential moves...(....)... counter....
- To stand out of the competition
- To give the track what they do....
- Boost for innovation
- Motivate to work hard.....
- Determine to analyze the Opportunities and threats... (Opportunities... exploit,..... Threats... Avoid...)
- Application of economic principle... matching demand and supply based on competitors capacity.

Monitoring Competition

- Companies must monitor competition in order to make intelligent marketing decisions based on how competitors operate.
- Marketing myopia (Shortsightedness) is common, and refers to situations where companies fail to properly identify the extent of their competition.
- Some companies that are giants in their industry, such as Coke and Pepsi, have been competing for so long that the result is a stalemate (draw, tie), despite billions spent by each on [marketing](#).
- Competitive intelligence is a legal business practice, focused on the external environment, that involves gathering intelligence and turning it into useful information for business decisions.

Questions

Linking Strategy with Ethics and Social Responsibility

- ***Business ethics*** involves applying general ethical principles and standards to business activities, behavior and decisions.
- There should be a ***link between*** a company's ***efforts*** to ***execute*** a winning ***strategy*** and its ***duties*** to
 - ✓ Conduct activities in an ethical manner?
 - ✓ Demonstrate socially responsible behavior by being a committed corporate citizen?
 - ✓ Limit its strategic initiatives to those meeting needs of consumers without depleting resources needed by future generations

Examples of Ethical Norms and Social Responsibility

- Honesty
- Trustworthiness
- Respecting the rights of others
- Avoiding unnecessary harm to Workers

Social responsibility calls for companies to strike a ***balance*** between

1. Its ***economic responsibility*** to shareholders
2. The ***legal responsibility*** to comply with the laws of the countries where it operates
3. The ***ethical responsibility*** to abide by society's norms, and
4. The ***discretionary philanthropic (charitable) responsibility*** to meet the unmet needs of society
5. Environmental Responsibility: Being responsible with the environment without having any harmful effects to the envt.

Economic responsibilities

- are the most basic social responsibilities of business.
- Economic responsibilities are the duty of managers, as agents of the company owners, to maximize stockholder wealth.
- The essential responsibility of business is assumed to be providing goods and services to society at a reasonable cost.
- In discharging its economic responsibility, the company emerges as socially responsible by providing productive jobs for its workforce, and tax payments for its local, state, and federal governments

Legal responsibilities

- **reflect the firm's obligations to comply with the laws that regulate business activities**

Ethical responsibilities

- **reflect the company's notion of right and proper business behavior**

Discretionary responsibilities

- **are those that are voluntarily assumed by a business organization. These responsibilities include public relations, good citizenship, and full corporate responsibility**
- **Environmental responsibility: Orgn activities**