

## C

## Examine the environment in which businesses operate

The term 'environment' has multiple features. During this unit, you will have recognised how the economic environment has influenced businesses, for example retail outlets and businesses closing down due to the recession. Some shops such as high-end brand retailers, pound shops, technology, gambling sites and pawn brokers have thrived, while others have had to close down due to lack of sales.

### External environment

The external environment impacts on businesses and is comprised of many factors. These factors are often used by businesses to analyse how and why they will be successful or unsuccessful – this analysis is known as 'PESTLE' which stands for:

- Political
- Economic
- Social
- Technological
- Legal
- Environment.

#### Political

Government support, such as monetary grants or promotion, can inject considerable enthusiasm into new business ideas such as wind farms and solar panels. Although grants are time constrained, you have probably noticed both of these examples springing up around the country. Of course, there is a motive for government support according to government policy and promises.

The government website regularly updates with announcements. You may also recall the example of government bail-out when Northern Rock and the Royal Bank of Scotland (RBS) were in financial trouble. However, there are plenty of business owners who claim government do little to support their sectors.

#### Membership of trading communities

Businesses can benefit from being members of trading communities. These are often sector related, such as retail, health, publishing, tourism, catering, etc. and provide networking opportunities, advice, news and opportunities to buy or sell equipment, services, training, etc.

#### The European Union

The European Union (EU) is another form of trade association. The EU promotes itself as 'the best way to realise our global future'. Being a member of any trade association gives credibility in the eyes of the customer, just as you would expect a gas fitter or service engineer to be Gas Safe registered. It can be seen to open doors to opportunities that are closely guarded or seen as exclusive.

#### Economic

Economic factors greatly influence the success or demise of businesses. As you know, the recession has been blamed for the closure of thousands of high street stores. These businesses may have failed to take into account economic needs, competition and technological advancements. You have also learned about the success of new or diversified businesses, informed by government initiatives such as solar panels and air source heating.

#### Key term

**Retail** – the sale of goods, usually on a small scale, directly to the public for consumption rather than resale.

#### Key term

**PESTLE** – political, economic, social, technological, legal, environmental.

#### Link

Unit 19: Pitching for a New Business Learning aim B, also considers PESTLE analysis.

#### Research

Research examples of businesses that complain of too little government intervention. Can you explain why this might be?

### Key term

**Fiscal** – relates to government revenue, for example from taxes.

### Fiscal

**Fiscal** policy affects every type of business. It is government controlled and dictates levels of taxation based on the cost of borrowing. This is how the government generates its income and decides its budget. Every business owner and its decision makers cannot ignore changes to fiscal policy.

### Research

Can you find any examples of the effect of fiscal policy on small businesses? In groups, see if you can find any examples of the effect of fiscal policy on large businesses.

### Monetary and other government policies

Monetary policy affects everybody as it relates to the value of our currency and interest rates. This policy is determined by the government and decisions about how to meet expectations are controlled by the Bank of England and the Monetary Policy Committee (MPC). All businesses are affected by decisions made by the MPC.

### Supply side policy

These policies aim to improve productivity and produce economic growth. Ways to achieve this include reducing taxes, such as income tax in 2014, and reducing corporation tax (the tax paid by private and public limited companies) in 2015.

### Economic growth

The government is striving to grow the economy so that the UK does not return to a recession. If you imagine that the government is you, look at your own financial circumstances. Calculate how much money you have coming in and how much you expect to spend. What is left? Everyone needs money to survive, so you have to ensure that you do not spend more than you can afford or else you have to find ways of generating more income.

The country is no different and the government has to find ways to grow our economy at international, national, regional and local levels according to opportunity and need, for example, building projects, the Help to Buy scheme, and increasing job and training opportunities.

### Exchange rates

Another factor influencing the success or failure of businesses and our economy is exchange rates. These can fluctuate greatly and how our UK currency, pounds sterling, compares with the US dollar, euros and the Japanese yen is analysed daily. Each of these currencies is influential in the UK's purchasing and selling power globally, although not exclusively, depending on the countries trading. Exchange rates are influenced by many factors such as unemployment, **inflation** and other complex factors such as the activity on the stock exchange and speculation. In other words, how much our currency is worth when trading with other countries. You may well have experienced fluctuations if you have ever bought foreign currency to go on holiday.

Imagine how fluctuating exchange rates impact on the travel industry. Airlines, rail and logistics companies are just a few of the businesses which must try to forecast their income while anticipating the costs of running the business, for example vehicle maintenance, fuel costs and the predicted number of passengers, etc.

Exchange rates are partly responsible for fluctuating oil prices. For example, in the summer of 2015 the price of petrol was 30p per litre less than two years previously. Consider what other factors might have influenced this reduction.

### Key term

**Inflation** – a general increase in prices and fall in the purchasing value of money.

## Social

### Attitudes to saving

Banks and the government rely on people to save money. The money saved is used to boost the economy as it is borrowed by businesses and householders for mortgages, etc. However, with less money in people's pockets (disposable income) and interest rates remaining at a low rate previously unheard of, banks and government are finding it difficult to encourage saving. This is why the government has introduced initiatives such as increasing the amount that can be invested in **ISAs** and premium bonds.

#### Key term

**ISA** – individual savings account (a good way to save money without having to pay tax on it).

### Spending and debt

Changes to spending habits influence the types of business that can start up and expand. For example, recent times have seen an increase in pawn brokers, gambling sites, pound and charity shops, payday lenders and businesses like Bright House which offer weekly payment schemes. (Charity shops do not have to pay business rates.) By contrast, pubs, building contractors, clothing, furniture and photography stores, etc are struggling to survive.

### Social responsibility requirements

A sense of social responsibility also influences spending habits. For example, with the increase of charity shops people can make their money go further while also helping a good cause. Consumers are being encouraged to consider ethical matters and the consequences of their actions much more. According to the Office of National Statistics (ONS), sales of tobacco and alcohol have dropped while the biggest growth area is recreation and culture, although this includes mostly electronic goods.

### Change

Changes, for example to the **demographic trends**, can have a significant influence on business. For example, in Slough, Berkshire, there is a wide diversity of ethnicity which has led to new businesses catering for specialist foods, local government services and training opportunities. In Kent, there are large Nepalese settlements while, in other areas of the UK, immigrants from Somalia are building communities. These are just a few of the factors influencing our businesses.

#### Key term

**Demographic trends** – the characteristics of a country's population.

### Consumers' tastes/preferences

Changes to consumers' tastes or preferences also influence the nature of businesses. For example, the food industry is now strongly influenced by foreign foods and recipes, while fast food remains very popular. There have been increases in restaurants such as burger chains and 'simple' food restaurants: for example, one London restaurant is dedicated to grilled cheese sandwiches and one to just cereal.

However, tastes can also remain unchanged – reports from the Foreign and Commonwealth Office (FCO) reveal that our favourite takeaway food is still traditional fish and chips.

#### Research

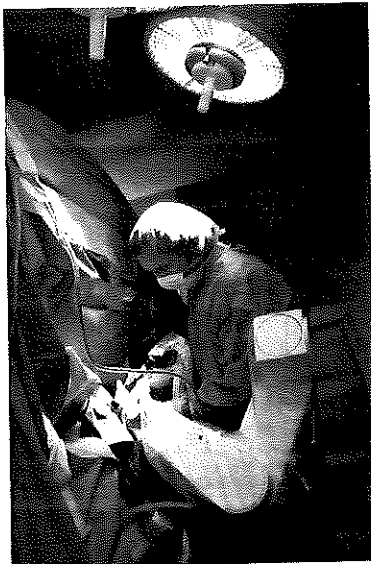
How many different nations are represented by fast food outlets and restaurants in your local area?

### Discussion

Discuss your research findings with your peers. How do your findings compare and how do you think these businesses reflect the local population? Now look at your nearest city. Are your findings different? Or do they reflect the same as your local area?

## Technological change

Technological advancements and changes influence businesses and create opportunities for new businesses. During the mid 1980s, businesses started to introduce fax machines, and electronic typewriters and word processors became more commonplace. Early adopters used computers although few employees were skilled in their use. By the mid 1990s, this led to a change in the training courses and qualifications being offered to meet demand and public interest; by the early 21st century internet usage was almost a necessity for businesses to function.



► Robotic surgery taking place

### Automation

Automation has been in existence for a long time, with robots building cars, but, if traced back, it could be claimed that automation appeared as early as the 8th century. The first programmable robot was developed in 1954 and robots were first introduced into the motor industry in 1962.

Of course robots are not the only form of automation. Today we take it for granted that we spend much of our everyday lives interacting with some form of automation. This includes buying tickets, setting alarm clocks, timers for heating, water, cooking, programming washing machines, etc. Even certain surgical procedures or treatments are carried out to some extent by automation.

### Improved communications

Technologically, improved communications have changed the way businesses operate and especially how they are structured, for example more people can now work from home or remotely. This has led to WiFi connections being provided on trains, in stations, on ships, in aeroplanes, in restaurants, coffee shops, shopping centres and open spaces. All this encourages us to take work on holiday or maximise travel time into business time.

New businesses are increasing rapidly and some innovative ideas may even operate from a 'back bedroom' - these are sometimes based on a new craze, such as the aluminium scooter in the mid 1990s. However, unless business owners know how to sustain their business idea, and can cope with changes in demand, they can be short lived. One recent 'back bedroom' innovation is that of Marc, 'inventor' of Sublime Science children's parties.

### Legal

Certain legislation must be complied with in business otherwise heavy fines are imposed and even imprisonment. Some of the laws affecting businesses are outlined in Table 1.6.

► Table 1.6: A sample of laws which affect business

Laws and regulations	Business type affected	What it means
Partnership Act 1890 (undergoing changes late 2015)	Partnerships	All partnerships are governed by this Act regardless of whether the partnership has been registered as a legal partnership or limited company. A partnership can only be dissolved if one partner wishes to retire or unfortunately dies. A partner cannot be sacked or made redundant. Regardless of the time as a partner or contribution to the business, partners must have equal share of all profits and losses, unless other legal contracts are in place stating otherwise.
Companies Act 2006 (undergoing updates late 2015)	Limited, unlimited, private and public companies	This Act sets a code of conduct for businesses to operate to protect the business and its operations (both internally and externally), its employees and shareholders. This Act informs company policies and their operations including financial, rules for forming and dissolving a business.
Charities Act 2011	Registered charities, non-profit	The aim of this Act is to protect the charity and its fundraising activities in line with business expectations. All fundraising activities exceeding £10,000 per year must register as a charity. Charities have to set up trustees to ensure the charity operates within the law. They are not being responsible for debts but can face greater public liability.
Competition Act 1998 (undergoing amendments late 2015)	Any business	This Act came into force to prevent domination by any one business by addressing: <ul style="list-style-type: none"> <li>• anti-competitive agreements which prevent, restrict or distort competition in the UK</li> <li>• abuse of dominant market positions which prohibits limiting production, markets or technical development to the detriment of the consumer.</li> </ul>
UK Corporate Governance Code	Public sector including schools, colleges	This Code comprises the rules and regulations which all governing bodies need to comply with and legal requirements for operating, including: <ul style="list-style-type: none"> <li>• formal financial accounts</li> <li>• record keeping of decision-making such as minutes of all meetings</li> <li>• rules by which governing bodies conduct themselves including requirements for holding meetings (frequency, attendance)</li> <li>• who can and cannot be a governor.</li> </ul>
Financial services regulation	Financial organisations	These are rules which act to protect consumers and provide monitoring of financial activities by third parties, for example auditors. The Stock Exchange is regulated by these guidelines, just as banks and other financial services are supervised.
Industry regulators	Sector specific	These regulators act as supervisors to ensure conformity and compliance across business sectors. For example, Gas Safe regulate gas appliances, fitting, servicing and manufacture. The Care Quality Commission is a health regulator. The Health and Safety Executive (HSE) regulates all aspects of business (and personal) operations. All businesses have their regulators, including registered charities (Charity Commission of England and Wales). Your qualifications are regulated by Ofqual to ensure they are relevant, appropriate and of sufficient quality.
Government departments	All businesses and the public	The government has many departments aimed at ensuring everyone operates in a responsible and trustworthy manner and for the benefit of public good.

### Research

Check for anticipated changes to existing legislation and the introduction of new rules and regulations.

### Key terms

**Environmental factors** – those factors outside of the business over which you mostly have no control.

**Ethical trends** – trends determined by moral principles.

Businesses are responsible for keeping up to date with developments and changes to legislation and regulations. Ignorance cannot be used as an excuse for non-compliance.

All rules and regulations, including laws, can be difficult to understand and are easily misinterpreted. Always seek professional advice if in doubt. This is why large organisations often employ their own legal department, just as the place of your study may have a specialist in their governing body.

## Environmental factors and ethical trends

More than ever, businesses and individuals are concerned about **environmental factors** and **ethical trends**. We all share a sense of social responsibility for our survival and that of the planet. Factors are outlined below.

- ▶ Carbon emissions.
  - This means an impact on business costs such as increased taxes imposed on fuel.
- ▶ Waste.
  - Household rubbish must now be segregated between different bins which the council collect and dispose of in controlled ways. Landfill sites are also heavily regulated, as is how water and sewage are disposed of.
  - In order to reduce the waste from bags given out by supermarkets and larger stores, the government imposed a charge on plastic bags from October 2015.
- ▶ Recycling.
  - Businesses must comply with the government's green policies which ultimately impact on all our lives. The government's 'lets recycle' policy is under review in their quest for zero waste.
  - Examples of businesses built on recycling include The Recycling Factory, which sells ink cartridges, and Traid, which remakes donated clothes for resale.
- ▶ Pollution.
  - The amount of pollution produced impacts on our health, buildings and surroundings. Demand for reduced pollution is forcing businesses to close, such as Didcot Power Station, demolished almost 43 years after it opened in 1970.

Businesses can benefit from being seen to support environmental issues, for example those affecting the planet, the food we eat and people's welfare, such as Fairtrade food production, recyclable products, free range eggs, etc.

Organisations can also be forced out of business if they don't consider environmental factors and ethical trends. One of the biggest law suits ever in the USA was won in 1996 when Pacific Gas and Electric were forced to pay damages due to chromium water contamination which impacted on hundreds of people's lives.

Some businesses choose to adapt their business operations, for example Pret A Manger have made changes to their plastic packaging to make it more environmentally friendly.

## Internal environment

### Corporate culture

Business (corporate) culture is a hot topic. You might have heard people talk about a blame culture – how an organisation is structured can have a great impact on whether or not there is a blame culture and, more importantly, whether employees and managers share the same view of this. Corporate cultures vary hugely from business to business. For example, large banks in the city are known for their long hours and

cut-throat attitudes whereas technology start-ups, such as those found in Silicon Valley and Old Street, are known for their relaxed, casual atmosphere. What impact do you think different cultures have on businesses?

## Corporate Social Responsibility (CSR)

You will have learned a little about CSR earlier in this unit. Three such examples given were URENCO, Banyan Tree Resorts and MMO.

CSR can greatly influence the operations of a business. For example, in the nuclear industry many people jump to conclusions about the dangers of enriching uranium: they readily conjure up stories which frighten others or embellish stories from historic events such as Chernobyl in 1986. These examples are usually driven by fear of the unknown and incorrect assumptions, but they can impact greatly on the success of a business. A more recent example in the nuclear industry was the Tsunami disaster at Fukushima in March 2011. This led to reductions in demand and lack of confidence in investing in planned nuclear power stations.

## Ethics

Businesses are also shaped by ethical considerations. One such example is the range of services offered by the NHS. In 1978, the birth of Louise Brown, the world's first ever test tube baby, led to some disapproval and claims that such intervention was unethical.

The health service is probably the most obvious example of the importance of ethics - IVF being almost commonplace and R&D appearing to make rapid progress, committees and government are challenged constantly about the ethics, for example, of body transplants. Very recently the announcement of human hand transplants and the proposal for 3D printing of body parts are undergoing an ethical debate.

Such matters impact on the way businesses are organised and operate, and on their funding and company values. For example, new businesses have emerged to meet the demand and supply of automated prostheses, pacemakers and computer software to stimulate brain function.

Businesses need policies and procedures in place to ensure their employees behave ethically. One example of where government stepped in to stop unethical practice was the decision to cap exorbitant interest rates charged by unscrupulous payday lenders.

CSR is an ethical consideration and you may also have been introduced to policies during your induction at your place of study or work. Other examples of ethical policies are **whistle-blowing** and those associated with equality such as homophobic bullying.

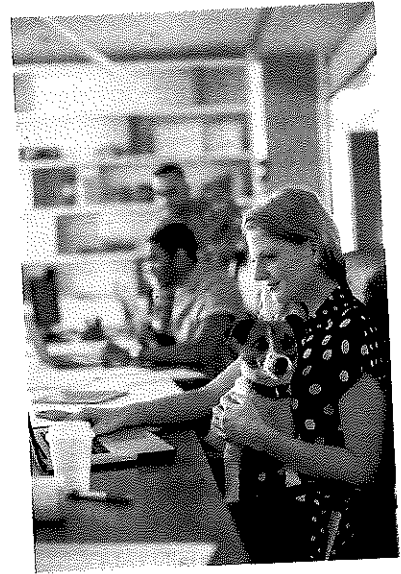
## Competitive environment

Just as some people are more competitive than others, businesses vary in how they regard competition. Those businesses which view competition as destructive may have overlooked competition as an opportunity.

Competition can be at different levels:

- ▶ local
- ▶ national
- ▶ international.

Having competitors does not mean that a business will automatically succeed or fail - rather, it relies on careful business planning and a consideration of all factors. For example, if Little Italy decided to open a coffee bar at a small rural railway station



- ▶ Can you think of the type of business that would have an office as shown in the photo?

### Key term

**Whistle-blowing** - informing on someone who is doing something wrong or illegal.

which already had one, it could be viewed as a bad business decision. However, if their reputation preceded them by offering a superior product, better customer satisfaction or improved value for money, then their business might well wipe out their competitor. Decisions like this cannot be taken lightly. You can probably name several examples where competitors appear to work alongside each other in harmony such as opticians, dental practices, estate agents, chemists, department stores, supermarkets, fast food chains, electrical retailers, etc.

### Factors influencing competitive advantage

In order to keep a competitive advantage, it is vital that a business keeps its eye on what its competitors are doing and tries to anticipate what they are planning to do. Factors which influence are outlined below.

#### Key term

**Wholesale** – the sale of goods on a larger scale at a lower price, usually sold direct to the retailer to sell on at a profit.

- ▶ **Differentiation:** for example developing new products, branching out into new products or services, especially something unique from your competitors, such as the Dyson Ball cylinder vacuums.
- ▶ **Pricing policies:** how a business determines prices for **wholesale** and retail products or services to achieve its planned profits.
- ▶ **Market leadership:** defines a business which has the largest or larger share of the market in relation to its competitors, for example Coca Cola and British Airways.
- ▶ **Reputation:** something a business cannot buy and which has to be earned. Businesses such as Waitrose, Virgin Atlantic, M&S and Walt Disney thrive on their reputation which has been developed and maintained over many years. Customers also highly rate Amazon, Microsoft, Apple and Plusnet. A bad reputation can rapidly ruin a business no matter how large or small. BT has been working hard to improve its reputation. Security company Blackwater even changed its name to X, and then to Academi, in an attempt to improve its reputation, without success, after a terrible incident in Iraq in 2007 that resulted in lost lives.
- ▶ **Market share:** the percentage of a given market that a business holds. Holding a market share does not mean that the business is the market leader, however. For example, in 2014 Samsung was reported to hold 26 per cent of the global market share in Smart televisions whereas in 2009 it was market leader with its range of LCD TVs.
- ▶ **Cost control:** managing and controlling costs for a business to remain viable. For example, Phones 4U acted as an interface or broker between mobile phone companies but the businesses it provided its services to decided to sell its services directly. Unfortunately, these other business declined to pay Phones 4U, leading to its bankruptcy.
- ▶ **Technology relationships with customers:** different means of technology are relied upon heavily for communicating with customers such as:
  - databases holding customer details, purchase history and preferences, etc
  - telephone and online support.

Finding an answer to a problem with a product or its operation might be resolved speedily by searching online or ringing an out-of-hours support line but relationships can be made, maintained or broken by the technology. For example, misunderstandings due to language differences, listening to annoying music while queuing for a response and sometimes being charged high costs, do little to build positive relationships.

#### Key term

**Outsource** – buying services or products from outside suppliers, often overseas, to cut costs.

While businesses are trying to manage their costs, they may be driven to **outsource** services such as after sales, help desks, etc. and these can impact positively and negatively on their reputation. BT and British Gas both experienced such challenges.



- Suppliers: all businesses rely on their suppliers and their ability to supply when required and at the agreed price. The external environment impacts on suppliers and subsequently the business being supplied. The process is known as **logistics**, and includes:
  - supplies being available at the cost agreed (materials to supplier may have increased)
  - transport (timescales interrupted due to road works, bad weather, ferry strikes, etc)
  - availability of personnel (interruptions due to holidays, sickness, strikes, shortages).
- Employees: external environmental factors impact on businesses, one example being loss of productivity due to sickness. While holidays are usually planned and businesses anticipate changes to schedules in advance, sickness is generally unpredictable.
- Other factors impact on the number of employees a business can afford and also the availability of potential employees when a business is seeking to recruit. Examples of businesses struggling to recruit include:
  - suitably skilled staff
  - graduates with appropriate qualifications.

What is the benefit to the business if they do manage to recruit suitably skilled staff?  
 What happens if staff are not suitably skilled?

### Benefits and importance of establishing and maintaining a competitive advantage

Benefits include controlling costs, having an advantage over competitors, informing future plans such as structure, pricing, location of business, means of promoting and providing services or products.

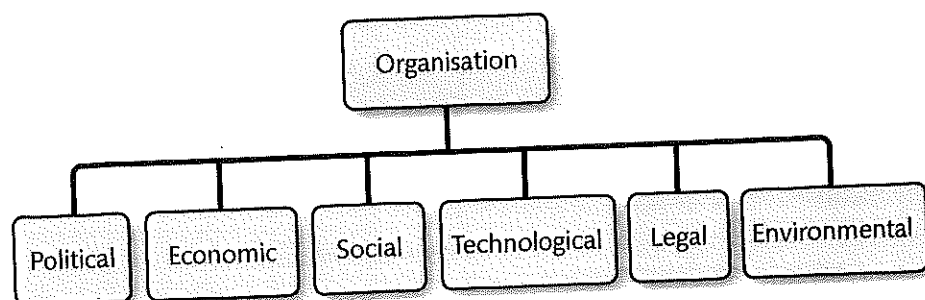
Important features include anticipating business and job security, providing what the market demands or needs and anticipating areas for development.

## Situational analysis

A situational analysis is an investigation into the state of the internal and external factors which affect a business, in order for managers/owners to determine plans for its future. This assessment requires an evaluation of potential customers and the competition in order to speculate on the financial future for the business and inform decision making. This analysis of a business underpins the marketing or a business plan which managers use to review the business aims and objectives. An assessment of the business environment is undertaken using various techniques which are outlined below.

### PESTLE analysis

This is a framework for evaluating external factors and their impact on the business to inform business strategy. There are many ways to replicate a suitable template to use, such as that shown in Figure 1.6:



► **Figure 1.6:** Example template for PESTLE analysis

Each of the **PESTLE** categories is explored with regard to its impact on the business:

- ▶ political factors
- ▶ the economy
- ▶ sociological and cultural aspects
- ▶ potential technology developments
- ▶ current and potential legislation
- ▶ environmental considerations.

This analysis can, and possibly should, be combined with a SWOT analysis.

### SWOT analysis

A **SWOT** analysis helps to examine the internal and external elements in a business. It is a useful approach to undertake in conjunction with, prior to or subsequent to carrying out a PESTLE analysis. The two can then be compared and challenged. A simple template can be used to undertake a SWOT analysis.

Evaluation judgements are listed in response to the heading in each box, as shown in Figure 1.7.

#### Key term

**SWOT** – strengths, weaknesses, opportunities and threats.

<b>Strengths</b> What are the strengths of the business, such as employees, product, etc.?	<b>Weaknesses</b> What are the weaknesses of the business?
<b>Opportunities</b> What are the opportunities for the business based on the other responses?	<b>Threats</b> What are the threats?

▶ **Figure 1.7:** Simple SWOT analysis template

### 5Cs analysis

This type of analysis is used to inform the marketing of a business having undertaken other forms of situational analysis, such as PESTLE and SWOT. Each category is analysed by responding to questions which seek to identify, for example, the components that make up each of the **5Cs** (see Figure 1.8). This type of analysis is used to inform business operations as it focuses on current internal operations using data and statistics.

#### Key term

**5Cs** – company, collaborators, customers, competitors, climate.

	Categories	Areas evaluated	Judgements
<b>SWOT ANALYSIS</b>	Company	<ul style="list-style-type: none"> <li>• Product image and branding</li> <li>• Technology</li> <li>• Culture</li> <li>• Aims, vision</li> </ul>	
	Collaborators	<ul style="list-style-type: none"> <li>• Suppliers</li> <li>• Stakeholders</li> <li>• Distributors</li> </ul>	
	Customers	<ul style="list-style-type: none"> <li>• Demographic</li> <li>• Where, what and why they buy</li> <li>• Pricing</li> <li>• Frequency and quantity purchased</li> </ul>	
	Competitors	<ul style="list-style-type: none"> <li>• Current and potential</li> <li>• Market share</li> <li>• Strengths and weaknesses of competition</li> </ul>	
	Climate	<ul style="list-style-type: none"> <li>• Political and environmental</li> <li>• Financial: interest rates, exchange rates</li> <li>• Technology</li> </ul>	

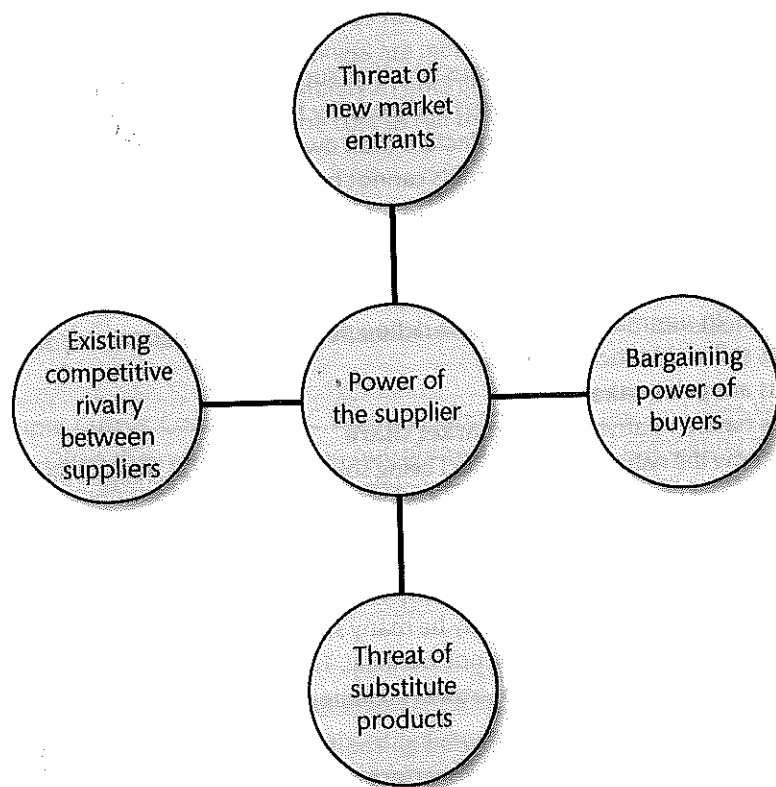
▶ **Figure 1.8:** Example template for 5Cs analysis

## Porter's Five Forces

This is used to evaluate the position of a business in terms of its competition. Five categories are considered:

- ▶ existing competitive rivalry between suppliers
- ▶ threat of new market entrants
- ▶ bargaining power of buyers
- ▶ power of suppliers
- ▶ threat of substitute products (including technology change).

Each category is evaluated in relation to the impact of suppliers on the business, which might be replicated as shown in Figure 1.9.



▶ **Figure 1.9:** Example template for Porter's Five Forces

Templates for undertaking **Porter's Five Forces** analysis also vary, placing each of Porter's Five Forces at the heart of the evaluation. This evaluation can also be undertaken in conjunction with SWOT and PESTLE analyses, by using the results of each analysis to evaluate each factor of Porter's Five Forces.

### Key term

**Porter's Five Forces** – supplier power; threat of new entrants; threat of substitutes; buyer power; rivalry.

## II PAUSE POINT

In what other ways could you structure a portfolio?

### Hint

Look up the definition of portfolio – it does not have to be a folder containing paper. How else could you communicate your findings?

### Extend

Using your results from your situational analyses or further analyses, evaluate how the business may react to future changes.