Business environment

Economics, Macroeconomics

BUSINESS ENVIRONMENT SYLLABUS CHAPTER I Business environment- Dynamic factors of environment- Importance of scanning the environment- Fundamental issues-Economics environment of business - Sock) - cultural environment- Political/ Legal environment -Cultural environment. CHAPTER II Political economy - Government and business -. Public control, of business - Trends and structure of Indian economy - Socio - economic problems of India CHAPTER III Government controls and regulations -, Regulating economic and industrial activities - Industrial Licensing policy - Control of monopolies -, Capital issues control - Government control over FDI and collaboration - Distribution and price control - New EXIM policy - Foreign exchange flow regulation -Technology transfer. CHAPTER IV Monetary and fiscal system - Banking and credit structure in India — Financial institution - Fiscal system - theory and practice. CHAPTER V Economic planning and development - Government and planning - India's eight five year plan and structural reforms - Industrial policies and promotion schemes - Government policy and SSI - Interface between Government and public sector. CHAPTER VI New Economic Policy Environment in India - Privatization - Liberalization and Globalization - Experiences and issues - Environmental assessment and evaluation. REFERENCES : Mohinder Kumar Shartna - Business Environment in India Adhikary M, Economic environment of business Amarchand, D. Government and Business Francis Cheunilam : Business and Government Maheswari & Gupta : Government, Business and Society Kuchal, S. C : Industrial economy of India Fredrick Davis : Business and society. Business environment | 1 | Environment - Introduction | | | 2 | Business Environment & Economy | | | 3 | Control of Business Environment | | | 4 | Monetary & Fiscal

System | | | 5 | Planning & Development | | | 6 | Liberalization & Globalization | | CHAPTER I Business environment - Dynamic factors of environment - Importance of scanning the environment - Fundamental issues - Economic environment of business - Socio - cultural environment - Political / Legal environment -Cultural environment This chapter focuses on the following aspects of Business environment: Definition of business, meaning of business environment, the classification of business environment, need to study environment in business decisions, the methods of scanning the business environment, issues that are to be addressed while scanning the environment, various types of factors that influence business environment, non-economic environment and its impact on business decisions. To highlight the importance of the Business environment, three case studies have been appended at the end of this lesson. Definition of business The term business is understood and explained in different ways by different people. For some, business is an activity, for some it is a method of transacting, for sonic others, it is a method of money making and some people argue that business is an organized activity to achieve certain pre-determined goals or objectives. Dictionary meaning of business is: the act of buying and selling of goods and services, commerce and trade. Based on all these meanings of justness, we may define business as: gainful activity through which various elements of society conduct exchanges of the desirable things. In the olden days, the people engaged in different activities in a society were classified into four groups : Brahmnas, Shatriyas, Vysyas and Sudras, Of these our fold classification of social activities, the activities of vysyas included basically, facilitating exchange. Hence, business as an exchange activity remained since the days of exchange started. It could also be recalled that business as a social activity became popular only when the wants of different people in a society were to be met with the available resources. In other words, whenever there was a scope for producing something, which is wanted, then business activity automatically emerged. But now a days, business is viewed more as a profession or occupation. From the days of family owned business, we have reached a stage of professionals and experts starting and running business. It could also be noted that business administration and business management have emerged as the most prospective field of study and occupation. Persons with educational background in business, enter business or join business organizations to make them successfully function. Unlike the olden days, a number of interests are involved in business today, viz. owners, investors in business, suppliers, customers, employees, government, stake holders, administrators, managers, strategists, executives, and so many others. Hence, every business activity has to meet the goals or aims or objectives of these various groups of people. That in fact, has made business a most complicated activity. Modern business has a number of features. Understanding of these would help to appreciate and organize business activities in a highly professional way. 1. Business is an economic activity : Business involves organizing activities to satisfy human plants. These activities may result in the manufacture or production of a commodity or extension of a service. When a good or service is produced, resources are involved. Resources like human resources, physical resources and financial resources are all required to realize output to meet human needs. These resources are limited in supply, and so business involves identification of resources, evaluation of resource qualities, buying these resources and utilizing these resources. These resources being scarce in relation to their demand, the resources carry some value [i. e., price]. They cannot be procured at any cost to produce anything to meet human wants. So automatically selection among various resources come up which is made on the basis of requirement and cost. Once they are procured, then they are used in a very judicious manner so that there is no waste. That is optimal utilization-of resources is to be achieved. In this context, several decisions like resource selection, resource procurement, resource mix, resource utilization, etc. are all involved. As in all these stages, choice among alternatives is involved, every business activity is to be treated as economic in nature. Depending upon the business activity, the approach to selection among alternatives would differ. For example, in a manufacturing business, the choice is about input selection to supply quality output, in a service organization the choice is about-inputs and delivery process, in a government organization it is about production and equitable distribution of output, in an institution like bank, provision of various investment opportunities of short term and long term to the public, etc. 2. A business organization is an economic unit Every business organization is engaged in transforming inputs into output to meet the requirements of the people. The selection of input and size of procurement will depend upon, the size of the organization. This would also depend upon the nature or product or service extended/by the business unit. All these are attended with the objective of making profit or surplus. Only when there is surplus achieved, can the business units grow. Hence creation of surplus in a business becomes the focal point and this is best achieved through optimal utilization of resources. That way, all business units have to achieve the maximum output with minimum inputs which in other words is the effort to achieve economic efficiency. Only economic efficiency can enable firms to be efficient in every other sense. Therefore, business organizations are only economic units in nature. 3. Business decisions making is essentially an economic process All business decisions involve selection from alternatives. In other words, the rational choice of inputs is implied in every business decision. Hence, to be rational, a business unit goes through the process of : determining objectives, identifying opportunities, generating alternatives, classifying these alternatives as feasible and infeasible alternatives, then rank the feasible alternatives on some criteria and then select those alternatives fulfilling the constraints. For example, if the objective of a business unit is to maximize profits, then this would call for minimizing cost and maximizing revenue. On the cost side, the business unit have to identify, procure and utilize resources in the optimal way and on the revenue side, the business unit should determine the price which would facilitate maximization of revenue. Price determination again would depend on various factors like demand, supply, competitive scenario, government interference, statutory compulsions, conflicting interests of the stake holders of the business, etc. Therefore, every decision made in a business would automatically depend on the economic process. Changing concept of business It has been stated already that the concept of business has undergone a vast change. From a producer driven stage business has become consumer centered and driven stage. While the earliest concept was

* sell what is produced' the modern concept is 'produce what is wanted' So every business depends on consumers and their ever changing needs. Any business unit which has successfully understood its customers and offer the product or service meeting their requirements alone is successful. But in this process, business units have to manage pressures from its owners and other stake holders. It should take into account the requirements of the workers and the trade unions. It should abide by the rules and regulations of a number of government agencies and institutions. It should meet the challenges and threats from competitors. Most important, it has to fulfill its social obligations. To survive every business unit has to also consider: the revolutionary changes in technology, market expansion, information explosion, competitor strategies. These are days when the consumers are better informed and so no business unit can afford to ignore consumer awareness and preferences. Technological development has brought with it the compulsion to use modern methods and techniques. Social obligations have made business units to meet pollution norms, etc. Trade union pressures have made them to design satisfactory service conditions for the work force. Then there is compulsion to provide for development of human resources in the organization to achieve organizational development. All these have made modern business ‘ tight rope walking.’ BUSINESS ENVIRONMENT Business involves activities, which links an organization with outside world. Within an organization, a business is governed by the behaviour of its employees, management or decision makers. But externally a business is influenced by a score of factors, which range from customers to competitors and government. Therefore, a business cannot be independent

of (he influence of these external factors. It should also be noted that a business has absolute control over all the internal factors, it has no control over the external factors. So often it becomes necessary for business houses to modify their internal decisions and policies, on the basis of the pressure from external factors This highlights the need to be ever- cognizant of changes and influences of external factors so as to conduct business on healthy lines. It is in this context that business environment assumes all significance. Business environment therefore refers to the influences and pressures exerted by external factors on the business. The following Figure would help to understand the various factors which constitute the business environment. From the Figure: 1, it would be clear that business organizations function in an environment subject to the influence of various constituents. Earh one of the constituents have in turn a number of factors influencing them. For example, economic environment has micro and macro environmental factors affecting it. To develop a right perspective about business environment, let us discuss briefly about each one of the external environment constituents. 1. Demographic environment : This refers to the size and behaviour of population in a country. Suppose a country has a huge size of population, then, the country would provide extensive business or marketing opportunities for all types of business organizations. On the other hand, a country with low size of population would force the business organizations to seek external market for their products or services. Similarly, if the population in a country is well - tuned to 'use and throw concept’ [like most of the Western countries] then there would be limited scope for repair shops and employment scope in that segment would be almost nil. But alternatively this would give wide marketing opportunities for manufacturing organizations. On the other hand, if the population is averse to 'use and throw' concept, then the business opportunities would be limited for manufacturing organizations but the repair shops, self-employed technical persons and spares manufacturers, would have roaring business. Hence, the size and quality of population emerges as a vital factor influencing business environment. 2. Economic environment: Economic environment refers to the overall economic factors like economic philosophy of the country, economic structure, planning, economic policies, controls and regulations, etc. All these have a serious impact on the functioning of business organizations in a country. For example, in a Capitalistic economic system, business organizations would be subjected to limited government regulations and controls. They would be more governed by market forces [demand and supply] rather than by other factors. On the other hand, in a Socialist system, the government would determine everything on behalf of the country. In a Communist set up, the government has absolute control over every aspect over production that private enterprises may not exist at all. In a Mixed economic system, government would be selective in allowing die presence of private enterprises in certain activities, reserving some spheres completely for governmental operations. Hence, the economic philosophy of the country directly determines the scope and functions of business organizations in that country. 3. Geographical and ecological environment: Geographical environment refers to climatic conditions and natural resources, which determines flu manufacturing scope and the nature of the products that could be marketed. For example, a country like Kenya has to manufacture more of products based on forest resources, while the Gulf countries can produce only crude, Japan can have business in fish, fruits, etc., Countries in the tropical region would have organizations specializing in products from geographical resources available in abundant in that region, while organizations in Mediterranean countries have a Different business scope, Scandinavian countries have scope for dairy product manufacturing, etc. Similarly ecological imbalance is taking place at an alarming rate in the world today, that deforestation and hunting of rare species of animals for food are all prohibited now. Hence, while identifying the business opportunities, business organizations have to be conscious of the limitations posed by the geographical and ecological considerations. 4. Legal environment: It is well known that every country has a number of legal regulations to ensure that the interests of business organizations do not run counter to national interests. Right from the stage of incorporation of organizations, their listing in stock exchange, reprisal of customer complaints, payment of tax to government, manufacturing practices, human resources development to pricing of products and services, a number of legal regulations have to be fulfilled. For example, in USA and several western countries, consumer protection is very active, that even a medical practitioner is subjected to huge liabilities in limes of deficiency in services. In India and other countries, very rigorous legal provisions arc in place to prevent hunting of rare species, that any organization, which manufactures products based on such species, have lo get legal sanctions. In case of failure to honor cheques issued, organizations are now a days made to pay hefty compensations. Hence, the deterrence in terms of legal provisions has become the order of the day. All organizations have to first of all address these provisions become coming in to steam. 5. Technological environment: This is a very significant external factor determining the destiny of business organizations. Supported by computerize operations, modem business organizations have succeeded in analyzing customers, minimizing the defects in products, ensuring service at the right time and place, etc. While communications use to take unduly long time in those days, business communications are instantaneous these days, thanks to modem satellite technology. Modern organizations have recognized that research and development alone can ensure organizational growth and stability. They have become more and more pro-active and remain as change agents of the economy. Governments have also become more technology conscious that right from police controls to registration of title deeds, computerizations has been adopted. Customer servicing through call centers is the latest necessity of organizations. Manufacturing activities have become more and more technically sophisticated. Therefore business environment has become highly dynamic. 6. Social environment: Social environment today has brought compulsions on business organizations to adhere to certain business ethics and morals. Social responsibility of business is an important force that modern business organizations cannot wriggle out of their duties and responsibilities towards the society. For example, every leather manufacturing or process unit is made to install pollution prevention system. Similarly, the expectations of various interests in the society have undergone a sea of change. The shareholders, promoters and owners expect a reasonable return on their investments. The workers expect security of service, terminal benefits, accident relief and various other compensations from the organizations. Government expects the business units to pay tax regularly and participate in social improvement. The distributors and agents expect the organizations to ensure smooth delivery process and demand more commission and compensation. Suppliers expect the organizations to give them continuous business and prompt payment of bills. Therefore each social group has a specific interest, the combination of all these, exerts enormous pressure on the business unit. A business unit which succeeds in meeting the interests of all these groups remains successful and grows. 7. Educational and cultural environment: Educational environment in a country determines the quality of population. A country with very high illiterate population would always experience political and economic instability. Similarly, lack of education may also give scope for the existence of superstitious beliefs, fatalistic attitude, etc. People's choice of goods and services would be more governed, by their religious faiths and beliefs. For instance, in the colonial days, the Indian population was a victim of the Britisher's divide and rule tactics. The economic development of a country completely depends on the literacy level which alone can pave the way for improvement in science and technology, modernization, industrialization, etc. In such a country, the business opportunities are plenty. Cultural environment refers to the values, norms, customs, ethics, goals and other accepted behaviour pattern of people in a country. In olden days, religion was the basis of all activities in a society. The religious leaders and institutions determined what business should do and what people must consume. In India, the existence of caste system has done more damage than any good. Caste based politics has become the order of the day. Under the pretext of working for backward and downtrodden people, several persons have amassed fortune. This is worsened by political support and policies. A modern organization does not have the liberty to recruit people on merit but it has to follow strictly die reservation policy of the government. Another serious aspect of the cultural environment is the attitude and behaviour of the people in urban and rural areas. The urban - rural divide has created enormous problems for administrators and specifically business organizations prefer urban educated person to persons from rural areas. 8. Political environment: Political stability is one important factor winch determines the business growth or downfall. A country with relative political stability would witness inflow of foreign capital and collaboration. By political stability we mean that the policies of government remaining consistent. As the business decisions arc based on government policies, frequent changes in these policies would force business organizations to change their policies too which, makes functioning very difficult. Sometimes, when the policies determined by a party in power are reversed by the succeeding party forming the government, there would be far reaching changes in business environment For example, India was following a policy of protectionism till late" 1908's. Hence, the industrial development and economic development could not take place at a rapid rate. In the absence of competition, the business organizations, made people to accept inferior quality goods and services. Once, the liberalization policy is adopted, the scene has completely changed. Today, no business can survive unless it provides quality goods or services on par with the multinational corporations. Another aspect of political environment is the political ideology with which a party is wedded to, would make the government tow the lines of countries with similar ideologies. Until the disintegration of USSR, India was simply following USSR's lines, but after the disintegration, India has to literally fend for itself. With the pressures mounted by the Western countries, India had to accept various trade and monetary policies. This has brought about a complete change in business environment. NEED TO SCAN ENVIRONMENT Having discussed very briefly the features of each one of the constituents of business environment, let us discuss why the environment should be analyzed by the business organizations. It is well known that business enterprises cannot remain independent of the society and the institutions. So whatever decision they take as to be in tune with the requirements of society and the dictums of the institutions. A business organization has to continuously monitor the environment so as to identify the business opportunities and threats. By exploring its strengths and minimizing its weaknesses, if the organizations can capitalize these opportunities and effectively thwart the threats, then it would be able to grow. Let us elaborate this with an example. Suppose an organization wants to introduce a new consumer durable product in the market. Then it would study whether there would be demand for this product and the product would be accepted by the society. At the outset, the organization would examine whether the product would suit the culture in the society. Suppose the product is 'use and throw' type. Then people would certainly be influenced by this feature of the product while evaluating the price of the product. In India, such a product would never be accepted as the culture here is to lengthen the life of every product by repairing it. Similarly suppose the product requires some critical component from abroad. Then unless the government policy is favourable the component has to be imported at a very high cost, which in turn would drive the price up. . Suppose the product is only one of its types, the organization would then emerge as a monopoly supplying the product. This may not be tolerated by the government. Suppose the manufacturing of the product involves advanced technology, then the type of human resources required would be well educated and trained. Obviously this will rule out the job 'opportunities for persons educated in rural areas. Further, if the manufacturing process involves scope for pollution, then the organization has to address it in relation to the provisions of the pollution control norms. Hence, in every decision of the organization, the external environment has an important role to play. Any future plans of expansion and forecasting of demand will depend upon the changes in the business environment. These changes may include both the current and expected changes. Unless these changes are also foreseen, decisions taken would turn out to be suicidal. In the case of organizations which have been pro-active, the changes in the environment do not affect them much. But those which fail to understand from their own experience or that of the other changes would remain challenges for ever. Among the various constituents of business environment discussed above briefly, we will focus on the following constituents and discuss them in greater detail. The constituents now elaborated are: Economic environment, political environment and cultural environment. 1. Economic environment The economic environment is composed of various set of economic policies, economic system, strategy of economic growth and development, resource endowment, size of market and status of infrastructural facilities in a country. All these affect the business environment one way or the other. To understand the impact of these on business environment, let us discuss each one of these components in detail. Economic policies: Economic policies include fiscal policy, monetary policy, foreign trade policy, licensing policy, technology policy, price policy, etc. These policies lay the framework within which every organization has to function. A] By fiscal policy we mean, the government's tax efforts, public expenditure and public borrowing. Through these the government can effectively encourage consumption, investment and savings habits and also restrict them. For example, suppose there is inflation in a country. Inflation implies that the people have high purchasing power and so they demand goods. To curb this, the government may raise the personal tax and also the corporate tax. Consequently, individuals will be left with lesser disposable income and to minimize tax, they may start saving through various tax - saving schemes. As far as the corporate are concerned, they have to part with more by way of tax to the government and this would bring down the rate of profit and dividend declared. As a result the corporate would resort to upward price revision, which might lead to further fall in demand for their products and services. During deflationary period, the government would reduce the tax so as to encourage more spending and investment. Even in tax policy, the government can be selective in taxing more of rich and exempting the poor completely. This would facilitate income re-distribution and improve the conditions of poor. Similarly, by altering its expenditure on various public projects, the government would be able to influence the prevailing economic condition. Government expenditures are incurred on infrastructural development, public utility services like hospitals, new industrial units of very huge size, etc. For instance, suppose there is inflation in a country. The government would reduce its level of expenditure, thereby reducing the income of the people. With lesser income, the demand would, go down and so the price. At the time of deflation, the government would expand its public expenditure by investing in a number of public projects, so that there will be income generation find demand generation which will revive the economy. Public borrowing is one more instrument in the hands of the government to influence the economic condition in a country. This involves government issuing bonds and encouraging common public and other institutions to buy them. By this, the government would be able to bring down the level of purchasing power in the economy and control the inflation. During deflation, the government would redeem the bonds and so with more purchasing power, the economy would be able to revive. B] Monetary policy refers to the set of policies determined and implemented by the central bank of a country to control the economic condition. The central bank of a country has the basic responsibility to maintain the price level and money supply in a country. This is possible only when the central bank has certain instruments. These instruments available with the central bank to control the money supply and price level are called monetary policy instruments. They are called Credit control policy. Credit controls can be of two types: Quantitative credit controls and Qualitative credit controls. The former aims at limiting the money supply, while the latter is used to channelize the available credit in the country. Quantitative credit control policy includes three tools: bank rate, open market operations and variable reserve ratio. Bank rate refers to the rate at which the central bank would re-discount the eligible bills already discounted by the commercial- banks. By revising the bank rate upwards, the central bank would be able to make the discounting by business organizations with commercial banks costly. This would discourage discounting and thereby money supply in the economy, would come down. Alternatively, by lowering the bank rate, the central bank makes credit available at a cheaper rate, and so the business organizations would go for a larger discounting of eligible bills with commercial banks. This liberal credit policy would have expansionary effects on the economy. Similarly, using open market operations, the central bank would buy or sell the securities in the open market and through that increase or contract money supply in the economy. For example, suppose there is inflation in an economy. To bring down the money supply, the central bank would sell the securities it has which will be bought by the commercial banks and other institutions. In this process the excess money with these institutions would be siphoned off, there by they have to restrict credit. Alternatively when there is deflation, the central bank would buy the securities and the money equivalent transferred to the banking system would facilitate adoption of liberal credit. Variable reserve ratio refers to the increase or decrease in the quantum of Statutory liquidity ratio and the Cash reserve ratio which the commercial banks have to maintain as a proportion of their total deposits. By increasing the ratios, the commercial banks would be left with lesser volume of funds and so they can lend less. By reducing the ratio, the commercial banks would be left with more funds with which they can make lending liberal. All these policies would have a direct impact on the business organizations and their operations. Through qualitative credit controls, the central bank can : regulate consumer credit, alter the margin requirements, resort to persuasive efforts, take direct action on erring commercial banks, etc. Through these policies, the central bank would be able to regulate and direct the available credit to the priority sector and discourage credit for less priority or no priority sector. Hence, business organizations, which fall under priority sector, would be able to expand their business with cheap funds and assistance C] Foreign trade policy: The foreign trade policy determines the scope for trade between countries. It would directly affect the business prospects of the business organizations. A liberal policy would extend the scope for exports and imports, while a restrictive policy would narrow the scope. Similarly, if protectionism is favored, then the business organizations will have lesser market threats from multinational corporations. Alternatively if liberalization is the policy, then every domestic business organization has to tune itself to every type of challenge posed by the business giants from abroad. Foreign trade policy also includes the exchange rate policy and exchange controls and customs duties. All these are fundamental to the growth of a business organization. For example, suppose there is full" convertibility, then the business organizations would be able to export and import and make payments with lesser restrictions. On the other hand, if there is only partial convertibility, the scope for trade is correspondingly less and the business organizations have to go through a sickening process of getting licenses for export or import and route all their payments through proper channel. Customs duties also play a vital role in determining the volume of external trade. A rise in customs duties would discourage domestic demand because the price of imported goods and services would go up find remain at a high level compared to the domestically produced goods and services, A reduction in customs duties would encourage imports and be favourable to the domestic manufacturers. Government frequently changes the foreign trade policy, keeping in view the requirements of the country and the economic condition. To tide over the Glance of payments difficulties, government may resort to various policy measures like devaluation, exchange clearing agreements, tariffs and duties, exchange control regulations, etc. These tools would be suitably modified to achieve the desired goals. For example, to encourage exports and discourage imports, the government may devalue the currency, by which the imports of Indian goods abroad become cheaper and the imports of foreign goods in India become costlier. Hence the business organizations have to continuously monitor the changes in the trade policies so as to position themselves accordingly. D] Licensing policy: In the pre-liberalization days, India adopted licensing policy in regulate the growth of industries in India. Since the days of independence, India adopted licensing policy, which in effect made the government control the growth of independence in accordance with the national priorities. For example, in India, till 1985, the industries in India were classified into four categories: industries completely owned by public sector, industries where both public and private sector participation was permitted, small scale industries and collage industries. Except the first category in all the other categories, private sector presence was permitted through licensing. This was resulted in several adverse effects, which were all explained in detail by the Dutt committee report. But till 1985, liberalization was never accepted as a part of growth strategy. But after 1985, the situation slowly changed that by 1991 India adopted a policy of liberalization. Consequently, the business scope and prospects of the Indian business organization changed since 1991. As has been already pointed out they were exposed to market competition and threats after liberalization. Performance has become a necessity for survival. By about the end of 20th century, the government also proceeded to disinvest several public sector units thereby opening up the challenges all the more for Indian industries. Therefore, the licensing policy and its direction have a lot of impact on the business organizations. E] Technology policy: One of the most important economic policies is the technology policy. Improvement in technology is a condition for growth and survival in any organization. From a stage of man-dependent environment, the business organizations are all fast becoming machine-dependent [computer dependent]. Right from the stage of enquiries down up to planning the logistics, computers are widely used. Only from the mid -1990's the government started adopting a favourable technology policy. Apart from permitting free imports of computers and components as well as telecommunication equipments, the government has devised a number of schemes like Software Technology Park, to give a Phillip to the technology in India. Computerization has come to stay in telecommunication, railways, roadways, postal services, educational services, medical services, engineering, financial services, etc. This liberal technology policy has resulted in the growth of new industrial segment, viz., and information technology. Millions of youngsters get trained and are gainfully employed. Indian software engineers are considered as the best in the world and several of the multinational corporations depend on Indian supply of trained software and hardware professionals. The business environment has completely transformed over the past five to six years that unless organizations also accordingly change themselves, their survival will become a serious question. F] Price policy: This refers to the controls that government has on the price in a country. This is necessary, because, unless price is controlled, there is bound to be inflation and then economic instability. Further in Indian context, nearly 35% of the population is living below the poverty line. They do not have any permanent employment. Especially the rural poverty is very serious. To overcome this situation, the government resorts to price control policy. All the essential and basic necessary goods are subjected to price control. While the poor and downtrodden are provided the essential goods at a controlled and subsidized rate through public distribution, the others are expected to meet their requirements through open market. Through demand and supply management, the government makes all the efforts to keep the prices under--control. For instance, by building up buffer stocks, the government overcomes the shortage of food commodities during adverse period. Similarly, specific concessions are given to industrial units located in backward regions and rural areas. This helps them to run on sound basis. As regards the manufactured products, the government adopts the administered price mechanism to control the prices. For example, the cooking gas is supplied to the public at one price, to the commercial establishments at a different price. This helps to minimize the strain of the population using LPG as cooking media. Similarly till April, 2002, petrol and diesel were subjected to administered price controls. Sugar, cement, etc., are also subjected to administered price. Hence, through price policy the government protects the interests of the people and this policy has a direct impact on the functioning of the business organization in our country. 2. Political environment It is well known that the business environment in a country is very much interlinked with the political environment. The political environment simply means the political ideology which is adopted by the government. In a democratic country like India, this political ideology changes as and when there is a change in the party ruling the country at the Centre and the State level. A number of examples could be cited to prove how the political ideology has influenced the business environment of the country. Before independence, under the guidance of Mahatma Gandhi, India was wedded to the policy of ' Swadeshi'. That is, Gandhi advocated the use of only Indian made goods and to completely abstain from imported goods, specifically British goods. As a result immediately after independence, Indian government followed a restrictive, trade policy imposing very heavy customs duty on imported goods. This was thought that such a policy would help to achieve both the political commitment as well as protection of domestic producers from the invasion of foreign-manufacture-s and traders. A deeper look into such a policy would reveal that India never wanted to entertain a policy of allowing foreign trading activities on Indian soil as this would lead to colonization. After all the British East India Company entered the Indian shores under the pretext of trading with India in 1600 AD and the country had to pay a heavy price for the next 350 years being a colony. Hence, a restrictive trade policy was very much favored by every one and in such an environment the business environment was such the domestic producers could operate under the umbrella protection of the government. This is also evident from the Industrial policy of the government in 1948, which clearly posed a threat to foreign interests in India. At the same time, the Indian government was very much influenced by the Russian type of planning. Being a declared democratic socialist country, India adopted planning as the strategy of economic development. The First Five Year plan was formulated and implemented without relying much on industrial development, when at the end of the I Plan it was realized that growth is impossible without industrial development, a shift focus was necessitated that the government gave emphasis on industrial development. But here again, the government approached the issue with caution. It felt that a controlled and guided industrial development would yield better results than a free unrestricted industrial development. The consequence was the Licensing policy. Though imports were permitted, industrial development through collaborative efforts with entrepreneurs abroad was subjected to a very critical scrutiny. When the Licensing policy led only to concentration of economic power in the hands of a few private sector units like TATA, Birla, and others, the government brought in the Monopolies Restrictive Trade Practices Act, in 1970. This has on the one hand put a check on growth of monopolies in India, on the other hand the industrial development was not taking place at a desired pace. The seeds for liberalization were sown in 1985, when the government felt that India could achieve miraculous growth through this liberalization course, it proceeded in that direction. This culminated in the introduction of Liberalization policy in l99l. This resulted in a peculiar scenario in —which ‘ democratic socialism with capitalistic ideologies’ existed. Throughout the four decades after independence, India's policies were more governed by the political factors rather than economic necessities or compulsions. Hence, at the beginning Indian government adopted a purely socialistic pattern of development strategy while by 1990’s development by subscribing to capitalistic pattern has become the reality. This shift has a great impact on the business environment that domestic business today has to realign itself to survive and grow, in a competitive atmosphere. Having discussed the effect of political environment on business environment let us examine how far the economic system is an important factor influencing business environment. Economic system refers to the organizations and institutions created for the purpose of satisfying the wants of human beings. In a country, available resources have to be utilized to manufacture and distribute goods and services, which would meet the needs of the people so that they are satisfied. These institutions and organizations function with their own rules and regulations. The economic system has certain broad characteristic. 1. The economic system always functions with scarcity of resources. How the system effectively and efficiently uses the resources will determine the extent to which the needs of the people are met. 2. An economic system comprises people. That is, a society of human beings alone can constitute economic system. 3. A set of institutions are created and used for the purpose of smooth functioning of an economic system. For example, banks, money, technology, government, price mechanism, planning etc., are all institutions through which the systems operate. 4. The basic objective with which an economic system functions is to satisfy the wants of the people. Unless there is want for a commodity or service, nothing can be produced. Hence, the economic system allocates the resources in such a way that the wants of the people are satisfied. 5. On the basis of the above characteristics of an economic system, it should be clear that the economic system is very dynamic in nature. That is, the economic system undergoes changes with every change in the institutions, though the rate of change would differ from institution to institution. The economic system functions to answer three vital questions: a] what to produce b]how to produce and c] for whom to produce. Answering these questions assumes enormous significance as that would determine every activity within a country. The first question 'What to produce' depends on what is wanted. The economic system would throw signals through which the requirements of the people could be understood. But not all wants could be satisfied. This is because; a country may not be gifted with all the necessary resources to produce all the goods. Hence, depending upon the resource endowment a country would decide what it could produce. Then there is a problem of prioritizing the available resources among the goods to be produced. Resources should not be used for the production of unwarranted goods. The production of goods, which are harmful to human beings, like narcotic drugs, should be prevented. Hence, considering the availability of resources, the economic system should opt to produce only goods that would satisfy the wants of human beings. In this context it is also necessary to weigh the individual requirements and the national requirements for goods. The latter should be given preference over the former. The second question ' How to produce' addresses basically, issues relating to selection of right strategy, technology and investment. For example, a country like India, with very huge population should not prefer capital -intensive technology, as that would lead to more unemployment of human resources. Similarly, while selecting the technology, a country should weigh a number of considerations like relevance of technology, cost of technology, support in case of failures, consequences of the technology used, etc. Another vital aspect is the investment that a country has to make while selecting the strategy and the technology. A very important question is whether the available funds should be invested in sophisticated research and development or meeting the basic needs of the people. Hence, the second question would ultimately determine the efficiency with the available resources are utilized. ' For whom to produce' implies that based on the resource utilization, the country as a whole should benefit and not a few segments. Hence, having produced the goods and services, how they could be equitably distributed is an important aspect. The distribution of national product would differ from country to country depending upon the economic system in vogue. It has been already pointed out that the way in which the above three questions are answered depends on the economic system which functions in a country. To understand how these answers differ among the economic systems, we should understand the different types of economic systems. In the next section, the details of different types of economic systems are discussed. Types of Economic system Economic systems may broadly be classified into three categories: Capitalism, Socialism and Mixed economy. A number of other types also emerged but all of them came close to any one of the above three types of systems. Such systems include: communism and Marxism Let us now discuss the features, strengths and weaknesses of each one of these systems. 1. Capitalism Capitalism is an economic system based on the principle of free enterprise. Individual ownership of resources is an important feature. With control and command over resources, individuals can conduct any type of business. The object in such a system is to maximize private gains. Any type of enterprise or production of any commodity or service is permitted, so long it is wanted by the society. In such a system the market forces determine the resource allocation and price. That is, the demand and supply forces together determine what to produce, how to produce and for whom to produce. Price mechanism is the nucleus of the capitalistic society. The price mechanism clearly reflects the wants of the people. Once this is known, the producers would allocate the resources to manufacture and sell the products in great demand. While doing so, there is no control or regulation over production. In other words, oligopoly environment prevails. But each producer differentiates his product that he would be able to stay in the market. Technology and innovation ensure the stability and growth of organizations. As a result only efficient organization would survive. The resources would be fully utilized. The system is so flexible that it can adjust itself for any economic condition. The workers get equal opportunities and those with skills would be able to command better wages and salaries. On the whole capitalism offers scope for growth of efficient individuals and organizations. But capitalism has a number of weaknesses. The important ones are discussed below. 1. Economic inequality is invariably found in capitalistic societies. Individuals and organizations with ownership of resources and hold over the market for (heir product or service, would be able to maximize their gains. Those who have no such property would remain poor and become poorer. So it is said that under capitalism, rich becomes richer and poor becomes poorer. The inequality in wealth and income widens over a period under capitalism. 2. The scope for the emergence of monopolies in capitalistic societies is very high. Organizations by virtue of their economic power would be able to easily eliminate rivals and competitors in the market. There is also possibility of such monopolies influencing the government in policy making and intervention. 3. Though it is said that capitalism would always lead to ideal allocation of resources and fuller utilization of resources, in reality the experience is that resources are held by individuals and organizations and under utilization is the result. Sometimes, products which are not really national priority are produced and forced on the public, through advertisements and sales promotion techniques. 4. Though it is expected that in capitalistic societies the output would increase to optimal level, in. practice this is never found. Producers always restrict output to maintain a high price and also maximize profit. So excess capacity would exist in many industries. 5. In a capitalistic society the divide between the haves and have-nots widen that over a period. Existence of poverty among the sophisticated sections of people is also seen. This results in built up of frustration in the society. Over a period this might lead to revolution and social upheaval. 2. Socialism Socialism refers to an economic system ir which the following features predominant: The resources are owned by the State or state owned institutions. Production takes place in the interest of the society and not for maximizing profits of individuals or organizations. Government decides the type of productive efforts to be permitted. In other words, in a socialist country, government can adopt licensing system and other types of regulations to prevent the emergence of monopolist and exploitative tendencies. Maximization of Community welfare is the objective than profit maximization. Another very important feature is the government ensures equitable distribution of national product. Public distribution system assumes enormous significance in such an economic system. On the whole, the socialistic society differs from capitalist society in every sense. In the broad spectrum of economic systems, socialism and capitalism occupy two extremes. In the world today, pure capitalistic society is not seen in any country. Even in USA, government interference in various economic activities is found. For example, in the field of national defense, atomic energy, space technology, social security, etc., the presence of government is almost complete. Government also retains the right to interfere in the market system, whenever there is deliberate and intentional attempt to monopolize the resource ownership or the market. Similarly, in the erstwhile Soviet Union, socialistic principles were followed. But even here, there were instances of private ownership of property, enterprises, etc., were reported. - That is why it is very difficult to come across pure capitalistic or socialistic societies. The merits of socialism includes: 1. Collective ownership eliminate emergence and existence of monopolies. 2, Resources utilization is planned and achieved in the interest of the society. 3. Government with its control over the resources is able to use resources fully utilized and avoid wastage and production of unnecessary goods. 4. As equality in distribution is the fundamental feature of socialism, there is no scope for widening inequalities rind the government takes steps to narrow the gap between the rich and the poor through various measures. However, socialistic states suffer from the following limitations: 1. Excessive dependence on government decisions often result in delay in offering any public service. 2. Bureaucratic control becomes an integral part of the socialistic principles. As a result the benefits and its direction of flow is determined by the bureaucrats. 3. Government by undertaking excessive responsibility on its shoulders, abets inefficiency and corruption in the society. 4. No incentive and motivation for individual excellence or achievements is possible in such a society and so innovations and inventions do not really lake place in large scale in such a society. 5. With governmental presence in every walk of life, efficiency and productivity suffer. 6. Lack of support for individual liberty kills initiative. 3. Mixed economy Evolution of the concept of Mixed economy: There was no reference to the mixed economic system in Economic literature in the past. Economists were mainly familiar and advocated the Laissez faire or free enterprise system, as several countries could develop fast following the free enterprise system, in which there was no or little government intervention. The entire economic system operated with the price mechanism at its center point. The producers produced what the consumers wanted and this provided very little scope for the government to intervene in the system. The Classical economists and their ardent supporters believed that the invisible hand will direct the economy and with private initiative and enterprise, every country should be able to record a faster growth as proved in the case of UK, USA, Europe, Australia, and other countries. But over a period under the leadership of Karl Marx, a new economic system was developed called socialism, in which there is no scope for any private enterprise as everything owned and controlled by the government. The government decided the type of developmental activities and me requirements of the society and used the available resources in the provision of these requirements. Several countries like USSR, Communist China, Vietnam, Cuba and others preferred this socialist system in which government is made the custodian of the society. The main reason for Die emergence of this new economic system was the failure of capitalism during the 1929 depression to revive every economy from depression. Keynes himself thought that capitalism without some of its evils could certainly help economic recovery. Hence, a time came when economists felt that cent per cent free enterprise or cent per cent government governed economic development cannot work satisfactorily. A compromise between these extremes was thought of as an ideal economic system. The new system called 'mixed economic system' contained the merits of both the capitalism and socialism and appeared to be full of promise. This mixed economic system is adopted by India as indicated by the First Industrial Policy Resolution 1948. Characteristics of mixed economy: i. Co-existence of public and private sectors: In a mixed economy, one will find the existence of both the private and public sectors. In such a system, the government will undertake the responsibility to build and develop certain sector activities and leave the other activities for the private initiative. In India, the government announced the adoption of the mixed economy system through its 1948 Industrial Policy Resolution. The government clearly earmarked the industries to be completely under the state control, the industries which are to owned and controlled by the state as well as the private sector and industries which are completely left for the private sector. In this way the Resolution provided for the simultaneous existence of both private and public sectors. ii. State participation in economic development: This is the second feature of mixed economy, according, to which the state reserves its right to design and decide the type of development to be achieved. In such a set up, the government strives to promote the welfare of the country by ensuring social order, social justice and establishing all the necessary institutions which are required to achieve the desired pattern of growth and development. iii. Distribution of ownership and control of resources: This is the next feature of mixed economy. In this system, the government itself enters the field of production so that the available resources are fully utilized. This will also help to avoid concentration of wealth in the hands of a few and enable distribution of ownership and control of productive activities. As a result there is no scope for exploitation of any group, say labor, by any other group. In this way the weaker section of the community is well protected and taken care of. Only the mixed economy will enable the government to attain the objectives of the Directive Principles of the Indian Constitution. iv. Directing the investment in socially desirable projects and channels: Mixed economy facilitates the flow of investment into channels which confers the society with several benefits. For example, the Indian government has invested huge amount in several projects to develop the infrastructural facilities. This forms the basis for the development of other sectors. The investment in these infrastructural areas will not come forth from the private sector as the return is nil. Hence, the government in a mixed economic set up provides the thrust by developing the necessary background and strength which will encourage the private sector to invest in profitable opportunities. In this way the government plays a key role in a mixed economic system. v. Scope for achieving balanced economic development: I Left to itself, the private sector would establish its enterprises only in urban or sub-urban areas and that too in already well developed states. This will mean other areas will have no scope for development. But in a mixed economy, the government will itself undertake the initiative to set up industries in backward areas and encourage the private initiative to set up industries in such areas by offering several concessions and exemptions. In the absence of nixed economy, several states in India would have remained industrially backward. vi. Ultimate control and regulation in the hands of government: This feature of mixed economy clearly spells out that in every activity affecting the economy, the government will be the ultimate authority. Though the private sector is assigned its role to perform, the government will still monitor and control the way in which the private initiative is performing its role. Infact, according to the 1948 Industrial Policy Resolution, the government made it clear that the industries already established by the private sector belonging to that category in which new industries will be established by the government alone, the government would undertake the review of the working of these industries in private sector after a period of ten years and if found not satisfactory, they would be taken over by the government. Though this was criticized as a threat of nationalization, yet through such a provision the government underlines its authority. Similarly in the banking and insurance sectors, the government nationalized banks emphasizing its powers to control and regulate any sector. vii. Co-operation in the field of economic development: According to this feature of mixed economy, the government formulates the design for development and invites the private sector to participate in the development. It clearly spells out the guidelines which would govern such cooperative efforts and the limits of freedom granted to the private sector. In Indian case, the government prepares the plans for development and spells out the areas left for the private initiative and the areas that will be under state control. Hence, there is scope for the development of private sector, though only according to the design developed by the government. Planning process under mixed economy: As has been already stated, in a mixed economy there is a need to achieve a compromise between self-interest and social interest This is a very difficult task as the government has to carefully foresee the type of development it wants to achieve and closely monitor the activities of the private sector to ensure that the social interest is never at stake. Obviously, planning is a very difficult exercise in a mixed economy set up. The success of planning will depend upon; i) the extent to which the public sector is able to rise to achieve the social gains aimed for, ii) the success of the state in guiding and regulating the private sector activities towards social goals and iii) the extent lo which (lie state is able (o check the distortions taking place in investment by private sector affecting (he interest of the public sector. Hence in the planning process the state has taken up the following steps to ensure the accomplishment of the objectives of the mixed economy, a. By holding complete ownership of defense and heavy industries, the government has provided an industrial base with which the private sector is expected to plan its investment activities. b. The state also has made huge investments in economic infrastructures so as to help the extension of market for goods, raising the productivity in agricultural and industrial sectors, encouragement of further productive investment c. The government has complete control of the financial institutions including banks so that it can ensure that the banks and other institutions play a key role in the development activities of the state. The government could also realize the expected gains by encouraging the priority activities in every sector. The economic institutions are made to support the weaker sections of the community. d. Through powerful legislations like MRTP Act, FERA, etc., the government could ensure that there is no scope for exploitation of the common people by the private enterprise. Such a legal framework lays down the rules of the game and ensures fair play in a mixed economic set up. e. As a method of protecting the weaker and downtrodden people, the government has policies like rationing, price controls, etc. Such regulations are built in the planning mechanism itself, so that the private sector cannot exploit the community. f. Towards the improvement of welfare in the economy, the state has undertaken several specific programs aimed at specific target groups. For example schemes aimed at the backward and schedule tribe providing them reservation in educational, employment and other opportunities, rural oriented schemes for the rural folks, health for all schemes, provision of free educational and medical facilities up to a certain level, etc. All these schemes aim at improving the social welfare. In all these activities the private sector is also welcome to play its role. g. The government