INTERNATIONAL BUSINESS ENVIRONMENT

M.Com Sem-IV

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Meaning of Business Environment:

Business Environment is the sum total of all external and internal factors that affect business. You should keep in mind that external factors and internal factors can influence each other and work together to influence a business. Business environment refers to all the external economic, social, political and natural forces that affect business and its operation.

All these powers are governed by the control of business, meaning that business has no control over all these, but they affect the business. In this way the business environment is made up of a combination of different components over which we have no control and more and more we can study and adjust ourselves. Business environment is the sum of various social, economic, political and legal and a condition under which business has to work.

Definition "The sum total of all individuals, institutions and other forces that are outside the control of a business enterprise but the business still depends upon them as they affect the overall performance and sustainability of the business."

Features of the Business Environment:

The following are the salient features of the business environment:

Dynamic Nature: - The components of business environment are constantly changing. It has an impact on business. It is therefore said that business environments are dynamic.

Uncertainty: - Business environments are uncertain and it is difficult for businessmen to forecast these uncertainties.

Complexity: - business environment consists of many components. All these components are related to each other. This is why it is very difficult for businesses to cope with them.

Inter-Dependence: - Different components of business environment are related to each other.

Totality of External Forces: - Business environment is the sum of all the powers that are available outside the business and which the business has no control over. This is not one, but a group of many different powers, so their nature is of perfection.

The following are parts of the business environment:

Internal Environment

The internal environment encompasses all the components that affect the business and within the business itself.

These components are often:

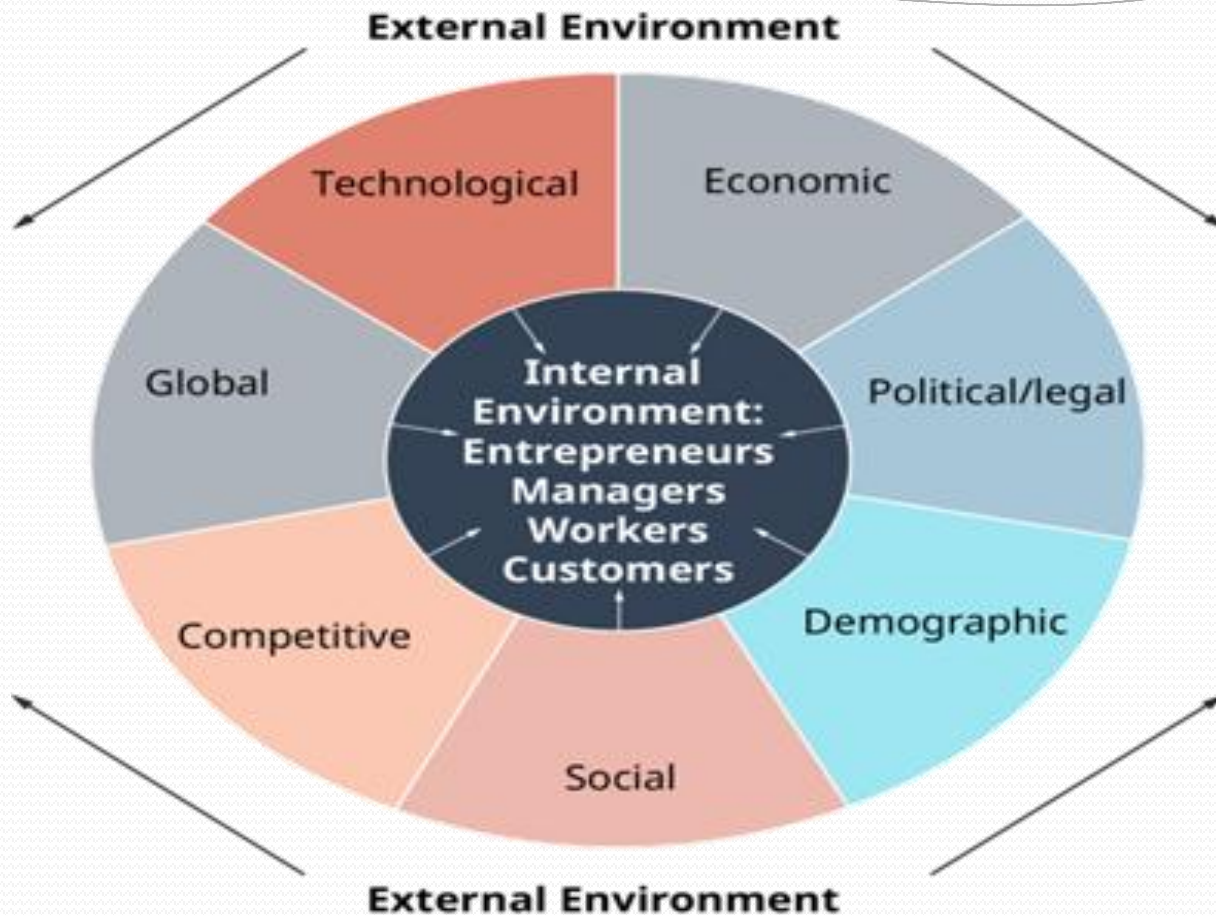
- **Objectives of Business**
- **Business Policies**
- **Production Capacity Of Business**
- **Participation in Management**
- **Management Information System**

External Environment

The external environment of the business includes components that are outside the business and affect the business.

The outdoor environment is divided into two parts:

- **Functional environment**
- **General environment**



Source :https://opentextbc.ca/businessopenstax/chapter/understanding-the-business-environment/

- **Importance of Business Environment:**

1. **Enables to Identify Business Opportunities**
2. **Helps in Tapping Useful Resources**
3. **Coping with Changes**
4. **Assistance in Planning**
5. **Helps in Improving Performance**

- **Elements of Business Environment:**

Elements of the business environment can be divided into the following parts:

- **Political Environment**
- **Economic Environment**
- **Social Environment**
- **Technological Environment**
- **Legal Environment**
- **Demographic Environment**
- **Natural Environment**
- **International Environment**

Elements of Business Environment:

Economic Environment: - Out of all the elements of business environment, the economic environment is a complex system. It has many components such as economic conditions, economic policies, economic systems, capitalist system etc.

Social Environment: - Businessman must have social knowledge because society is the basis of business. Under social knowledge comes social values, social institutions, social beliefs, education, social beliefs, etc. The social environment affects one's business in different ways.

Political environment: - Political environment also greatly affects business environment. Business has to perform its actions according to the government's point of view. Political decisions change the direction of business.

Legal Environment: - Under the legal environment, different types of legal policies, different statutory controls are included. There is a close relationship between business and law. The businessman always has to work within the purview of law.

Technical environment: - Under the technical environment, new devices, mechanical improvements, system discovery, design, new development etc. are included.

- **Economic Environment:**

Economic Environment consists of Gross Domestic Product, Income level at national level and per capita level, Profit earning rate, Productivity and Employment rate, Industrial, monetary and fiscal policy of the government etc.

The economic environment factors have immediate and direct impact on the businessman so businessmen must scan the economic environment and take timely actions to deal with these environments. Economic environment may put constraints and may offer opportunities to the businessman.

Some Aspects of Economic Environment:

1. **Role of Private and Public sector**
2. **Rate of growth of GDP, GNP, and Per Capita Income**
3. **Rate of Saving and Investment**
4. **Balance of Trade**
5. **Balance of Payment**
6. **Transport and Communication System**
7. **Money Supply in the Economy**

Economic systems:

An economic system is a means by which societies or governments organize and distribute available resources, services, and goods across a geographic region or country. Economic systems regulate factors of production, including capital, labor, physical resources, and entrepreneurs. An economic system encompasses many institutions, agencies, and other entities.

An economic system, or economic order, is a system of production, resource allocation and distribution of goods and services within a society or a given geographic area. It includes the combination of the various institutions, agencies, entities, decision-making processes and patterns of consumption that comprise the economic structure of a given community. As such, an economic system is a type of social system. The mode of production is a related concept.

Which include the following subcategories of different systems?

- Planning, coordination and reform.
- Productive enterprises; factor and product markets; prices; population.
- Public economics; financial economics.
- National income, product and expenditure; money; inflation.
- International trade, finance, investment and aid.
- Consumer economics; welfare and poverty.
- Performance and prospects.
- Natural resources; energy; environment; regional studies.
- Political economy; legal institutions; property rights.

- **Economic policy:**

Economic policy refers to the actions that governments take in the economic field. It covers the systems for setting interest rates and government budget as well as the labor market, national ownership, and many other areas of government interventions into the economy. Such policies are often influenced by international institutions like the International Monetary Fund or World Bank as well as political beliefs and the consequent policies of parties.

- **Types of Economic Policy:**

Three main types of economic policy:

Fiscal policy: Changes in government spending or taxation.

Monetary policy: Changes in the money supply to alter the interest rate (usually to influence the rate of inflation).

Supply-side policy: Attempts to increase the productive capacity of the economy.

Fiscal and monetary policy comes in two types:

Expansionary: Intended to stimulate the economy by stimulating aggregate demand.

Expansionary fiscal policy involves increasing government spending or reducing taxes. Increasing government spending increases aggregate demand directly, whereas decreasing taxes increases aggregate demand indirectly by increasing consumption and investment.

Expansionary monetary policy involves increasing the money supply, which decreases the interest rate and stimulates consumption, investment and net exports.

Consumption increases because borrowing is now cheaper, but also because people need to spend less on things such as mortgage interest payments. Investment increases because the opportunity cost of investment (the return from sticking the money in a savings account) has fallen Net exports increase because a fall in the interest rate makes holding the domestic currency less attractive, which causes it to depreciate, making exports cheaper and imports more expensive.

Contractionary: Intended to slow the economy down by decreasing aggregate demand. It's the opposite of expansionary policy, in that it involves reducing government spending, increasing taxes or reducing the money supply.

Supply-side policies are designed to increase the natural level of output, for example, by making markets work better, increasing the level of investment or increasing the rate of technological progress. Examples are making the labour market more flexible, giving firms incentives to invest or engaging in research and development.

- **Monetary policy:**

Monetary policy consists of the process of drafting, announcing, and implementing the plan of actions taken by the central bank, currency board, or other competent monetary authority of a country that controls the quantity of money in an economy and the channels by which new money is supplied. Monetary policy consists of management of money supply and interest rates, aimed at achieving macroeconomic objectives such as controlling inflation, consumption, growth, and liquidity. These are achieved by actions such as modifying the interest rate, buying or selling government bonds, regulating foreign exchange rates, and changing the amount of money banks are required to maintain as reserves.

Definition: Monetary policy is the macroeconomic policy laid down by the central bank. It involves management of money supply and interest rate and is the demand side economic policy used by the government of a country to achieve macroeconomic objectives like inflation, consumption, growth and liquidity.

Monetary policy is the policy adopted by the monetary authority of a country that controls either the interest rate payable on very short-term borrowing or the money supply, often targeting inflation or the interest rate to ensure price stability and general trust in the currency.

Monetary policy refers to a regulatory policy whereby the central bank maintains its control over the supply of money to achieve the general economic goals. Main instruments of the monetary policy are: Cash Reserve Ratio, Statutory Liquidity Ratio, Bank Rate, Repo Rate, Reverse Repo Rate, and Open Market Operations.

❖ Instruments of Monetary Policy:

The instruments of monetary policy are of two types:

1. Quantitative, general or indirect (CRR, SLR, Open Market Operations, Bank Rate, Repo Rate, Reverse Repo Rate)

2. Qualitative, selective or direct (change in the margin money, direct action, moral suasion)

These both methods affect the level of aggregate demand through the supply of money, cost of money and availability of credit. Of the two types of instruments, the first category includes bank rate variations, open market operations and changing reserve requirements (cash reserve ratio, statutory reserve ratio).

Policy instruments are meant to regulate the overall level of credit in the economy through commercial banks. The selective credit controls aim at controlling specific types of credit. They include changing margin requirements and regulation of consumer credit.

a. Bank Rate Policy:

The bank rate is the minimum lending rate of the central bank at which it rediscounts first class bills of exchange and government securities held by the commercial banks. When the central bank finds that inflation has been increasing continuously, it raises the bank rate so borrowing from the central bank becomes costly and commercial banks borrow less money from it (RBI).

The commercial banks, in reaction, raise their lending rates to the business community and borrowers who further borrow less from the commercial banks. There is contraction of credit and prices are checked from rising further. On the contrary, when prices are depressed, the central bank lowers the bank rate.

It is cheap to borrow from the central bank on the part of commercial banks. The latter also lower their lending rates. Businessmen are encouraged to borrow more. Investment is encouraged and followed by rise in Output, employment, income and demand and the downward movement of prices is checked.

b. Open Market Operations:

Open market operations refer to sale and purchase of securities in the money market by the central bank of the country. When prices start rising and there is need to control them, the central bank sells securities. The reserves of commercial banks are reduced and they are not in a position to lend more to the business community or general public.

Further investment is discouraged and the rise in prices is checked. Contrariwise, when recessionary forces start in the economy, the central bank buys securities. The reserves of commercial banks are raised so they lend more to business community and general public. It further raises Investment, output, employment, income and demand in the economy hence the fall in price is checked.

c. Changes in Reserve Ratios:

Under this method, CRR and SLR are two main deposit ratios, which reduce or increases the idle cash balance of the commercial banks. Every bank is required by law to keep a certain percentage of its total deposits in the form of a reserve fund in its vaults and also a certain percentage with the central bank.

When prices are rising, the central bank raises the reserve ratio. Banks are required to keep more with the central bank. Their reserves are reduced and they lend less. The volume of investment, output and employment are adversely affected. In the opposite case, when the reserve ratio is lowered, the reserves of commercial banks are raised. They lend more and the economic activity is favorably affected.

2. Selective Credit Controls:

Selective credit controls are used to influence specific types of credit for particular purposes. They usually take the form of changing margin requirements to control speculative activities within the economy. When there is brisk speculative activity in the economy or in particular sectors in certain commodities and prices start rising, the central bank raises the margin requirement on them.

a. Change in Margin Money:

The result is that the borrowers are given less money in loans against specified securities. For instance, raising the margin requirement to 70% means that the pledger of securities of the value of Rs 10,000 will be given 30% of their value, i.e. Rs 3,000 as loan. In case of recession in a particular sector, the central bank encourages borrowing by lowering margin requirements.

b. Moral Suasion:

Under this method RBI urges to commercial banks to help in controlling the supply of money in the economy.

Objectives of Monetary Policy in India:

While the main objective of the monetary policy is economic growth as well as price and exchange rate stability, there are other aspects that it can help with as well.

Promotion of saving and investment: Since the monetary policy controls the rate of interest and inflation within the country, it can impact the savings and investment of the people. A higher rate of interest translates to a greater chance of investment and savings, thereby, maintaining a healthy cash flow within the economy.

Controlling the imports and exports: By helping industries secure a loan at a reduced rate of interest, monetary policy helps export-oriented units to substitute imports and increase exports. This, in turn, helps improve the condition of the balance of payments.

Managing business cycles: The two main stages of a business cycle are boom and depression. The monetary policy is the greatest tool using which the boom and depression of business cycles can be controlled by managing the credit to control the supply of money. The inflation in the market can be controlled by reducing the supply of money. On the other hand, when the money supply increases, the demand in the economy will also witness a rise.

Regulation of aggregate demand: Since the monetary policy can control the demand in an economy, it can be used by monetary authorities to maintain a balance between demand and supply of goods and services. When credit is expanded and the rate of interest is reduced, it allows more people to secure loans for the purchase of goods and services. This leads to the rise in demand. On the other hand, when the authorities wish to reduce demand, they can reduce credit and raise the interest rates.

Generation of employment: As the monetary policy can reduce the interest rate, small and medium enterprises (SMEs) can easily secure a loan for business expansion. This can lead to greater employment opportunities.

Helping with the development of infrastructure: The monetary policy allows concessional funding for the development of infrastructure within the country.

Allocating more credit for the priority segments: Under the monetary policy, additional funds are allocated at lower rates of interest for the development of the priority sectors such as small-scale industries, agriculture, underdeveloped sections of the society, etc.

Managing and developing the banking sector: The entire banking industry is managed by the Reserve Bank of India (RBI). While RBI aims to make banking facilities available far and wide across the nation, it also instructs other banks using the monetary policy to establish rural branches wherever necessary for agricultural development. Additionally, the government has also set up regional rural banks and cooperative banks to help farmers receive the financial aid they require in no time.

- **Fiscal policy:**

Fiscal policy refers to the use of government spending and tax policies to influence economic conditions, including demand for goods and services, employment, inflation, and economic growth.

Fiscal policy is the means by which a government adjusts its spending levels and tax rates to monitor and influence a nation's economy. It is the sister strategy to monetary policy through which a central bank influences a nation's money supply. These two policies are used in various combinations to direct a country's economic goals. Here's a look at how fiscal policy works, how it must be monitored, and how its implementation may affect different people in an economy.

Fiscal policy is the use of government spending and taxation to influence the economy. Governments use fiscal policy to influence the level of aggregate demand in the economy in an effort to achieve the economic objectives of price stability, full employment, and economic growth.

The government has two levers when setting fiscal policy:

Change the level and composition of taxation, and/or
Change the level of spending in various sectors of the economy.

There are three main types of fiscal policy:

Neutral: This type of policy is usually undertaken when an economy is in equilibrium. In this instance, government spending is fully funded by tax revenue, which has a neutral effect on the level of economic activity.

Expansionary: This type of policy is usually undertaken during recessions to increase the level of economic activity. In this instance, the government spends more money than it collects in taxes.

Contractionary: This type of policy is undertaken to pay down government debt and to cap inflation. In this case, government spending is lower than tax revenue.

Objectives of Fiscal Policy

Generally following are the objectives of a fiscal policy in a developing economy:

1. **Full employment**
2. **Price stability**
3. **Accelerating the rate of economic development**
4. **Optimum allocation of resources**
5. **Equitable distribution of income and wealth**
6. **Economic stability**
7. **Capital formation and growth**
8. **Encouraging investment**

Importance of Fiscal Policy in India:

- In a country like India, fiscal policy plays a key role in elevating the rate of capital formation both in the public and private sectors.
- Through taxation, the fiscal policy helps mobilize considerable amount of resources for financing its numerous projects.
- Fiscal policy also helps in providing stimulus to elevate the savings rate.
- The fiscal policy gives adequate incentives to the private sector to expand its activities.
- Fiscal policy aims to minimize the imbalance in the dispersal of income and wealth.

Difference between Monetary and Fiscal policy:

The government uses both monetary and fiscal policy to meet the county's economic objectives. The central bank of a country mainly administers monetary policy. In India, the Monetary Policy is under the Reserve Bank of India or RBI. Monetary policy majorly deals with money, currency, and interest rates. On the other hand, under the fiscal policy, the government deals with taxation and spending by the Centre.

- **Monetary policy involves changing the interest rate and influencing the money supply.**

- **Fiscal policy involves the government changing tax rates and levels of government spending to influence aggregate demand in the economy.**

They are both used to pursue policies of higher economic growth or controlling inflation.

Fiscal Policy	Monetary Policy
Change in government spending and tax rates	Change in interest rates / money supply.
Set by the Government	Set by a Central bank
No specific target	Target inflation
Side effect on government budget / borrowing	Side effect on exchange rate and housing market
Strong political dimension to changing tax rates	Mostly independent from the political process www.economicshelp.org

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thank you!