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MFA Made Easy (Managerial Portion)

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STUDY NOTES

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CH # 1 POLITICAL ENVIRONMENT AND BUSINESS

INTRODUCTION

Tutor
Note

The environment of an organisation is a term that describes anything outside an organisation that affects what it does or how it acts.

A famous method of analysing environmental factors is **PESTEL**
- **P** – Political factors
- **E** – Economic factors
- **S** – Social, cultural and demographic influences
- **T** – Technological factors.
- **E** – Ecological factors
- **L** – Legal factors

Significance of environmental factors and its understanding

- These factors can have a significant effect on organisation
  - Can affect its activities and profitability
  - Might affect the planning and other decision-making
- Management should monitor developments in the environment, and should consider how organisation should respond to that.
- This type of analysis is sometimes called an **environmental scan**.

- Politics in the world started since the establishment of society after agricultural revolution.
- Politics has been evolving since then according to experiences of society and their needs.
- We cannot find a single definition of politics which can satisfy all the intrinsic values.
  - *"Politics is the most concentrated expression of economics" (Vladimir Lenin)*
  - *"Politics is distinctive form of rule whereby people act together through institutionalized procedures to resolve differences, to conciliate diverse interests and values and to make public policies in pursuit of common purposes." (Bernard Rowland Crick)*
- Politics has direct or indirect impact on state, society, individual, economy and government
- Business activity is always dependent on the political policy and decision making.
- The political setup in any country depends upon various factors such as,
  - Political ideology of the ruling political party.
  - Pre-existing laws and regulations
  - Socio-religious constraints.
  - Political opposition and their economic agendas.
- To become a successful business manager, one should take into consideration the political environment for business, and then capitalize on opportunity available and mitigate risks.

THE SPECTRUM OF POLITICAL IDEOLOGIES

Communism Extreme Left Radicals Dictatorial socialism

- All means of production must be in the hands of state
- No private property
- Distribution of state earnings on the basis of the need of people.
- Production by the state industries would be based on the needs of people
- Egalitarian, class less society, where everyone has equal material.
- No individual freedoms.
- It is comprehensive political system which has its own economic system.
- There is no room for ‘organized religion’. (They consider religion as ‘opium of masses.’)
- However individual religion is supported in some form.
- Communists want change through any means possible including violence.
- Soviet Union is an example

Liberals Left wing Democratic Socialism

- Most and important means of production in hands of state with few exceptions are allowed.
- Private property is allowed.
- It recognizes the distinction amongst people based on their ability and their contribution.
- Distribution of output amongst people should be based on their input.
- Challenges ‘status quo’.
- People are responsibility of state, and it needs to regulate business through laws.
- Religion is allowed in this system
- They favor change through peaceful means.
- Everyone is equal in-front of the law.
- Implementation of ideology through social change.
- Major characteristics are collectivism, economic equality, social service, nationalization.
- Sweden is an example

Centre Moderates Democracy

- They want change but not at the cost of tradition.
- State must play the role of guardian for all.
- Individual freedom is recognized.
- Full religious freedom.
- Private property is allowed.
- Ownership of private and public means of production needs to be balanced.
- They believe in international cooperation for the benefit of all however they also recognize their national interests.
- Slow social change.
- Canada is an example

Conservatism Right Wing Laissez Faire Democratic Capitalism

- Free market, open competition
- Elitist and oligarchy (rule by the few rich and powerful)
- Law favors the elite.
- Maximum private property with least ownership of means of production by state.
- Maintain 'status quo'.
- Attainment of national or state goals by any means possible, including amending the laws.
- Individual liberties are recognized with exceptions.
- Religious practice in all forms is allowed.
- Large corporations can flourish in this system and charge consumers as much as they want.
- There is a tendency of suppression and oppression by majority.
- Attainment of National Interest over international cooperation.
- Power Politics.
- United States is an example

Fascist Capitalism Extreme Left Dictatorial Capitalism Reactionaries

- No individual freedom.
- Authoritarian rule.
- Private property as prescribed by the ruling regime.
- Extreme inequalities.
- Protection of national interest at all costs.
- Implementation of ideology through any means possible, including violence.
- This system does not allow dissenting opinion.
- Nazi Germany, Fascist Italy and Spain are examples

IMPACT OF POLITICAL IDEOLOGIES ON BUSINESSES

- Many political decisions have serious economic and business implications.
- Important economic policies such as industrial policy, policy towards foreign capital and technology, fiscal policy and foreign trade policy are often political decisions.
- Business manager has to be familiar with ideologies and past approaches of key political parties to analyze possible future policies of existing and forthcoming ruling parties.

Several ways in which political factors can affect business

Government spending

- Direction of state spending is based on its inherent political ideology.
  - Govt inclined towards left would spend on public, free health, education for all etc
  - Right- wing state would spend more on defense, international security, alliances etc

Taxation

- Various ideologies propose different sorts of (direct & indirect) taxation.
- Tax policies can have a massive effect on a business' overhead and profit margins.
- These policies may be used to:
  - Reduce income of individuals and companies and thus reduce private expenditures
  - Provide resources for public expenditures (roads, public schools, hospitals or parks)
  - Exercise control over the private sector investment
  - Improve country's business competitive position

Economic policies

- Different political parties or individuals enact different policies to guide national economy
- A pro-agriculture political approach may not be able to pay attention to other sectors.
- An ideology relying on non-agriculture sector for economic growth may manage economy that is not conducive for agriculture sector.

Labor Laws

- Political parties often focus minimum wages, insurance requirements, labor regulation etc
- Local labor laws are also affected by international labor regulations.
- Some Western economies do not allow imports from such countries who do not ensure labor health policies, labor safety from fire hazard, proper work load etc.

International relationship and policies

- An ideology that support good international relation and welcomes foreign investments will have direct impact on sustainability of local businesses.
- A protectionist policy (to save and promote own industry) may have different impact.

INTERACTION BETWEEN BUSINESSES AND THE GOVERNMENT

- Pressure groups and lobbying are 2 ways in which government decisions and policies are managed by business owners.
- Political parties need the support of businesses – especially larger, influential ones (votes, contributions to economy, reduction of unemployment and party funding etc)
- Business manager should keep an eye on political parties influenced by their supporters from business community and pressure groups of businesses.

Financial incentive strategy
- Businesses may use their economic leverage to influence public policymakers.
- They can use economic power to threaten to leave a city, state, or country unless a desired political action is taken (that would favor the business).

Promoting a Constituency-Building Strategy

- Businesses may influence political environment by seeking support from organizations or people who are also affected by policy or who are concerned with business's position.
- Some of the influencing approaches are as follows:

Stakeholder Coalitions	- Business may try mobilize employees, stockholders, customers, and local community to support their political agenda. - If political issue is negative for business, it's also negative for stakeholder - Often, businesses organize programs to get stakeholders, acting as lobbyists or voters, to influence government officials
Advocacy Advertising	- These ads focus on organization's views on controversial political issues. - These issue advertisements can appear in newspaper, TV, or other media
Trade Associations	- Its coalitions of companies in the same or related industries - To coordinate efforts in promoting common interests of industry - Some examples are: * Federation of Pakistani Chambers of Commerce & Industry * Overseas Investors Chambers of Commerce and Industry (OICCI), * All Pakistan Textile Manufacturers Association (APTMA) voiced its concerns over load shedding and hike in industrial tariffs since - They represent many businesses include companies of all sizes & sectors - The associations also publish widely circulated magazines and newsletters

Managing the Political Environment - the Public Affairs Department

- In many organizations, managing political activity falls to department of public affairs
- Role of the public affairs department is to manage the firm's interactions with governments at all levels and to promote the firm's interests in the political process.
- Creation of public affairs units is now a global trend
- Typical public affairs executive spends most of the day direct lobbying with politicians, hosting visits by politicians to the company's locations, or attending fund-raising activities.

THE ROLE OF POLITICS IN PAKISTAN'S ECONOMY

Period I: Early Foundations, 1947 to 1958
(During this time 4 governor generals and 7 Prime Ministers were changed)

- After death of first prime minister, Liaquat Ali Khan (16th Oct 1951), and rise of bureaucrat Ghulam Mohammed to Governor-General, supremacy of politicians was weakened.
- On 17th April 1953 he replaced political PM with another bureaucrat Mohammad Ali Bogra.
- On 24 Oct. 1954 Ghulam Mohammad dissolved the first Legislative Assembly and replaced with handpicked cabinet (e.g Gen. Ayub Khan, Chief of Army, was made defense minister)
- Political instability was too severe; tensions between tiers of government were damaging;
- Challenge of setting up the state institutions was so difficult
- Influx of millions of refugees from India was also too demanding.
- Economy was also affected by stoppage of water into Indus river system by India in 1948
- With all political instability, businesses had opportunity to invest and grow with minimum competitive pressures.

Period II: Gen Ayub Khan, 1958 to 1969
(Ayub Khan took government after military coup and left after country vide protests)

- Under Ayub Khan, first military regime took administrative and political charge of Pakistan
- Assumed complete control of the state on 7th October 1958 and ruled over almost 11 years
- Economy was quickly revitalized under Ayub Khan, with economic growth averaging 6%
- Agenda was to produce quick results and they allowed investment by anyone with capital.
- Hundreds of units were established across the country and rich became more richer
- Manufacturing growth was exceptionally 8.51%
- Pakistan established its first automobile and cement industries
- Government constructed several dams, (notably Tarbela Dam and Mangla Dam), canals, and power stations, in addition to launching Pakistan's space program.
- Agriculture grew at good rate of 4% with introduction of Green Revolution technology.
- By 1969, Pakistan’s manufactured exports were higher than combined exports of Thailand, Malaysia and Indonesia.
- Tax collection was low (due to tax holidays) averaging less than 10% of GDP.
- Bonus vouchers facilitated access to forex for imports of machinery and raw materials
- Tax concessions were also offered for investment in less- developed areas.
- Ayub Khan banned all political parties, banned politicians on corruption charges, dismissed civil servants, curtailed judicial powers, restricted free press & introduced basic democracy
- All these successes were achieved through concentration of wealth in a few hands
- However, perception that income inequalities had increased substantially and that wealth was concentrated in the hands of 22 families fueled resentment among common people.
- During this era the businesses were carrying a risk of serious reaction from masses due to increasing perception about government’s policies being supporting elite class.
- In East Pakistan there was feeling of non-inclusiveness in power expected to create hostile environment for businesses in East Pakistan owned by West Pakistan’s residents.
- Single biggest spending during this time was establishment of Islamabad as new capital.

Period III: Bhutto's Socialist Movement, 1971 to 1977
(Z.A. Bhutto took charge after fall of Dhacca replaced by Zia through militarycoup)

- Bhutto took advantage of anger against Ayub's economic policies and promised to restore the principles of distributive justice and equity under slogan of Islamic socialism.
- Bhutto's policies of nationalizing industries, banks, insurance companies, educational institutions and other organizations, slowed down journey toward modernization
- Oil price shock of the 1970s as well as floods and withdrawal of external assistance also contributed to the slowing pace of economic growth.
- Growth rate in 1970s fell to 3.7% per annum from 6% in the 1960s.
- Income inequalities rose more while inflation accelerated, thereby hurting the poor.
- Economic policies aimed control of the leading enterprises in the hands of the state.
- Labour reforms were also initiated, giving labour far greater rights than in the past.
- Bhutto was committed to alter the feudal system and undertook extensive land reforms to redistribute balance of power (through government intervention in all areas)
- Bhutto period witnessed widespread improvement of agriculture to benefit rural classes.
- Banking sector, which was earlier confined to the urban areas, underwent a revolution and shifted from class banking to mass banking, with an extended reach into rural areas
- Typical to a socialist ideology Z. A. Bhutto's was interested in policies that largely benefited the poor and working class to reduce poverty levels.
- In Bhutto regime businesses re-aligned their focus and investment strategies.
- Nationalization resulted in flight of capital and entrepreneurs outside Pakistan.
- Moreover, further private investment in large scale industry was discouraged.
- This encouraged the cottage industries to capture the space created by large industries
- Businesses in a leftist (socialist) regime may benefit by focusing their efforts on the opportunities created from the shifting focus from urban centers to the masses.
- Growth and profitability for the business can be created that focuses on public and masses.

Period IV: The Eighties, 1977 to 1988
(Zia's military government ended with a bomb blast in his plane)

- Bhutto government was overthrown by a military coup in July 1977
- Government control was taken over by a right wing military leader, General Zia ul-Haq.
- Political party activity was soon banned, limiting political participation to local level only.
- Political ideology was based on religion, centralization & personal control over state affairs
- This was the 3rd and longest rule of a military dictator in Pakistan.
- Zia benefited from participating in campaign to overthrow the Soviet Union in Afghanistan
- Large amounts of military and economic assistance from the US flowed into Pakistan.
- The long-term costs were, however, affecting the overall country in the adverse manner.
- Economic conditions, however, did improve: GDP grew at 6.6% annually, with agriculture at 4% and manufacturing sector at 9%.
- But fiscal deficits widened to 8% of GDP despite decline in development expenditure.
- Domestic borrowing to finance these deficits did not weaken growth immediately but had serious impacts for public finances and macro-economic stability in 1990s.

Period V: The Nineties, 1988 to 1999
(2 governments of Benazir Bhutto and 2 governments of Nawaz Shareef)

- Like 1950s, this period saw heightened political instability.
- Despite far-reaching reforms introduced in 1991, economic indicators once again fell sharply in contrast with the 1980s for several reasons other than political instability.
- Failure to implement continual agreements led to loss of Pakistan's credibility among the international financial community.
- Confidence of local investors eroded when foreign currency deposits were suddenly frozen.
- GDP growth rate decelerated to 4%.
- Agriculture sector recorded higher output but growth of the manufacturing sector was low.
- Investment ratio fell to 13.9% during 1998 and 1999
- Persistence of fiscal (above 7% of GDP) & external deficits (5% of GDP) led to accumulation of large levels of domestic and external debt throughout decade.
- Development expenditures took a major hit and GDP dropped to 3% from earlier 8%
- Social sector expenditure were pressed to cover high debt service & defense expenditures.
- Poverty nearly doubled from 18% to 34%, and the unemployment rate rose as well.
- At least four main factors determined Pakistan's economic performance in the 1990s.
    - Political instability & frequent change in government with reversal of decisions taken by the preceding government created an environment of uncertainty
    - Widespread mis-governance by 2 major political parties ruling the country
    - Lack of political will to make timely and difficult decisions.
    - Unforeseen shocks (e.g. nuclear testing in May 1998) accelerated flight of capital, led to imposition of economic sanctions and disrupted external economic assistance.
- Both parties were committed to deregulation, privatization, and reliance on market forces

Beyond the nineties, 1999 to present
(Pervaiz Musharaf took over through military coup and left after elections 10years later)

- In October 1999, incoming military government was faced with main challenges of heavy external & domestic indebtedness; high fiscal deficit and low revenue generation capacity; rising poverty and unemployment; and a weak balance of payments with stagnant exports.
- Authoritarian military ruler included technocrats in the government.
- Structural policy reforms laid the foundations for accelerated growth from 2002 to 2007.
- Economic growth rate averaged 7%, up from 3.1% in 2001 to 2002.
- Poverty was reduced by between 5 and 10%age points.
- The unemployment rate also fell from 8.4% to 6.5%
- Approximately 11.8 million new jobs were created between 1999 and 2008.
- Re-profiling of the stock of debt brought down the debt-to-GDP ratio from 100% to 55%.
- Foreign exchange reserves increased to cover 6 months' imports from few weeks' imports.
- Investment rate grew to 23% of GDP with estimated $14 billion of foreign capital inflows
- The exchange rate remained fairly stable throughout the period.
- Situation worsened after March 2007 with a judicial crisis.
- Focusing on elections resulted in serious lapses in important economic management
- Assassination of Benazir Bhutto, plunged the country into a state of uncertainty

- Transition from the military to the civilian-elected government was not managed properly.
- Lack of attention to economic issues by new government further added fuel to fire
- A close assessment of reforms enabled many businesses to invest in the right direction and reap the benefits of business friendly environment.
- Businesses keeping an eye on emerging disorder in 2007 effectively mitigated their risks.

Political Instability and Economic Growth

- Pakistan has seen 23 governments in past 60 years, including: 14 elected or appointed prime ministers, five interim governments and 33 years of military rule by 4 leaders.
- Average life span of a politically elected government has been less than 2 years
- Economic policy regime, on other hand, has only changed twice in all of Pakistan's history.
- Liberal private sector-led growth model in 1950s/1960s was rolled back by Bhutto in 1970
- Since rejection of this model in 1977 and revival of liberal model, the general thrust of economic policy has remained unaltered.
- PPP and PML (N) have been the dominant parties that were in charge of steering economic affairs. Both had different ideologies that played a significant role in devising policies to drive growth, stability and social changes.
- PML (N), is mainly composed of industrialists and is more favorable for the industrialists;
- Whenever PML (N) assumes power, they are supported by businessmen and industrialists.
- In turn, policies of PML(N) are more favorable to the business community.
- A rightist government does not believe in direct intervention in personal lives of the public, instead they provide entrepreneurial opportunities to drive economy & social betterment
- PML (N)'s platform is generally conservative, which involves supporting free markets, deregulation, lower taxes and private ownership.
- PML (N) generally opposes labour union management and large-scale workers' unions.
- The party holds that "prosperous agriculture is the backbone of national prosperity
- During its federal government, PML-N successfully privatised the major heavy industries.
- The other largest party, PPP, established itself based on the slogan 'Roti, Kapra, Makan'.
- Governments of PPP have traditionally targeted the poor and lesser privileged segments of the country and community in Sindh and rural Punjab.
- They have also favoured labour unions and the rights of the workforce in large public sector organisations such as PIA, Railways and Pakistan Steel Mills.

Authoritarian vs. Democratic Regimes

- Authoritarian and Democratic regimes are two ends of the spectrum in political ideology.
- Right wing generally wants to minimize regulations on businesses, which would allow a business owner to have more power over their employees.
- Left wing generally wants to put the employee on a more level playing field with the employer or dismantle the relationship entirely.
- A similar pattern appears in social policy, where the left tends to be more open to people breaking from tradition, while the right tends to be more reverent towards tradition.

ERA	Year	GDP Growth (%)	Manufacturing (%)	Inflation (%)	Per Capita Income (US$)
Gen. Ayub Khan	1958	5.47		6	83
	1960	4.89		6.95	83
	1962	7.19	13.2	-0.52	91
	1964	9.38	11.4	4.18	105
	1966	3.08	8.6	7.23	126
	1968	6.49	6.3	0.17	146
	1969	9.79	8.6	3.19	153
Z. A. Bhutto	1971	2.32	6.4	4.73	179
	1973	7.45	8.73	23.07	101
	1975	3.25	0.6	20.9	168
	1977	7.73	1.8	10.13	213
Zia ul Haq	1978	5.53	13.59	6.14	243
	1980	640	14.22	11.94	303
	1982	6.79	13.63	5.9	368
	1984	8.71	14.39	6.09	349
	1986	5.81	14.75	3.51	335
	1988	4.67	14.94	8.84	379
Latest ERA	2006	5.6	9.4		837
	2008	5	6.1	12	991
	2010	2.6	1.4	10.1	987
	2012	3.8	2.1	11	1198
	2014	4.1	5.7	8.6	1251
	2016	4.6	3.7	2.9	1368
	2017	5.2	5.8	4.8	1465
	2018	5.5	5.4	4.7	1482
	2019	1.9	-0.7	6.8	1285
	2020	-0.4	-5.6	10.7	1194

Tutor's Note:
The above table is only for understanding the economic trends in different political eras and is not meant to be memorised

CH # 2 ECONOMY AND THE BUSINESS PERSPECTIVE

- Economic environment refers to the external factors and the broader economic trends that can impact a business.
- It can be classified into microeconomic and macroeconomic environment.
- **Microeconomic** environment relates to consumers behaviour, market environment, competition in the market and demand and supply forces prevalent in the market place.
- **Macroeconomic** relates to broad economic factors that affect the entire economy and all of its participants, including individual business. The focus of this chapter is macroeconomics.

ECONOMIC INDICATORS

Classification of economic indicators

An economic indicator is a type of economic data on a macroeconomic level, that helps in evaluating the overall economy of a country.

Type	**Description**	**Examples**
Leading economic indicators	- To forecast at what stage the economy will be in, at some time in the future. - These indicators, in particular give an indication for whether a peak or trough will be reached in following 3-12 months.	- Stock market returns - Index of business confidence - Manufacturers' new orders - The money supply - New building permits for private housing
Coincident economic indicators	- Events and measures that occur at the same time as a peak or trough occurs. - Used by governments to assess at what stage in the cycle the economy is in.	- Gross Domestic Product (GDP) - Number of people in employment - Industrial production - Personal incomes - Manufacturing and trade sales
Lagging economic indicators	- Used to assess whether an economy has reached a peak or trough 3-12 months after it would have occurred.	- Consumer Price Index (i.e. inflation) - Unemployment - Interest rates - Average income - Balance of Trade

THE ECONOMIC CYCLE

- An economic cycle consists of several years of economic growth following by economic recession.
  - When national income increases from one year to the next, there is economic **growth**.
  - When national income falls from one year to the next, there is economic **recession** (or in extreme cases, economic decline).
- Government economic policy usually tries to achieve continued economic growth, but if recession becomes unavoidable, policy is then aimed at making the recession as short and as minor as possible.

STOCK MARKET RETURNS

- Stock market is considered as one of the leading indicators
- Performance of a stock market is measured through stock market index.
- Stock market index is the index of the market capitalization of a section of stock market.
- **Market capitalization** is market value of a publicly traded company's outstanding shares.
  - It is equal to share price multiplied by the number of shares outstanding.
  - It reflects what investors are willing to pay for its stock.
  - It's a tool used by investors to describe market and to compare return on investments.
  - It measures a company's worth on the open market and its perceived future prospects
- Market capitalization could be based on:
  - Full-cap (includes all of the shares issued by a company)
  - Free-Float (proportion of total shares issued by a company that are readily available for trading at the Stock Exchange, excluding shares held by controlling directors, sponsors, promoters, government and other locked shares)

Stock Exchange Indices

KSE-100 index

- The most recognized index of Pakistan Stock Exchange
- It includes the largest companies on the basis of market capitalization.
- The index represents 85% of all the market capitalization of the exchange.
- It is calculated using Free Float Market Capitalization methodology.
- The KSE100 has a base value of 1000 as of November, 1991.

All Share Index

- It consists of all listed companies on PSX based on Full Cap methodology.

Stock Exchanges Indices and Business Decisions

- Stock market's movements can impact companies in a number of ways.
- Rise and fall of share price values affects a company's market capitalization
- Businesses also consider stock performance in decisions related to issue of shares.
- If a stock is performing well, a company might be encouraged to issue more shares because they will be able to raise more capital at a higher value.
- Market value of a company is also an important factor when considering mergers etc
- Companies may hold shares as cash equivalents and value fall can lead to funding problem.
- Increase in stocks' value may generate interest for new products or businesses

INFLATION

- Inflation is the increase in price levels over time.
- Rate of inflation is measured using one or more price indices or cost indices, such as a Consumer Price Index (CPI) or a Retail Price Index (RPI) or an Index of Wages Costs.
- Businesses are affected by inflation
- They have to pay more for resources (e.g. materials and labour).
- They will try to pass on their extra costs to their customers (by raising the prices of their own goods and services).
- Individuals have to pay higher prices for goods and services, so they need more money to pay for them.
- If they are in work, they might demand higher wages and salaries.
- This 'inflationary spiral' can go on indefinitely
- Rate of inflation is also affected by **inflationary expectations**. (Rate of inflation that businesses and individuals expect in future).

Implications of high inflation for National Economy

- Increases in national income are the result of two factors:
  - Increase in 'real' quantity of goods and services; and
  - Increases due to higher prices and costs.
- It is possible for measured national income to increase (due to inflation) when the real economy is in recession (due to decrease in real quantities)
- Normally when the rate of inflation is high, and inflationary expectations are high, the 'real' economy is likely to stagnate or go into recession.
- A government might think that some inflation is unavoidable
- Rate of inflation and inflationary expectations should be kept under control, to give the 'real economy' an opportunity to grow.

Implications of inflation (Social & Economic)

- In a time of inflation, debts such as bank loans fall in real value over time.
- Lenders and savers lose because the value of their loan or savings falls. (e.g. a person with cash savings might be earning 3% after tax and inflation may be at 5%)
- Another effect is reduction in real value of fixed income or incomes raise less than inflation

A quick glance on inflation rates in Pakistan (as per Pakistan Bureau of Statistics - PBS)

- CPI inflation rushed by 9.70% on a year-on-year basis in June 2021 vs. 8.60% last year.
- Inflation rate remained high throughout the fiscal year 2020-21
- It reached a peak of 11.1% in April 2021 and achieved significant dip of 9.7% in June 2021

INTEREST RATES

- Amount of interest charged by lender on loan or amount paid by the bank on deposits.
- Interest rates are expressed as annual percentages.

Impacts of Increase in interest rates

- It will discourage investment as it would be more difficult for companies to earn good NPV
- It might encourage people to save, resulting in availability of more funds for investment.
- Consumption would fall for a number of reasons:
  - High interest rates encourage people to save.
  - It would result in lower disposable income for borrowers.
  - It make it more expensive to borrow, so less consumption.
- Profitability of banking sector's will increase (as their main business is lending)
- Increase in interest rate would increase the cost of doing business which will make it less competitive in international market, which is full of low cost producers like Bangladesh etc
- Financing cost also increase significantly and impacts expansion or upgradation etc

Decrease in interest rates

- A decrease in interest rates would encourage investment as it would be easier for firms to earn an adequate return on projects. However, it might discourage saving, thus resulting in a reduction in funds available for investment which would put upward pressure on interest rates.
- Consumption would rise for a number of reasons:
  - Low interest rates discourage saving.
  - It would result in higher disposable income for borrowers
  - It make it less expensive to borrow, so more consumption

Quick glance on interest rates in Pakistan during 2020-21 (Source: SBP's quarterly report)

- SBP's Monetary Policy Committee decided to keep rate unchanged at 7 percent during 3rd quarter to provide support in the domestic economic recovery in 3rd wave of Covid.
- A sizable expansion in fixed investment loans and consumer financing, especially auto-financing was witnessed due to low interest rate.

Fiscal policy

- Government policy on revenue (taxation), spending and government borrowing.
- Main objective of fiscal policy is to enhance and sustain economic growth by way of reducing unemployment and poverty in the country.
- To meet Government spending (e.g. government employees, development expenditure, health, education, defence etc), a government must raise the money in tax, and borrow gap.
- Government might also encourage private sector by offering tax incentives or subsidies

UNEMPLOYMENT

- Means that there are not enough jobs for the people who want them.
- In economic recession and falling demand for goods and services, many firms will make some employees redundant due to low profitability.
- Unemployment sometimes is caused by shortage of skilled labour.
  (As technological complexity of industry increases, demand for skilled labour rises).
- Such a shortage of skilled labour can be managed through:
  - Better standards of education
  - More training
  - Outsourcing to other countries (where skilled labor is available)
- <u>High levels of unemployment</u> are unwelcome in an economy because:
  - That is damaging to society and the welfare of the people
  - Economic growth is less than it could be

Unemployment and business decisions

- Less economic growth due to unemployment will directly affect businesses.
- Many households will have less income (resulting in lower sales)
- Demand for some cheaper products and services will increase
- Local companies might have to increase production due to higher demand.
- Businesses looking to recruit people may also be able to offer relatively lower pay.

BALANCE OF PAYMENTS

- It measures the financial transactions made between consumers, businesses and the government in one country with others.
- It is calculated by adding up the value of all the goods that are exported (i.e. sold to other countries) and imported (i.e. bought from other countries).
- It is made up by a combination, in a country, of:
  - the current account
  - the capital account
  - official financing account
- For any country, Surplus/deficit on trade = Net outflow or inflow of capital.
- Balance of payments (BOP) data is an important indicator for investment managers, government policymakers, State bank, businessmen, etc.
- Businesses use BOP to examine market potential of a country, especially in the short term.
  - A country with a large trade deficit is not as likely to import much
  - Government may adopt a policy of trade restrictions, such as quotas or tariffs etc
  - Government may promote industries focused on export
  - Government may also promote local manufacturing to avoid huge amounts on imports

Quick glance on Balance of payment in Pakistan in 2020-21(as per SBP quarterly report)

- Pakistan's external account position continued to improve during Jul-Jun FY2l.
- Cumulative current account remained in surplus, with a modest deficit in the 3rd quarter.
- There was an increase in remittances which improved current account, besides deferred interest payments, reduced air travel and lower oil prices.
- These factors were sufficient to offset a widening in the trade deficit.
- Import payments rose due to a revival in industrial activities and increased demand
- In addition, some agricultural commodities were also imported at higher prices.
- Overall export receipts were only slightly higher than last year.
- Sufficient inflows were available for debt payments without much impacting reserves.
- After a Covid- induced pause, the IMF program also resumed in late March.
- SBP's foreign exchange reserves rose by US$ 1.4 billion to a 3-year high of S$ 13.5 billion, resulting in a 10% Rupee appreciation and reduced forward liabilities of SBP.

GROSS DOMESTIC PRODUCT (GDP)

- GDP is a monetary measure of the market value of all the final goods and services produced within a country in a specific time period.
- It can be expressed as the GDP per capita (i.e. head of population) to compare economies.

  Economic activity (GDP) = C + I + G + (X – M)

  C = Amount of **Consumption** on goods and services
  I = Amount spent on **Investment** in long-term assets
  G = Amount of **Government** spending
  X = Amount of **Exports** of goods and services
  M = Amount of **Imports** of goods and services

- GDP is the total output from all of the sectors of an economy:
  - Primary sector (agriculture, mining etc.)
  - Secondary sector (manufacturing and construction); and
  - Tertiary sector (services)
- GDP per capita is often considered an indicator of a country's standard of living,
- GDP does not include services and products that are produced by nation in other countries.
- GDP for a particular year is measured by two ways:
  - **Nominal GDP** is the value at current prices in a specific time period, this includes the impact of inflation and is normally higher than the GDP.
  - **Real GDP** is an inflation adjusted value of GDP.
- As per SBP's quarterly reports on Pakistan's economy, the recovery in Pakistan's economy gained further pull in 3rd quarter of FY21.
- Growing momentum over 3 quarters of FY21 is reflected in provisional estimates of GDP growth of 3.9 percent for the full year.
- Compared to last year's contraction of 0.5 percent, the recovery this year was mainly achieved through a turnaround in large scale manufacturing (LSM) industry, and the services sector, particularly the expansion in the wholesale and retail trade segment.
- In the agriculture sector, growth in wheat, rice, maize and sugarcane, all expected to achieve record or near record high output this year, offset the decline in cotton production.

Changes in Economic Indicators and Some Common Business Responses

Change	Consumers	Businesses
Higher unemployment	May spend less, as fewer people are earning	May lower prices in order to encouragepeople to buy
Lower unemployment	May increase their spending,as more people are in work	May increase prices as demand increases
Increased interest rates	May spend less, as they are encouraged to save	May reduce products' sizes but leave the price unchanged, increasing the profit margin. (i.e. shrinkflation)
Decreased interest rates	May spend more, as there is less incentive to save	May launch bigger versions of products to charge higher prices
Increased value of Rupee (exchange rate)	May spend more on imported goods, as they are relatively cheap	May target new domestic markets for their products to attract new customers
Decreased value of Rupee (exchange rate)	May spend less on imported goods, as they are relatively more expensive	May target new international markets fortheir products as exports are cheaper

Ch # 3 Impact of social & legal environment on business

SOCIAL FACTORS AND THEIR INFLUENCE ON BUSINESS

- Values and culture of a business should be a direct reflection of society in which it operates.
- Business manager should be well versed with that external social environment
- Business need to respond to changes in society, including demographic changes.
- If they do not, they will continue to offer products and services that are less relevant.
- Examples of some social, cultural and demographic factors are:
  - Outing and dining out habits of a particular area or particular region.
  - Social media addiction.
  - Domestic travelling and international travelling, especially in vacations.
  - People interested and concerned with their looks when attending social gatherings.
  - People concerned about health and weight.
- Some key social factors that have a significant influence on businesses are discussed below

Attitudes and Lifestyle

- Consumer lifestyles and attitudes are continually changing due to education, globalization, urbanization, social media, advancements in technology and advertisements.
- These factors rapidly impact the dressing, house décor and food preferences.
- However, businesses must understand the dynamics of different cultures. Eg.
  - More focus on family values and joint family units in Pakistan than in the Europe
  - A tea manufacturer would do better in Pakistan rather than US (who are coffee lovers)

Social values

- It include common behaviors of a society that expressly or implicitly determine the boundaries of what is permissible, prohibited, acceptable and undesirable.
- For a business, it is important to be aligned with social values of the society
- Therefore, the policies, products, marketing pitch, stakeholder relationship of a business must be in line with the norms of the society. E.g.
  - Insurance companies may offer a higher education and marriage plans to parents in a society where they are the decision makers and financial supporter of their children.

Demography

- It is study of key statistics about the segments of a society, such as, age, gender, race and ethnicity and location.
- It help the businesses define the markets for their products and services.
- It also determines the size and composition of the workforce.

Age groups

- People born after 1980 are over 60% of world population and are much important element
- They have seen tremendous changes in the world as compared to the earlier generation.
- Because of such exposure they challenge conventional working styles & prefer innovation.
- They are used to of smart phone and internet and they acquire instant online information
- Another thing to consider is the varying nature of needs and preferences as per age group

Gender

- Decisions about product development, marketing strategies, hiring policies and selection of business locations are significantly impacted by the gender it plans to attract.
- E.g., marketing of baby products and households should be directed to women exclusively.
- Companies should also have proper evidence-based social analysis of their market about:
  - the influence on domestic decision making
  - gender-wise loyalty pattern that can be very different
  - gender-wise spending patterns

Ethnicity

- It is the segmentation or identification of people based on their cultural distinctiveness.
- This is generally expressed in language, values, religion, ritual, origin and ancestry.
- Companies should recognize the way different ethnic groups behave or react.
- Companies should also be mindful of the ethnic sensitivity. E.g.
  - In Pakistan, an advertisement of hotel room showing a wine bottle is not acceptable
  - Neckless with hanging cross would have good marketability in Christian community.

Wealth distribution

- Businesses have to define their target markets around different income groups. E.g.
  - Luxury watch company would not advertise in classified ad sections of the newspaper.
  - Supermarket targets middle to lower income segments by claiming lower prices
- Production plans of companies are made on basis of affordability of the relevant market.

Education

- Quality & quantity of educated population in a society directly impacts the strategy
- Good supply of educated and skilled work force helps companies to acquire good talent.
- Companies also adapt their advertising and communication according to the literacy level

Law and Order situation

- Law & order situation in either a specific vicinity, city or entire country affects the business.
- Following are some **negative effects** of an unfavorable law and order situation;
  - Loss of staff and customers.
  - Insurance/security costs become expensive.
  - Loss of profits due to stolen goods from businesses.
  - Businesses spend money on installing effective security measures e.g. alarms.
  - Foreign investment is discouraged and tourism is reduced.

LEGAL ENVIRONMENT AFFECTING BUSINESS

The Role of Legislation in Business

- Legal system of a country is very important to businesses.
- Law regulates business practices, defines business policies, rights and obligations involved in business transactions. For example, business laws may:
  - Make a business or a transaction illegal
  - Impose conditions on certain businesses
  - Regulate the rights and duties of people carrying out business to ensure fairness
  - Protect people dealing with business from harm caused by defective services
  - Ensure the treatment of employees is fair and un-discriminatory
  - Protect investors, creditors and consumers
  - Regulate dealings between business and its suppliers
  - Ensure a level playing field for competing business
- Government can change the rules and regulations concerning businesses from time to time.
- Managers should ensure that they are up to date with laws.

Different types of Laws affecting businesses

Companies law

- In Pakistan, the requirements for incorporation, management, operations and winding up of companies are provided in the Companies Act, 2017, issued by SECP.
- Companies Act regulates companies for protecting interests of shareholders, creditors, other stakeholders and general public and inculcate principles of good governance.
- Companies are required to comply with the requirements of the Act
- Companies which do non-compliance will be subject to relevant penalties imposed by law

Partnership law

- Law relating to partnership businesses in Pakistan is Partnership Act, 1932.
- It includes process of registration and dissolution of firms, rights and duties of partners etc.
- Partnership firms have ease of doing business as they don't have to follow those strict requirements as imposed by Companies Act on the companies

Employment law

- To provide protection to employees, against unfair treatment or exploitation by employers.
- Business organisations are directly affected by employment laws.
- Some of the aspects of employment law are given in the table below:

Minimum wage	▪ Minimum hourly / monthly rate of pay that may be paid to any employee
Working conditions	▪ Maximum hours of work per week or month. ▪ Maximum retirement age etc
Unfair dismissal	▪ Rights against unfair dismissal by an employer. ▪ Employer must demonstrate that dismissal was not for a reason that law would consider 'unfair'. ▪ Otherwise, it might be required to re-employ the individual or pay him/her huge compensation.
Redundancy	▪ Law may require transferring an employee to another job before opting for redundancy.
Discrimination	▪ Against various categories of employee (On grounds of physical disability, gender, race, religion and age)
Gender Equality	▪ Countries including Pakistan have laws for anti-harassment to eliminate gender biasness, women protection at workplace and gender equality

Health and safety law

- Provides rules and regulations about minimum health and safety requirements that must be provided in the place of business
- Employers are sometimes required by law to provide a safe workplace (where employees are not exposed to unreasonable physical dangers or unreasonable risks to health).
- There should also be detailed regulations for particular types of industry/business or type of business premises (e.g. transport, food, construction and chemical processing)
- There might also be voluntary health and safety codes that the government encourages but does not enforce as legal requirement
- Specialist health & safety officers might be employed by company.

Data protection law

- It might be considered illegal that organisation should be able to:
  - Gather and hold personal data about individuals without a justifiable reason, and
  - Make use of that data without individual's permission.
- Someone holding and using personal data about individuals should also be under a legal obligation to:
  - Make sure that the personal data is accurate, and
  - Ensure its security (not be accessed by any irrelevant person)

Cyber laws

- It applies to internet and internet related transactions.
- To safeguard individual's information and confidentiality of clients where transactions are made over some network, collecting, storing, retrieving and disseminating of data.

Competition law

- To encourage fair competition in markets and avoid anti-competitive practices

Monopolies

- When a company has a monopoly of a market, it might engage in unfair business practices (e.g. charging higher prices than a competitive market)
- There might be laws to prevent a company from acquiring monopoly control over a market.
- When a company grows to that level Government might take measures to protect public.
- Similarly restriction or additional conditions can be imposed on a proposed merger to avoid / resist monopolies

Anti-collusion regulations

- Collusion occurs when some business entities secretly agree to do something for their mutual benefit that is against public interest.
  (e.g. a secret agreement to raise prices, and avoid competition etc)
- In many countries, collusion is a criminal offence.

Price controls

- Government might impose price controls on certain key products or services (e.g water, electricity or gas).
- Official approval might also be required for any increase in prices.

Sale of goods legislation

Usually specifies there are certain terms in the contract that a consumer may rely on. For example buyer is entitled to assume:

- <u>Title</u>
  That the seller of goods actually owns them (i.e. has title to them).
- <u>Description of goods</u>
  That those goods correspond to the seller's description.
- <u>Quality</u>
  That the goods supplied in the course of a business must be of satisfactory quality for the purpose intended.

Copyrights, Patents and Licenses

- To prevent the intellectual property of individuals
- **Copyrights** safeguard "original creations" such as writings, art, architecture and music from being copied or reproduced. Owner has exclusive right to display and share that work
- A **Patent** is a registered right that gives the owner exclusive right to features and processes of inventions (including its formula)
- A **License** is a permission to carry out certain business activities or practice under specific government regulation or certification body.

Legal Environment and Ease of Doing Business

- Economic activity requires sensible legal system that encourages growth in marketplace.
- These laws include rules that establish and clarify property rights, minimize the cost of resolving disputes and provide contractual partners with core protections against abuse.
- Businesses get strategic analysis to understand the dynamics of the business environment.
- A business manager examines many factors, like overall quality of an economy's business environment, financial system, market size, rule of law, and the quality of the labour force.

World Bank Ease of Doing Business Index (2003)

- This Report ranking is an assessment of business regulations across 190 economies.
- There are many other assessments as well but this annual ranking is often cited as the most authentic indicator of the regulatory environment for business operations.
- Ease of Doing Business Index comprises 10 Indicators on basis of which ranking is issued;
  - Starting a Business
  - Getting credit
  - Construction permit
  - Getting electricity
  - Registering property
  - Protecting minority investors
  - Resolving insolvency
  - Enforcing contracts
  - Trading across borders
  - Paying taxes
- To improve Pakistan's ranking in this Report, many measures have been taken in Companies Act 2017 to provide ease of business as follows:
  - Simpler and softer regime for smaller companies by waiving off certain requirements related to filing annual return, performing annual audit and other relaxations;
  - Introduction of maximum use of technology;
  - Removal of unnecessary requirements for all companies etc.

CH # 4 INFORMATION AND COMMUNICATION TECHNOLOGIES

IMPACT OF TECHNOLOGICAL CHANGE ON WORKING METHODS

Over the years, machines have replaced man for mechanical tasks. Computers have replaced man for many mental and intellectual jobs.

Impact of technological change on products and services

- Technological change has a huge impact on the nature of products and services
- Companies need to maintain technological developments in the design and manufacture of products, and in the provision of services, in order to remain competitive.

Impact of technological change on organisation structure etc

Computerisation, communications technology and other aspects of technological change have led to major developments such as:

1) Downsizing

- Means the reduction in size of a business organisation. Its business activities are conducted by a smaller number of people.
- Technological change makes downsizing possible

2) De-layering

- Means removing one or more levels of management in the organisation structure.
- De-layering is made possible by high-quality communications and that is now quiet possible through technological developments.

3) Restructuring

- Restructuring may be vertical and horizontal both.
- Different organizations merge functions, sections and departments according to the technological advancement and continuously restructure the organizational structure.
- Like real time, online data availability has shifted regional decision making into centralized.

4) Outsourcing & Virtual Company

- An entity does not need to carry out many operations itself.
- Instead, it can outsource (delegate) work to a sub-contractor.
- Outsourcing is made much easier by high-quality telecommunications & computer systems

Reasons for outsourcing

- Entity would focus activities within the entity on core competencies, with aim of gaining more competitive advantage in these core areas.
- Entity would outsource work to entities that have core competencies in these areas of work.
- Outsourced work might require specialist skills that the entity cannot employ internally

Problems with outsourcing

- Loss of control over the outsourced activities.
- Something may go wrong, and action performance does not meet expectations.
- Affect on relationships with the suppliers

Virtual organisation

- Virtual organisation does not have an identifiable physical existence.
- It does not have a head office or operational premises.
- It might not have any employees.
- A virtual organisation is operated by means of:
    - IT systems and communications networks (e.g. telephone and e-mail)
    - Business contacts for outsourcing all operations.
- These organisations use their brand name as major core competence.
- One person, or a small number of individuals, can operate a virtual organisation.

Other modern concepts

Online Social Media

- Social media has changed the business models.
- Personal and business entities now have become the digital identities.

Big Data

- Extremely large data sets are being gathered, analysed computationally to reveal patterns, fashions, trends, associations and preferences, especially relating to human behaviour
- These big data sets are being used to take business decisions.

Artificial Intelligence

- Different business segments are using artificial intelligence, various services are being provided with the help of artificial intelligence (like frequently asked questions)

INFORMATION TECHNOLOGY AND INFORMATION SYSTEMS

Information technology (IT)

- IT developments have resulted in many new products & improvements in existing products
- IT developments have also radically altered methods of communication.
- The Internet has emerged as a major source of external and easily accessible information.
- Commercial transactions can be processed more quickly.
- Changes in IT will continue, and these will have a significant impact on business strategy.
- IT and changes in IT affect every business entity.
- Business entities should be prepared to change as IT changes, and to take advantage of new opportunities provided by IT, rather than try to oppose change.
- IT should be used constructively for setting strategic targets and implementing strategies

Information systems (IS)

- Businesses depend on information technology for everything from running daily operations to making strategic decisions.
- Computers are the tools of this information age, performing extremely complex operations as well as everyday jobs such as word processing and creating spreadsheets.

The main types of information system in organisations include:
- **Transaction processing systems.** Systems for processing routine transactions, such as bookkeeping systems and sales order processing systems.
- **Management information systems.** Systems for providing information, mainly of routine nature, to management for planning and controlling operations.
- **Decision support systems**. Used by managers to help them to make decisions of a more complex or 'unstructured' nature. A DSS will include a range of decision models, such as forecasting models, statistical analysis models and linear programming models.
- **Executive information systems.** Gives an executive access to summary information about a range of issues, and also to 'drill down' into greater detail if this is required.
- **Expert systems.** A system that is able to provide information, advice & recommendations on matters related to a specific area of expertise.
- **Enterprise Resource Planning** Bringing together human resources, operations, and technology are becoming an integral part of business strategy.

<u>Information Systems (IS) strategic support</u>
- Quality of decision making depends on quality of information to management.
- Quality of the service to customers also depends on the quality of transaction processing.
- An entity should ensure that its Information Systems (IS) are suitable and will assist the entity in achieving its long-term strategies.
- Better IS systems can give an entity a competitive advantage over its rivals
- Tasks that would take years on a PC can be completed in just hours on a supercomputer.
  - Supercomputers play a critical role in national security research as well (such as scientific research, simulations of earthquakes and predicting voting patterns)
  - Businesses, too, put supercomputers to work by analyzing big data

Data and Information Systems

- Businesses collect a great deal of data (i.e. raw, unorganized facts that can be moved and stored) in their daily operations.
- Only through well-designed IT systems and computers, this data can be processed into meaningful and useful information
- One such form of business information is the database
  (an electronic filing system that collects and organizes data and information)
- Using software called a database management system (DBMS), you can quickly and easily enter, store, organize, select, and retrieve data in a database.
- Databases are at the core of business information systems.
  - E.g. customer database containing name, address, payment method, products ordered, price, order history, and similar data provides information to many departments.
  - Marketing can track new orders and determine what products are selling best;
  - Sales can identify high-volume customers or contact customers about new offerings
  - Operations use order information to obtain inventory and schedule production;
  - Finance uses sales data to prepare financial statements.

Data warehouse and Data marts

- **Data warehouse** combines many databases across whole company into 1 central database.
- With this, managers can easily access and share data across the enterprise to get a broad overview rather than just small pieces of information.
- Data warehouses include software to extract data from databases, maintain the data in the warehouse, and provide data to users.
- They can analyze data much faster than transaction-processing systems.
- Data warehouses may contain many **data marts**
  (special subsets of a data warehouse that each deal with particular area or department).
- Companies use data warehouses to gather, secure, and analyzing data for many purposes, including customer relationship management, fraud detection and product-line analysis
  - Retailers might wish to identify customer demographics and shopping patterns
  - Banks can more easily spot credit-card fraud, as well as customer usage patterns.

Information and organisation structure

Changes in IS and IT have an effect on organisation structure.
- Databases and intranet systems can make information accessible to any employee.
- It is now easily possible for decisions to be taken 'locally' by employees or managers.
- IT therefore makes it possible for head office to control an organisation centrally.

Changes in IS and IT systems have already affected the organisation of many entities.
- Many organisations have a 'flatter' management hierarchy, with fewer middle managers.
- Decisions are taken either centrally by head office or locally by junior management.
- No need for employees to work together in an office, because they can communicate easily.
- Virtual organisations are working on their own, often from home, linked by IS/IT systems.

IT CONTROL & EFFECTIVENESS

Threats to systems security

- Data deletion or corruption due to human error.
- Technical error in the computer hardware, the software or the communications links
- Some computer systems may be exposed to risks of natural disasters (e.g. earthquakes)
- Systems are also exposed to risk from criminal damage, or simply theft.
- Deliberate corruption (e.g through virus or hacking).
- Loss of key personnel with specialist knowledge about a system.
- Exposure of system data to unauthorised users. (e.g. hackers)

In addition, there are risks within the computer software itself:
- Software might have been written with mistakes in it, so that it fails to process all the data.
- Software might not contain enough in-built controls against risk of input / processing error

General controls and application controls

General controls are controls that are applied to all IT systems and in particular to the development, security and use of computer programs. Examples of general controls are:
- Physical security measures and controls
- Physical protection against risks to the continuity of IT operations
- General controls within software such as passwords, encryption software, and firewalls
- General controls over the introduction and use of new versions of a computer program
- The application of IT Standards.

Application controls are specific controls that are unique to a particular IT system or IT application. They include controls that are written into computer software

General controls in IT

Physical access controls

- Putting locks on doors to computer rooms when there are no authorised staff in the room.
- Putting bars on windows, and shatterproof glass in computer room windows
- Locating hardware in places that are not at risk from flooding
- Physical protection for cables (to provide protection against fire and floods)
- Back-up power generators, in the event of a loss of power supply
- Installing smoke detectors, fire alarms and fire doors
- Regular fire drills, so that staff know the measures to protect data and files in emergency
- Obtaining insurance cover against losses in the event of a fire or flooding.
- Arrangements with different providers of hot and cold sites (in case of emergency shifting)

Passwords

- It is defined as 'a sequence of characters that must be presented to a computer system before it will allow access to the systems or parts of a system'
- Typically, a computer user is given a prompt on the computer screen to enter his password.
- Passwords can also be placed on individual computer files, systems and programs.
- To gain access to a system, it may be necessary to input both a user name and a password.
- However, password systems are not always as secure, mainly due to human error.

Problems of password systems include the following:
- Users might give their passwords to other individuals who are not authorised to.
- Users are often predictable in their choice of passwords, so that a hacker might be able to guess, by trial and error, a password to gain entry to a system or program or file.
- Passwords are often written down so that the user will not forget it.

A security culture should be developed within the organisation, so that the user's staff are aware of the security risks and take suitable precautions.

Encryption

- Encryption involves coding of data into a form that is not understandable to casual reader.
- Data can be encrypted (converted into a coded language) using an encryption key.
- A hacker would not be able to read the data, and would not be able to convert it back into a readable form without a special decryption key.
- Encryption is commonly used to protect data that is being communicated across a network.
- The on-line shopping system should provide for encryption of sender's details (using 'public key') and the decryption of message at seller's end (using a 'private key')

Preventing or detecting hackers

- Physical security measures to prevent unauthorised access
- Use of passwords
- Encryption of data
- Audit trails, so that transactions can be traced through system when hacking is suspected
- Network logs of attempts to gain access to the system
- Firewalls.

Firewalls

- Firewalls are either software or a hardware device between user's computer and modem.
- Purpose is to detect and prevent any attempt to gain unauthorised entry through Internet into a user's computer or Intranet system.
- A firewall:
    - Will block suspicious messages from Internet, and prevent them from entering system
    - May provide an on-screen report to the user whenever it has blocked a message
- Firewalls can be purchased from suppliers.
- Some firewall software can be downloaded free of charge from the Internet.

Computer viruses

- Viruses are computer software that is designed to deliberately corrupt computer systems.
- Viruses are written with malicious intent, but they may be transmitted accidentally.
- Viruses can be introduced into a system on a file containing the virus.
- A virus may be contained in a file attachment to an e-mail or On a storage device like DVD.
- Viruses vary in their virulence (amount of damage they may cause to software or data)

Term	Description
Trojan horses	A virus that **disguises itself** often hidden within other software or files. When system is carrying out one program, it secretly carries on another.
Worms	This is corrupt data that **replicates itself** within the system, moving from one file or program to another.
Trap doors	An entry point to a system that bypasses normal controls
Logic bombs	A virus that is designed to start 'working' (corrupting files or processing) when a certain event occurs.
Time bombs	A virus that is designed to start 'working' (corrupting files or processing) on a certain date/time.
Denial of service	Rendering system unusable by legitimate users (e.g. by overloading website with millions of computer-generated queries)

<u>Measures that might be taken to guard against computer viruses.</u>

- Computer user should install anti-virus software and keep up to date to:
  - Detect known viruses in a file; and
  - Isolate the virus so that it is not able to corrupt software or data in the computer.
- Computer user might restrict the use of floppy disks and re-writable CDs
- Firewall software and hardware should be used to prevent unauthorised access
- Staff should be encouraged to delete suspicious e-mails without opening any attachments.
- There should be procedures, communicated to staff, for reporting suspicions of any virus.

IT Standards

- IT Standards are a form of general control within IT that help to reduce the risk of IT system weaknesses and processing errors, for entities that apply the Standards.
- A range of IT Standards have been issued (e.g. ISO has issued IT security system standards).
- There are also IT Standards for the development and testing of new IT systems.

Application controls in IT

- Application controls are controls that are designed for a specific IT system.
- Common example of application controls is data validation. These are checks on specific items that are input to a computer system, to test the logical 'correctness' of the data. E.g.:
  - If a transaction is input to system without value, an error report should be produced.
  - Entered value should be within a range of codes, otherwise error would be generated
  - Key code numbers can be designed to include a 'check digit'.

Monitoring of controls

It is important within an internal control system that management should review and monitor the operation of the controls, on a systematic basis

IT controls audit

- Large organisations might employ an internal audit team.
- Organisation could also employ IT auditors who specialise in a particular IT system
- Alternatively, IT control audit might be outsourced to a firm of independent auditors
- The steps involved in IT Control audits typically include the following:
  - Auditor must understand the risks faced by the systems.
  - Auditor would then consider the design of the controls that have been put in place.
  - Auditor will then test the key controls to ensure they have been operating effectively.
- They might perform IT controls auditing on cyclical basis addressing different parts
- Alternatively they might audit all areas of the system at every audit.
- Another approach would be to adopt a 'risk-based' approach

<u>Exception reporting</u>
A periodic (e.g. daily / weekly / monthly) exception reporting should
- Describe control failures that occurred
- Describe the impact of the control failure
- Suggest the new control(s) that should be adopted

*The **effectiveness of IT control monitoring** is driven by the action taken by management to address control failures when they occur.*

COBIT (Control Objectives for Information and Related Technologies)

Purpose of COBIT is to provide management and process owners with an IT governance model that helps in understanding and managing the risks associated with IT. It is a control model to meet the needs of IT governance and ensure integrity of information and information system.
- An IT governance tool that has been of tremendous benefits to IT professionals
- Linking IT and control practices, COBIT consolidates and harmonises standards from prominent global sources into a critical resource for management control professionals.
- COBIT represents an authoritative, up-to-date control framework, a set of generally accepted control objectives and a complementary product that enables easy application
- COBIT applies to enterprise-wide information systems, including personal computers, mini-computers, mainframes and distributed processing environments.
- COBIT is used by the persons who:
  - have the primary responsibilities for business processes and technology;
  - depend on technology for relevant and reliable information
  - are providing quality, reliability and control of information technology.

Ch # 5 Technological disruption & business environment

TECHNOLOGICAL DISRUPTION AND BUSINESS ENVIRONMENT

Technology and disruption

- **Disruptive technology** is an innovation that significantly
  - Alters the way consumers, industries, or businesses operate.
  - Sweeps away the systems or habits it replaces (being latest)
- In their own times, automobile, electricity service, and TV were disruptive technologies.
- Risk-taking companies may recognize the potential of disruptive technology in their own operations and target new markets using their business processes.
- These are the "innovators" of the technology adoption lifecycle.
- Other companies may follow them only after seeing how it performs for others.
- Companies that fail to account for effects of disruption may find themselves losing market.

<u>Blockchain as an Example of Disruptive Technology</u>
- Blockchain (technology behind Bitcoin) is a decentralized distributed ledger
- It records transactions between two parties and moves transactions from a centralized server-based system to a transparent cryptographic network.
- It uses peer-to-peer agreement to record and verify transactions (no manual verification).
- It has many implications for financial institutions such as banks and stock brokerages. (e.g. executing peer-to-peer transaction will save time and cost, removing intermediary)

Disruptive Technologies of the digital age

- Human mind normally realize linear and not exponential possibilities (unlike technology).
- Disruptions are always first resisted by humans, but then they adopt it when see that useful
- These days IT is moving faster than ever, driven by developments in 3 basic areas;
  - Processing power,
  - Communication speed
  - Storage capacity.
- IT is combining with improvements in specific industry technology in almost every sector
- A big gap opens up between current organisations and capability which technology can do.

The Internet

- More people have more access to technology (devices etc) than ever before.
- Today's, nearly every manager has a desktop or laptop, fax, voice mail, mobile phone etc
- One of the most visible technological innovations over past decade has been the Internet.
- New ways of going online are contributing to the growing use of the Internet.
- Cell phones have access of internet connectivity and Wifi with faster data transfer speeds
- Now internet has changed the direction of businesses to create new dimensions

E-Business

- Electronic business exchanges between businesses have emerged.
- E-business has grown dramatically and become a way of life for all type of businesses
- As technology became more affordable and easier, small and medium businesses have invested in e-business and technology systems
- It gave the businesses a competitive edge over rivals by enabling them to add new services
- All businesses are more open to modify their business models to include technology infrastructure and create online channels for alternative sales.

M-Commerce

- Initially cell phones were clumsy analog devices but today's digital "smartphones" provide a range of applications, including e-mail and Internet access as well
- Initially, cell phones were used mainly as a communications tool.
- But now users all over the world have taken mobile phone as way of conducting commerce.
- **M-commerce** (commerce conducted via mobile), provides consumers with an electronic wallet when using their mobile phones.
- People can trade stocks or make purchases of everything using that E-Wallet

Social networking

- A system using technology to connect, explore interests and share activities around world
- Many businesses use social media tools to reach out to their customers.
- It has now become a major marketing channel (replacing Paper and TV advertising).
- Major online advertising tools include:
  - Search Engine Optimization (SEO)
  - Facebook Ads
  - Google Ads and clicks
  - Website banners

Blogs and Vlogs.

- A **blog** is a web-based journal or log maintained by an individual with regular entries of commentary, descriptions, or accounts of events or other graphics or video etc.
- A problem is differentiation between what is honest opinion or what is paid advertisement
- Many businesses use the medium of bloggers to push their products in the market
- This is done through free products, invitations to brand launch events etc.
- **Vlogs (**or video web logs) is a new type of blogs appeared in first decade of 21st century
- All that needed is access to a digital camera and high-speed Internet access.

EFFECTS OF DISRUPTION IN MAJOR INDUSTRIES

Technology and internet-based companies are accelerating pace of disruption at alarming rate

- Google has completely disrupted the Yellow Pages business which was once valued at $60 billion and is now below one billion dollars.
- Airbnb, worth over $25 billion has disrupted the hotel industry by accumulating the largest inventory of rooms without owning a single property.
- Uber, worth over $50 billion, has completely disrupted the local travel and taxi business without owning a single car.

In this chapter we will cover examples of only few industries, but healthcare, transport, courier services, publishing, restaurants, delivery and numerous others business segments are on their way to being disrupted. What is required is an understanding by governments and companies who need to play their role as enablers and promoters of disruption in the interest of consumer.

Textile Industry

- The technology have made the machines to be ease, speedy and process technology to new modes of clothing production based on the systems cost and productivity.
- The skills, management and training need of the organizations are also affected.
- The technology such as CAD, CAM, manufacturing management and IT systems facilitate many changes in the fashion and textile industry.
- Labor productivity have been increased and manufacturing costs have been reduced
- In sewing machine industry, technology provides a flexible method of adapting to changing styles, fabrics and sizes.
- Search for improved competitiveness increases the raise of new methods in designing, quick response, quality and service
- Design, cutting and marker making can be handled with use of most modern equipment.
- For woolen goods, cutting can be integrated directly into the fabric quality control process.
- The trading house system connects number of stages of textile manufacturing with retail.
- Companies use electronic data interchange as core technology for managing supply chains.

Example of Sportswear and the Dri-FIT revolution of Nike (over the past decades)

- The first ever Olympic Games were held back in 1896, and there arose need for clothing specifically designed to improve range of motion and performance.
- Fabrics of that time were quite heavy, and they did very little to keep athletes comfortable
- Back in the 1970s, the fitness revolution really began to take hold.
- Cotton and linen were still the fabrics of choice then, but technology was quite limited.
- When 1990s rolled around, performance shirts hit the market, too. Tops were cropped significantly and made with breathable fabric blends designed to keep moisture away.
- Nike first released its Dri-FIT line of products to the general public in the early 2000s.
- The fabric is a microfiber polyester, which move moisture from skin to outer layer of fabric (keeping athletes dry and comfortable in even the hottest temperatures)
- Dri-FIT was first introduced in shirts, Nike now uses the technology in gloves, hats, pants, socks, and even sleeves.

- These days, athletic wear designed to keep people comfortable isn't limited to just athletes.
- With dress shirts and slacks that breathe, stretch, and wick moisture, it's now possible to look sharp and feel great at the same time, both in and out of the office.
- Performance shirts in sports have been around for decades, but the technologies used to create fabrics and fabric blends continue to evolve.

Solar and renewable energy

- In next 10-15 years, electricity grid will be almost extinct or at least much less relevant
- Global focus is now also on improving battery life and user-friendliness
- Already many households that have a solar system installed at rooftops
    - Reliance on the grid is probably less than 50% of the energy demand
    - Next 50% will come much faster due to the expected technology improvements.
- This will require a major change in business models of large power producers and utilities.

The Internet of Things (IoT) and operations of Power generation

- It has the potential to significantly transform the power sector by optimising operations, managing asset performance, and engaging customers to lower energy cost.
- Smart meters and smart thermostats are already serving power sector
- The rapid growth in IoT is forcing traditional power utilities and industry participants to adapt, or be outpaced by strong new entrants possessing technological advancements.
- Smart meters and IoT connected power appliances has enabled consumers to track and monitor their energy consumption and save money in energy bills.
- Similar technology is expected to come in power generation and transmission segments.
- Even a maintenance engineer can look for the problems remotely using applications
- Increasing need for monitoring of renewable energy assets in remote areas for scheduled maintenance and reduced downtime is also likely to make IoT popular in utility industry.
- Once connected with IoT, system can perform effective load balancing, load flow analysis, identify faulty transformers, and alert the nearby maintenance team for quick response.
- Also, because of online or cloud nature of technology, cybersecurity issues can be increased

Education

- Technology has enabled students of some of the poorest and most remote communities to access the world's best libraries, instructors, and courses available through the Internet.
- Trends in online education should be an eye opener for thousands of physical institutions
- With higher broadband speeds, we are already witnessing tremendous growth in digital classrooms, online learning material, Ebooks and video content.
- Online education accelerated by the pandemic of COVID-19. All the institutions shutting down then have been forced to look at digital channels of providing education at lower cost
- Online education has also challenged the entire education system as it exists today.
- This should enable schools to rethink and prepare themselves for sort of learning required and how will they change their business model and secure employment of teachers & staff.

Retail and ecommerce

- Retail space is losing ground to online shopping in a big way with large malls and stores being consistently forced to reduce the number of locations.
- In Pakistan, trend of online shopping is visible with trips to malls (only as entertainment)
- Many stores are now also protesting successfully against high rents.
- This trend will hurt the retail business model of malls and retail stores making it difficult

Electronic media

- The growth of paid streaming services such as Netflix has taken away the consumer from the advertising-based business model (normal cable tv channels) to a greater extent.
- Low-quality content will be pushed away by consumers once they are able control what they wish to watch without seeing bombardment of irrelevant advertisements.
- This can potentially eliminate cable TV altogether.
- In addition to the cable channel business, it will disrupt the advertising industry as well

Banking

- Financial technology (Fintech) and virtual banking are the future with physical banks playing a much-reduced role in our daily lives.
- Fintech facilitates in money transfers, investment management, finance, and banking.
- Using Fintech, one can send and receive money via mobiles.
- Jazzcash and Easypaisa are some of the popular examples of fintech in Pakistan.
- In last 5 years, Pakistan has witnessed a drastic increase in e-payments due to coronavirus.

Automobile and transport Sector

- Some already huge disruptions are electric vehicles, ride addressing and self-driving cars.
- Businesses now would have to adapt to more simplified electric cars, as well as having to programme systems to drive the car and designing apps to guide a ride.
- Technology of Tesla is so innovative that its keeps changing through software updates.
- Companies need to become technology companies alongwith their existing business setups to compete with new disruptive entrants like Tesla, Uber and Careem.
- Tesla has also disrupted traditional process of new car sales by offering sales by website.
- Anyone can go to Tesla website, configure their car (including paint, seat materials and configuration, roof type, interiors, tires, mileage) and then place the order.
- Another advancement is with online portals, people can sift through thousands of cars listed for sale across Pakistan, look at pictures and then shortlisting some for next process
- Sellers can now also list their cars on portals eliminating the middleman

Note: Ch # 6 only contain 4 questions and solutions on Ch 1 to 5, therefore is not included in these notes

CH # 7 COMPETITIVE FORCES

COMPETITION AND MARKETS

Customers and markets

- A market is a place where buying and selling takes place.
- A market can be defined by the:
  - Products or services that are sold (e.g. clothes market, banking market, air travel)
  - Customers or potential customers (e.g. consumer market, 'youth market')
  - Geographical area (e.g. North American market or European market, Global vs Local)

Industries and sectors

- An industry consists of suppliers who produce similar goods and services.
  (e.g. aerospace industry, automobile manufacturing industry, a construction industry etc)
- Within an industry, there may be different segments.
- An industry segment is a separately-identifiable part of a larger industry.
  (e.g. insurance industry has several sectors, including general insurance and life assurance)
- Management need to recognise which industries and segments they operate in

Generic types of industry (by Porter)

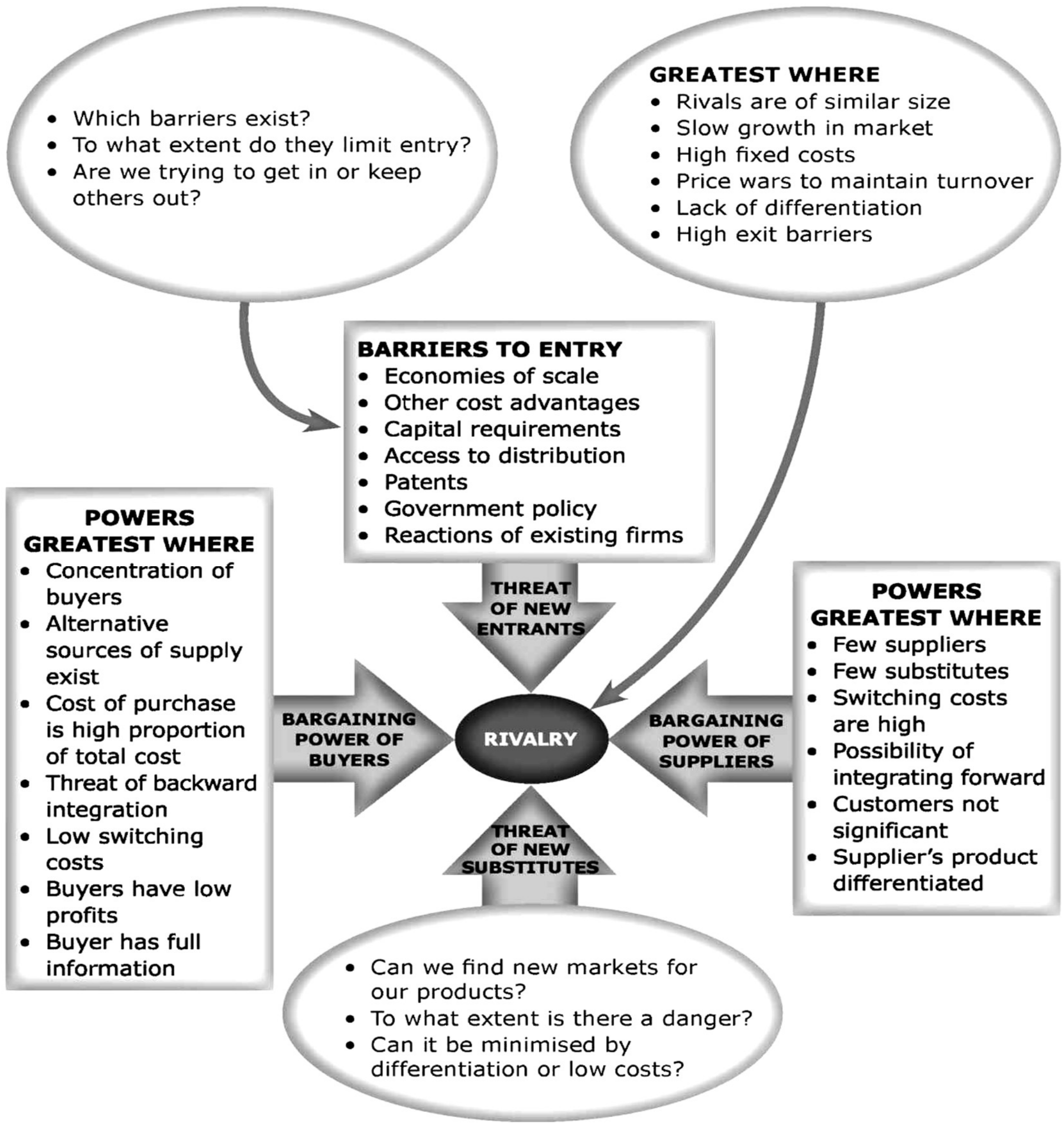
Fragmented industries	- Businesses are small and each sells to a small portion of the total market - Examples are dry cleaning services, hairdressing services, and shoe repairs
Emerging industries	- That have only just started to develop, and likely to become much bigger - Examples are space travel industry and telecommunication industry in Africa
Mature industries	- Where products have reached the mature phase of their life cycle. - Examples are automobile manufacture and soft drinks manufacture.
Declining industries	- Total sales are falling and number of competitors in market is also falling. - An example in landline telephone services
Global industries	- Operate on a global scale - Examples are microprocessor industry and the professional football industry

Convergence

- Sometimes, 2 or more industries or segments converge, and become part of same industry
- This can have a major impact on business strategy.
- Convergence can be either:
  - <u>Demand-led convergence</u>; where the pressure for convergence comes from customers. Customers begin to think of two or more products as interchangeable.
    (e.g. consumers reading newspaper online free of cost)
  - <u>Supply-led convergence</u>; where suppliers see a link between different industries and decide to bridge the gap between industries.
    (e.g. Convergence of entertainment, voice and data communication industries)

FIVE FORCES MODEL BY PORTER

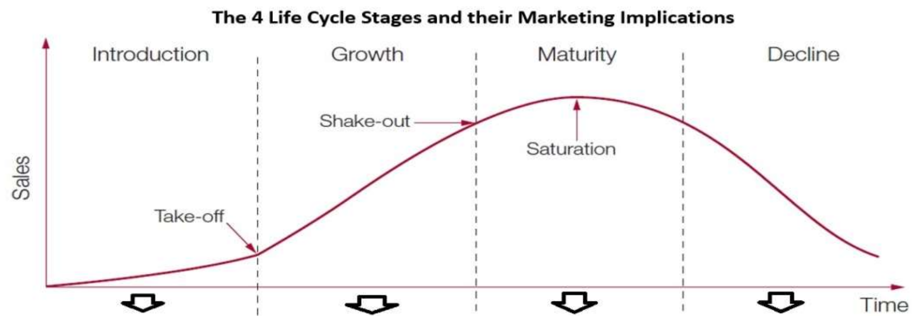
- Five Forces model provides a framework for analysing strength of competition in a market.
- It can also be used to explain why some industries are more profitable than others
- Porter argued that two factors affect the profitability of a company:
  - Industry structure and competition in the industry; and
  - Sustainable competitive advantage



LIFE CYCLE MODEL

The 'classical' product life cycle

- A 'life cycle' is the period from birth or creation of an item to the end of its life.
- Products, companies and industries all have life cycles.
- Classical life cycle for a product/industry goes through **4 stages or phases**:



Features

Sales	Low	Rapidly rising	Peak sales	Declining sales
Per unit Cost	High	Average	Low	Low
Profit	Negative	Rising	High profit	Declining profit
Competitors	Few	Growing	Stable	Declining number

Strategies

Objectives	Create product awareness & trial	Maximize market share	Maximize profit and defend the share	Reduce expenditure and milk the brand
Cost Involved (Implications)	Operating costs, Marketing and advertising	Costs of increasing capacity, increased cost of working capital	Costs to maintain manufacturing capacity, Marketing and enhancement	Close attention to cost of withdrawal
Product	Offer Basic product	Product extensions	Diversify brand and model	Phase out weak items or Reposition
Promotion	Heavy sales promotion	Reduce (take advantage of heavy demand)	Increase to encourage brand switching	Reduce to minimal level
Targeting	Early adopters (build awareness)	Mass market (build awareness)	Mention brand differences & benefits	Reduce (Try to retain loyals)

Examples	- Smart Glasses - E-conferencing - iris-based identity cards	- Tabs & Smart Phones - Email - Smart cards	- Laptops - Faxes - Credit cards	- Personal Computers - Handwritten letters - Cheque books

Benefits of Life cycle costing

- Potential profitability of products can be assessed before its major development
- Non-profit-making products can be abandoned at early stage before costs are committed.
- Techniques can be used to reduce costs over the life of the product.
- Pricing strategy can be determined before the product enters production.
- Attention can be focused to get the product to market as quickly as possible.
  (The longer company can operate without competitors the more revenue can be earned)
- By monitoring actual performance against plans, lessons can be learnt for future products.
- Also useful for assessing strategic position and the nature of competition in a market.

Tutor Note

Criticism on PLC approach:
- Relevant only for products where consumer demand is high
- Underlying stage of PLC is determined by marketing actions.
- Stages cannot be easily defined.
- Strategic decisions can change PLC

Timing of market entry and market exit (Relevance to strategic management)

- Entrepreneurial companies might look for entering a new market during introduction
- More cautious companies might delay their entry into the market until the growth phase
- Companies are unlikely to enter a market during maturity phase
  (unless they see growth opportunities in a particular part of the market)
- A company might need to make strategic decision about leaving a market, when product is in its decline phase. It should be possible to make profits in a declining market, but better growth opportunities might exist in other markets

Cycle of competition

- It is another concept for understanding the behaviour of competitors in a market.
- When a company achieves some success in market, competitors might try to do something even better in order to gain a competitive advantage.
- A new initiative by one company will result in a counter-measure from another company.
- A typical cycle of competition affects prices and quality.
  - A rival company might start to sell its product at a lower price to take its share
  - Another rival company might improve the quality at same same price as yours
  - First company might respond to them by improving its quality and reducing price.
- In maturity or decline phase
  - It becomes more difficult to lower prices without reducing quality.
  - Competitors might try to gain a bigger share by selling at a lower price with low quality
  - It lead to a ‘spiral’ of falling prices and falling quality and the life cycles comes to an end
- Concept of the cycle of competition is useful for strategic analysis, because it can help to explain strategies of companies in a market, and to assess future initiatives of competitors.

STRATEGIC GROUPS AND MARKET SEGMENTATION

Strategic groups

- It is a number of entities that operate in the same industry and that have similar strategies
- All entities in same strategic group can then be treated as if they are a single competitor.
- Instead of analysing each competitor individually, they can be analysed in groups
- When there are only a few competitors in the same industry, the concept of strategic groups has no practical value

Strategic space

- When all companies in an industry are put into strategic groups, and these groupings are analysed, a strategic space might become apparent.
- It is a gap in the market that is not currently filled by any strategic group.
- Existence of strategic space might provide an opportunity for a company to fill the space.

Product differentiation

- In most markets, products are differentiated in various ways.
- They are similar, but there are also noticeable differences like product design, pricing or branding etc
- Products might also be differentiated by the way in which they are delivered to customers. (e.g. internet service, home-delivery meal etc).
- Should make a product different from rival products in a way that customers can recognise.
- This strategy is usually associated with charging a premium price for the product - often to reflect higher production costs and extra value-added features provided for consumer
- Examples are Mercedes cars, Marriot hotels, Nesvita Milk (perceived for strong bones).

Market segmentation

- A market segment is a section of the total market in which the potential customers have certain unique and identifiable characteristics and needs.
- Market segmentation is the process of dividing the market into separate segments, for the purpose of developing differing products for each segment.
- A business entity might try to sell its products to all customers in the market.
- However, a business might instead choose to target its products to a particular segment

There are various ways of segmenting the market such as:
- Geographical area
- Quality and performance
- Function (e.g. running shoes, football boots, hiking boots, riding boots, snow boots etc)
- Type of customer: for example, consumers and commercial customers
- Social status or social group
- Age (e.g. adults, teenagers and younger children)
- Life style.

Tutor Note

Benefits of Segmentation

Better matching of customer needs

- Customer needs differ.
- Creating offers for each segment makes sense & provides customers with better solution

Enhanced profits for business

- Customers have different disposable income.
- They are, therefore, different in how sensitive they are to price.
- By segmenting, businesses can raise average prices and subsequently enhance profits

Better opportunities for growth

- Market segmentation can build sales.

Retain more customers

- Customer circumstances change, for example they grow older, form families, change jobs or get promoted, change their buying patterns.
- By marketing products that appeal to customers at different stages of life, a business can retain customers who might otherwise switch to competing products and brands

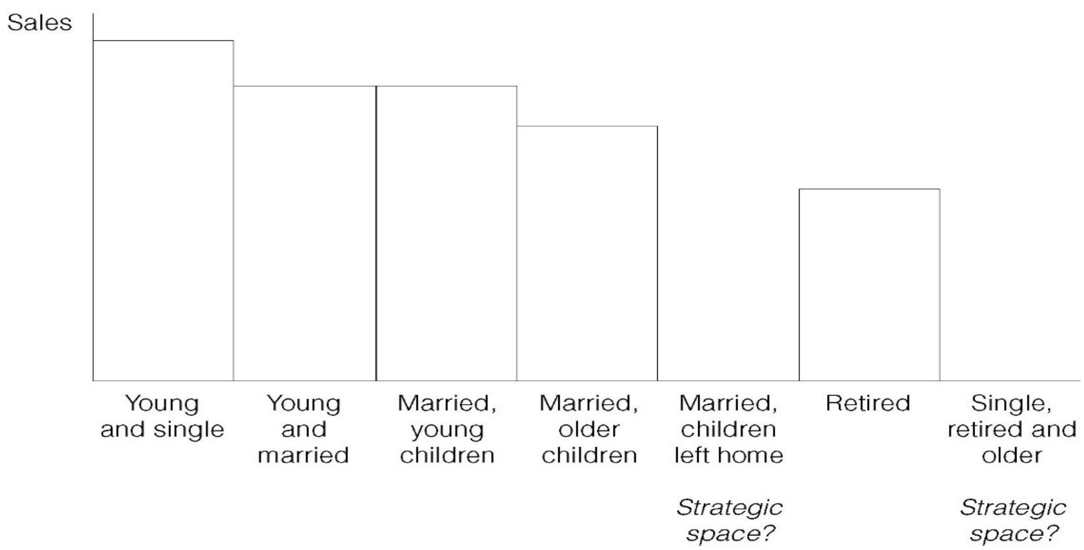
Target marketing communications

- Businesses need to deliver their marketing message to a relevant customer audience.
- If the target market is too broad, there is a strong risk that the key customers are missed and the cost of communicating to customers becomes too high / unprofitable.
- By segmenting markets, target customer can be reached more often and at lower cost

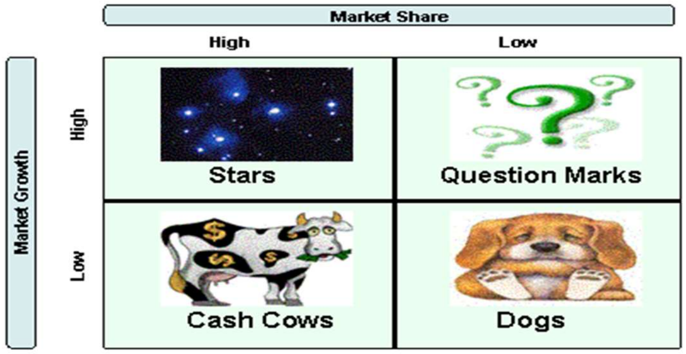
Gain share of the market segment

- Through careful segmentation, businesses can often achieve competitive production and marketing costs and become the preferred choice of customers and distributors.
- Segmentation offers the opportunity for smaller firms to compete with bigger ones.

Market segmentation and strategic space



BOSTON CONSULTING GROUP MATRIX (BCG MATRIX)



Stars

- High growth businesses or products which are relatively strong as regards competition.
- Often they need heavy investment to sustain their growth
- Eventually their growth will slow and will become cash cows(if maintain its market share)

Cash Cows

- Cash cows are low-growth businesses or products with a relatively high market share.
- These are mature, successful businesses with relatively little need for investment.
- They need to be managed for continued profit

Question marks

- Businesses or products with low market share but operate in higher growth markets.
- They have potential, but may require significant investment to grow market share
- Management have to think hard about "question marks"
  (which ones should they invest in and which ones should they allow to fail or reduce)

Dogs

- Businesses or products that have low relative share in unattractive, low-growth markets.
- May generate enough cash to break-even, but they are rarely worth investing in.
- A strategic decision for entity may be to choose between immediate withdrawal from the market or enjoying the cash flows for a few more years before eventually withdrawing.
- It would be an unwise decision to invest more capital in ‘dogs’, in hope of increasing share

Using the BCG matrix

▪ Build Share	Company can invest to increase market share (e.g. turning a "question mark" into a star)
▪ Hold:	Company invests just enough to keep the SBU in its present position
▪ Harvest:	Company reduces the investment in order to maximize short-term cash flows & profits from SBU (May be turning Stars into Cash Cows)
▪ Divest:	Company can divest the SBU by phasing it out or selling it (e.g. investing in the more promising "question marks").

Weaknesses in BCG model analysis

- A product can have a strong competitive position in market, even with a low market share.
- Competitive strength can be provided by factors such as product quality, brand name or brand reputation, or even low costs.
- A company might benefit from investing in market where sales growth is low.
- It might be difficult to define the market.
  - There might be problems with defining the geographical area of the market.
  - It might also be difficult to identify which products are competing with each other.
- BCG matrix might be better for analysing performance of strategic business units (SBUs) and market segments but It is not so useful for analysing entire markets
- It might be difficult to define what is meant by 'high rate' and 'low rate' of growth
- It might be difficult to define what is meant by 'high' market share and 'low' market share.
- Care is therefore needed interpreting a BCG analysis.

OPPORTUNITIES AND THREATS

See Ch # 8 (Last unit) for complete SWOT Analysis

CH # 8 INTERNAL ANALYSIS

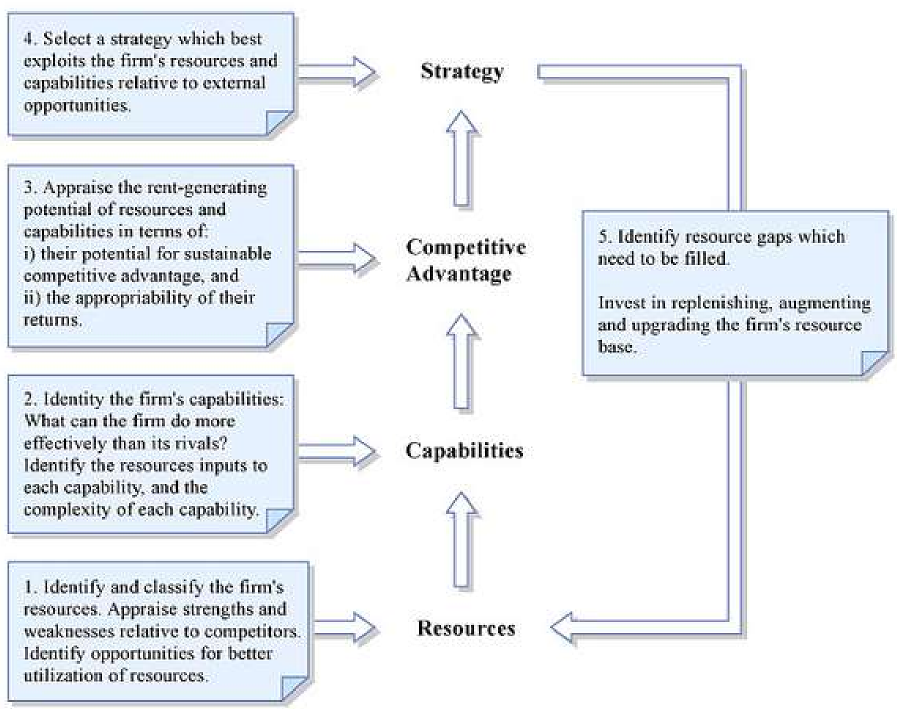
STRATEGIC CAPABILITY

'Strategic capability reflects the ability of an entity to use and exploit resources available to it, through competences developed in activities and processes it performs, the ways in which these activities are linked internally & externally, and overall balance of core competences across entity

- It can also be described as the ability of an organisation to use its core competences to create competitive advantage.
- Competitive advantage comes from successful management of resources, competences and capabilities.

Achieving strategic capability

Tutor Note



A RESOURCE-BASED APPROACH TO STRATEGY ANALYSIS: A PRACTICAL FRAMEWORK

CUSTOMER NEEDS

- Companies and other business entities compete with each other in a market
- Markets can be defined by their customers and potential customers.
- Most profitable entities sell their goods or services most successfully.
- Should Provide goods or services to customers that meets customer needs successfully

What are customer needs?

- Better-quality product
- Better design features
- Availability
- Convenience of purchase
- Right Price

Customers may be grouped into 3 broad types:
- Consumers: these buy products and services for their personal benefit or use
- Industrial and commercial customers: customers might include other business entities
- Government organisations and agencies.

Tutor Note

Difference between a Customer & Consumer

- A customer — Purchases and pays for a product or service
- A consumer — Ultimate user of the product or service; Consumer may not have paid for the product or service

Example: A food manufacturing business makes own label, ready meals for the major supermarkets; the customer is the supermarket to whom it supplies meals and the consumer is the individual who eats the meal

Who should the business target?
- In reality – it needs to understand needs and wants of both the customer and consumer.
- For supermarkets; Their requirements for ready meals (e.g. packaging, delivery etc).
- For consumers; It also needs to understand the needs and wants of the consumer. How are tastes changing? Are consumers happy with the standard / taste of the product?

The 4Ps of the marketing mix

- **Product** refers to the design features of the product, and the product quality. Features such as short lead time for delivery and reliable delivery could also be important.
- **Price** is the selling price for the product
- **Place** refers to the way in which the customer obtains the product or service, or the 'channel of distribution'.
- **Promotion** refers to the way in which product is advertised and promoted.

CRITICAL SUCCESS FACTORS FOR PRODUCTS AND SERVICES

Definition of a critical success factor

- **Critical success factors** (CSFs) are factors that are critical to the success of an organisation and the achievement of its overall objectives.
- They have been defined as: 'those components of strategy in which the organisation must excel to out-perform competition' (Johnson and Scholes).
- CSFs of a product or service must be related to customer needs.
- They are features of a product or service that will have main influence on buying decisions

CSFs and key performance indicators (KPIs) – Link with Strategy

- CSFs should be identified during the process of assessing strategic position. (Need to understand the main reasons why particular products or services are successful)
- CSFs are important in the process of making strategic choices. (Should select strategies that will enable it to achieve a competitive advantage)
- CSFs are also important for strategy implementation. (Performance targets should be set for each CSF)
- Measured targets for CSFs are called **key performance indicators (KPIs)**.

6-step approach to using CSFs (Johnson and Scholes)

Step 1
Identify the *<u>success factors that are critical for profitability</u>*. These might include 'low selling price', and also aspects of service and quality such as 'prompt delivery after receipt of orders'.

Step 2
Identify what is necessary ('*critical competencies*') in order to achieve superior performance in the CSFs. This means identifying what the entity must do to achieve success. For example:

- If CSF is 'low sales price', a critical competence might be 'strict control over costs'.
- If a CSF is 'low level of sales returns', a critical competence might be 'zero defects'

Step 3
The entity should *develop the level of critical competence* so that it acquires the ability to gain a competitive advantage in the CSF.

Step 4
Identify *appropriate KPIs* for each critical competence.

Step 5
Give emphasis to developing critical competencies for each aspect of performance, so that competitors will find it difficult to achieve a matching level of competence.

Step 6
Monitor firm's achievement of its target KPIs, and also monitor performance of competitors.

Competitor benchmarking

- Benchmarking is a process of comparing your own performance against the performance of someone else, preferably the performance of 'the best'.
- To identify differences between your performance and selected benchmark.
- Where these differences are significant, methods of closing the gap and raising performance can be considered.

Methods of benchmarking

Internal benchmarking	- Compare the performance of units within entity with best-performing unit. - E.g. an organisation with 30 branch offices might compare the performance of 29 of the branches with the best-performing branch
Operational benchmarking	- Compare performance of a particular operation with the performance of a similar operation in a different business entity in a different industry. - E.g., a publishing company might compare its order handling, warehousing & dispatch systems with similar systems of company in cloth manufacturing
Competitive benchmarking	- Compare own performance and its own products with those of its most successful competitors.
Customer benchmarking	- The benchmark is a specification of what customers expect. - An entity compares its performance against what its customers expect

Methods of competitor benchmarking

- Published financial statements of competitors should be studied.
- Financial ratios obtained from the financial statements of competitor should be compared with similar ratios for the company.
- Where there are significant differences in performance, the possible reasons for differences should be considered.
- The products or services of competitors should be analysed in detail.
- By talking to customers and potential customers who have had dealings with a competitor, and who are willing to discuss what the competitor is offering
- Sales prices should be compared.

Competitor analysis should also include an assessment of the CSF of all firms in the market.

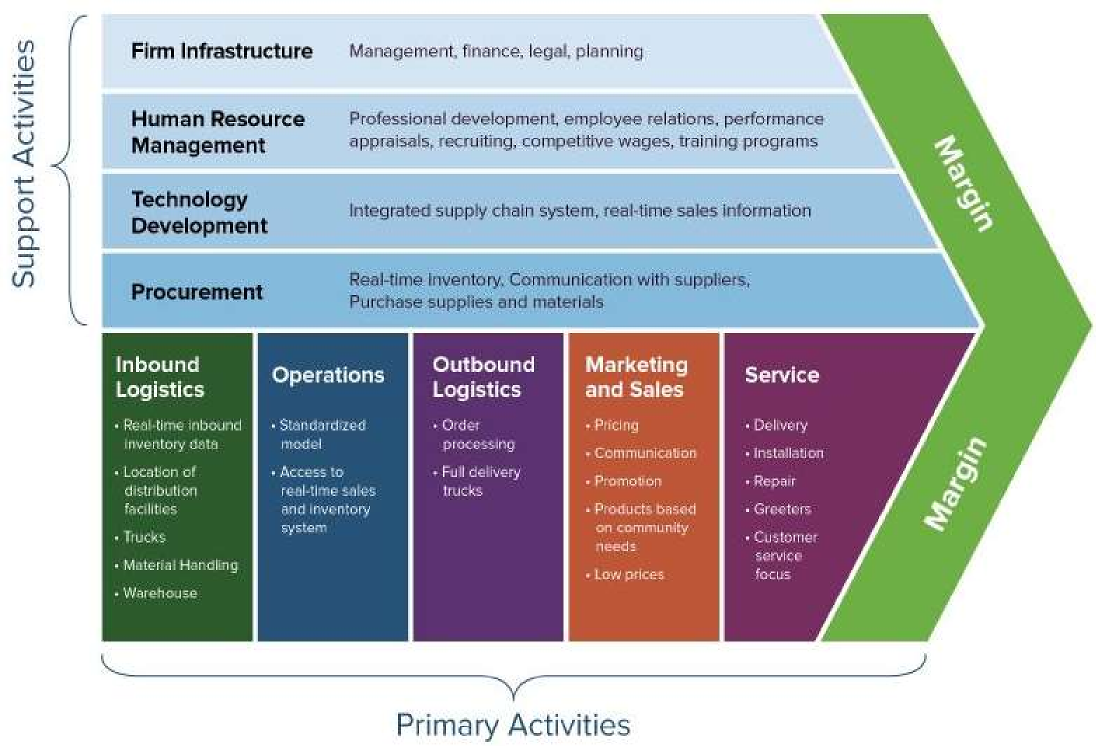
VALUE CHAIN

Definition of value

- Value relates to the benefit that a customer obtains from a product or service.
- Customers are willing to pay money because of the benefits they receive.
- Business entities create added value when they make goods and provide services.
  (e.g buying leather at Rs 1,000 and selling leather belt at Rs 5,000 creates a value of 4,000)
- Most successful business entities are those that are most successful in creating value.
- Customer should be willing to pay a higher price if he sees additional value in that product
  - This extra value might be real or perceived.
    (e.g. presumption of a good quality in a well-known brand name)
  - The extra value might relate to the quality or design features of the product.
  - Sometimes extra value can come from convenience of getting that immediately

The concept of the value chain by Porter

A **value chain** refers to inter-connected activities that create value. Activities within an organisation can be analysed into different categories. The total value added by the entity is the sum of the value created by each stage along the chain



- Value can be created by any of these activities.
- Company should analyse these activities to identify where they were most effective at creating value, and where they were least effective.
- Management can also identify which activities give them a competitive advantage

Primary Activities

1) Inbound logistics - All activities concerned with receiving and storing materials
2) Operations - The way in which inputs are converted to outputs
3) Outbound logistics - Activities associated with getting goods & services to buyer
4) Marketing and sales - Informing buyers and consumers about products & services
5) Service - Maintaining product performance after product has been sold

Support Activities

1) Procurement - How resources are acquired (e.g. negotiating with suppliers)
2) HRM - Recruiting, developing, motivating and rewarding the workforce
3) Technology Development
4) Infrastructure - Support systems and functions (e.g. finance, quality control etc)

Adding value

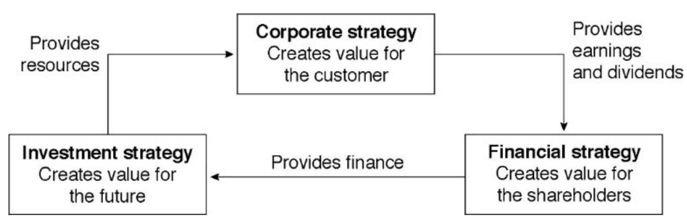
- Management should look for ways of adding value at each stage in primary value chain.
- Management should also consider ways in which support activities can add more value.

Methods of adding value

- Alter a product design, and include features that might meet the needs more better
- Making it easier for the customer to buy a product (e.g.providing a website for orders)
- Promoting a brand name. (giving a sense of better quality)
- Delivering a service or product more quickly.
- Providing a reliable service at the promised time

Value creation and strategic management

- By adding value, a firm will improve its profitability, by reducing costs or improving sales.
- Customer would also get a better-quality product or a lower selling price.
- The benefits can be re-invested to create more competitive advantage in the future.



RESOURCES AND COMPETENCES

Resources

- A resource is any asset, process, skill or item of knowledge that is controlled by the entity.
- Resources can be grouped into categories:
  - Human resources [Leaders, managers and other employees of an entity]
  - Physical resources. [Tangible assets of an entity]
  - Financial resources. [Financial assets and ability to acquire additional finance]
  - Intellectual capital. [Patents, trademarks, brand names acquired knowledge etc]

Threshold resources

- Resources that an entity needs in order to participate in industry and compete in market.
- Without threshold resources, an entity cannot survive in its industry and markets.

Unique resources

- Controlled by entity that competitors do not have and would have difficulty in acquiring.
- It might be obtained from:
  - Ownership of scarce raw materials (e.g. ownership of exploration rights or mines)
  - Location (e.g. a hydroelectric power generating company located near large waterfall)
  - A special privilege (e.g. ownership of patents or a unique franchise)
- Unique resources can be a source of competitive advantage, but can change over time e.g.:
  - Exceptionally talented employees might be approached by competitors
  - Competitors might find an alternative method of making a similar product

Competences

- Competences are activities or processes in which an entity uses its resources.
- They are created by bringing resources together and using them effectively.
- A competence can be defined as an ability to do something well.

Threshold competencies

- Activities, processes and abilities that provide an entity with the capability to provide a product or service with features that are sufficient to meet customer needs
- These are minimum capabilities needed to compete in a given market
  - The areas where the entity has the same level of competence as its competitors, or
  - These are easy to imitate (copy).

Core competencies

- Activities, processes and abilities that give the entity a capability of meeting CSF, and achieving competitive advantage.
- These are ways in which an entity uses its resources effectively, better than its competitors, and in ways that competitors cannot imitate or obtain.
- A competence which is not exceptional in some way is not considered as core competence

Sustainable core competences

- Competitive advantage is provided by sustainable core competences.
- These are core competences that can be sustained over a fairly long period of time
- Sustainable competences should be durable and/or difficult to imitate.

Core competences and the selection of markets

- A core competence gives a business entity a competitive advantage in a particular market.
- Core competence can be extended to other markets and other industries as well
- An entity should look for opportunities to expand into other markets where it sees an opportunity to exploit its core competences.

CAPABILITIES AND COMPETITIVE ADVANTAGE

Competitive advantage is any advantage that an entity gains over its competitors, that enables it to deliver more value to customers than its competitors. It is essential for sustained strategic success

Capabilities

- Capabilities are the ability to do something.
- An entity should have capabilities for gaining competitive advantage.
- These come from using and co-ordinating the resources and competences of the entity
- Each business entity should have capabilities that rivals cannot copy exactly.

Dynamic capabilities

- Business entities operate in a continually-changing environment.
- Dynamic capabilities is term used to describe ability of an entity to create new capabilities by adapting to its changing business environment, and:
  - Renewing its resource base
  - Developing new and improved core competences.
- Dynamic capabilities are abilities to create, extend and modify ways in which an entity operates and uses its resources in response to changes in the business environment.
- Dynamic capabilities refer to the ability of an entity to recognise the need for change and the opportunities for innovation, through new products, processes and services.

Cost efficiency and strategic capability

- Cost efficiency (for an accountant) means minimising costs through control over spending and the efficient use of resources.
- Company must achieve a certain level of cost efficiency to be able to compete and survive
- In strategic management, cost efficiency refers to the ability not only to minimise costs in current conditions, but to continually reduce costs over time.
- Cost efficiency has been described as a 'threshold strategic capability'.
- A cost efficiency capability is the result of both:
  - Making better use of resources or obtaining lower-cost resources, and
  - Improving competencies and capabilities

Ways of achieving cost efficiency

- **Economies of scale**
  - Ways in which average costs of production can be reduced by producing or operating at a higher volume of output.
  - Fixed costs is spreaded over a larger volume of output units
  - Large entities can make use of economies of scale.
  - Therefore businesses are very keen on continuous growth

- **Economies of scope**
  - In some industries, cost reductions might be achieved by making 2 or more products
  - Entity achieves lower costs per unit than competitors who produce only 1 product

Cost efficiency can become a strategic capability, which will give the organisation competitive advantage, for example by achieving 'cost leadership'

Corporate knowledge and strategic capability

- Corporate knowledge is knowledge and 'know-how' that is acquired by entity as a whole.
- It is created through the interaction between technologies, techniques and people.
- Knowledge gives a company a competitive advantage.
- It cannot be easily replicated by a competitor (i.e. something unique)
- A capability in knowledge management comes from a combination of unique resources and core competences:
  - Experience in an industry or market, and acquiring knowledge through experience
  - Knowledge that employees have or acquire through training
  - Management of people, and success in encouraging creativity and new ideas
  - Technology, which makes it possible to store and communicate knowledge
  - Management of IS/IT systems.
  - Information analysis techniques.

ANALYSING STRENGTHS AND WEAKNESSES

There are several techniques that might be used to assess resources and competences:

- Value chain analysis.
- Capability profile of the entity
- Resource audit.
- SWOT analysis.

Resource audit

A resource audit should identify all the significant resources that are used by an entity. These will vary according to the nature of the entity.

Human resources (Part-time and full-time employees, consultants, sub-contractors etc.)	▪ Size and composition of the workforce ▪ Efficiency of the workforce ▪ Flexibility of the workforce ▪ Rate of labour wastage/turnover ▪ Labour relations between management and workers ▪ Skills, experience, qualifications
Management	▪ Size of the management team ▪ Skills of the managers ▪ Nature of management structure and division of authority
Raw materials	▪ Costs as a percentage of total costs ▪ Sources, suppliers ▪ Availability ▪ Future provision. Scarcity? ▪ Alternative materials and alternative sources of supply
Non-current assets	▪ What are they? ▪ How old are they? What is their expected useful life? ▪ What is their current value? ▪ What condition are they in? ▪ What is the utilisation rate for each group of non-current assets?
Intangible resources	▪ Are there any intellectual rights, e.g. patent rights & copyrights? ▪ Are there valuable brand names? ▪ Does the organisation have any identifiable goodwill? ▪ What is the reputation of the entity with its customers?
Financial resources	▪ What is the capital of the entity? ▪ What are its sources of new capital? ▪ What are the cash flows of the entity? ▪ What are its sources of liquidity?
Internal controls and organisation	▪ How well does the entity control the use of its resources? ▪ How effective are its controls over efficient use of assets? ▪ How effective are its controls over accounting and reporting? ▪ How effective are its controls over compliance with regulations?

Evaluating resources (VIRO Framework)

- **V**alue — Does the resource provide competitive advantage?
- **I**mitability — Would it be costly for competitors to imitate the resource or acquire it?
- **R**arity — Do competitors own similar resources, or are the resources unique?
- **O**rganisation — Is the entity organised to exploit its resources to best advantage?

SWOT analysis

- SWOT is an abbreviation for Strengths, Weaknesses, Opportunities and Threats
- SWOT analysis is an important tool for auditing the overall strategic position of a business and its environment.
- SWOT analysis can be used in conjunction with other tools for position analysis
- To identify strengths and weaknesses, you should consider the following:
  - Resources
  - Competences
  - Capabilities
- To identify opportunities and threats, you should consider the following:
  - Changes, or possible changes, in the business environment
  - PESTEL analysis
  - Competitive environment.
- A SWOT analysis might be presented as four lists, in a cruciform chart, as follows.

Illustrative examples for a small company producing pharmaceuticals.

	Positive	Negative
Internal	**Strengths** - Extensive research knowledge - Highly-skilled scientists in workforce - High investment in equipment - Patents on six products - High profit margins	**Weaknesses** - Slow progress with research - Poor record of converting research projects into product development - Recent increase in labour turnover
External	**Opportunities** - Strong growth in total market demand - New scientific discoveries have not yet been fully exploited	**Threats** - Recent merger of major competitors - Risk of stricter regulation of new products

Interpretation of a SWOT analysis

- The significance or potential value/cost of each item is not considered in initial analysis
- Next step is to interpret it.
- Interpretation involves identifying those SWOTs that might be significant
- It involves ranking the SWOTs in some order of priority or importance.
- Strategic management should then consider how:
  - Major strengths & opportunities might be exploited to obtain competitive advantage
  - Major weaknesses and threats should be dealt with, in order to reduce the risks.

CH # 9 ETHICAL DECISION MAKING MODELS

BUSINESS ETHICS

- Ethics, also called 'moral philosophy' is a branch of Philosophy that defines and explains the concepts of right and wrong values, good and bad conduct, just and unjust decisions.
  - Should accountant conceal figures in annual report to make company look profitable ?
  - Should doctor donate organs of deceased person without his prior consent ?
  - Does manufacturing and selling cigarettes count as an ethical business ?
  - Should media companies advertise products that are injurious to health ?
  - Should lawyers continue to defend the suspect after knowing that he is guilty ?
- Ethics is a vast subject and has numerous definitions with varying nuances e.g:
  - "It is a set of moral principles or values"
    (This is relatively subjective since moral values vary from person to person)
  - "The principles, norms and standards of conduct governing an individual or group."
    (by Trevino and Nelson)
- Manuel Velasquez states that there are no ethical standards that are true absolutely, i.e., that the truth of all ethical standards depends on what a particular culture accepts.
- In organizations, rules of ethical conduct are developed that include corporate values, norms of dealing with suppliers and customers, professionally accepted behavior, gift policies, and other rules as to what is allowed or not within the working premises.

Business sense of ethical culture

A high ethical standing in corporate world consequently takes businesses to path of increased profits and growth. Whereas organizations inclined towards unethical practices are doomed.

Business committed to ethical behavior builds positivity in its relationship with employees, customers, investors, general public & other stakeholders and bring following benefits:

- Employees commitment
  - Employees trust that company is working for benefit of its employees and public
  - Employees who feel that their employer is not following ethical standards are more likely to break ethical code of conduct and compromise on company's values
- Investor confidence
  - Investors mainly look for financial fundamentals but they also look for a company that not just has a large market size but also is strong on ethical ground.
  - They understand that ethical culture within a company provides the right foundation and growth for the company in the right direction.
  - An organization without ethical standards is exposed to many risks and issues such as lawsuits, bad reputation, and loss of customers and profits.
- Customer satisfaction
  - A company's revenue comes from its customers
  - Long lasting relationship can only be built when the customer has trust in company
- Avoiding loss of profits
  - Unethical decisions potentially lead to significant loss along with other litigations.

Ethical issues and dilemmas in business

- In normal circumstances, there is a clear distinction between what is right and wrong
- On the other hand, there may be a situation when a problem requires an individual, group or organization to choose among several wrong or right actions
- **Ethical dilemmas** arise when norms and values are in conflict, and alternative possibilities lie within the two extremes of right and wrong.
  - These alternatives are not entirely right and wrong but fall somewhere in between.
  - Ideally, this means selecting an option that is the best among all the possibilities.
  - In such situations, the decision is based on the acceptability level of an individual.
  - Here decision maker is trapped in a state of confusion and needs guidance to follow.
  - For example, we all know that it is wrong to kill people but is it wrong to kill criminals. (In above example, between the two extremes comes the middle ground i.e. prisons)

"An ethical issue is a problem, situation or opportunity that requires an individual, group or organization to choose among several actions that must be evaluated as right or wrong, ethical or unethical" (Definition by Fraedrich and Ferrell)

<u>Guidance on ethical issues</u>

- Guiding principles for ethical decision making for a chartered accountant in Pakistan are given in ICAP Code of Ethics
- Additionally 2 frameworks for ethical decision-making are:
  - American Accounting Association (AAA) model
  - Tucker's 5-question model

ICAP's Code of Ethics for Chartered Accountants

- ICAP Code of Ethics is based on the provisions contained in the Code by IESBA of IFAC.
- Code establishes a conceptual framework that requires a CA to identify, evaluate, and address threats to compliance with the fundamental principles.
- That assists chartered accountants in complying with the ethical requirements of this Code and meeting their responsibility to act in the public interest.
- Code helps ICAP members meeting these obligations by providing with ethical guidance.

Professional accountants are required to comply with the following **5** fundamental principles:

1) INTEGRITY

- Straightforward & honest in professional & business relationships
- Integrity also implies fair dealing and truthfulness.
- Should not be associated with reports, returns, communications or other information where they believe that the information:
  - Contains a materially false or misleading statement;
  - Contains statements or information furnished recklessly; or
  - Omits or obscures required information to mislead

2) OBJECTIVITY

- Not to compromise their professional or business judgment because of bias, conflict of interest or the undue influence of others.
- For accountants in public practice, 'objectivity' is often associated with independence of mind and judgement.
- For accountants in business, however, the concept of independence is not much relevant (accountants in business are employees and are recipients of salaries and other benefits)
- Accountants in business should still try to apply the principle of objectivity in all the work that they do with the aim of being balanced, fair and unbiased

3) PROFESSIONAL COMPETENCE & DUE CARE

- Maintain & apply professional knowledge and skill to ensure that clients or employers receive competent professional service (using sound judgements)
- Act diligently in accordance with applicable technical and professional standards (carefully, thoroughly and on a timely basis) when providing professional services.
- Maintaining professional competence requires continuing awareness and understanding of relevant technical, professional and business developments. Continuing professional development (CPD) enables a CA to develop and maintain such competence
- CA shall also take reasonable steps to ensure that those working under his authority have appropriate training and supervision.
- Where appropriate, a CA shall make clients, employers or other users of the professional services or activities, aware of the limitations inherent in the services or activities.

4) CONFIDENTIALITY

CA should respect the confidentiality of information acquired as a result of professional and business relationships.

- Be alert to the possibility of inadvertent disclosure, including in a social environment, and particularly to a close business associate or an immediate or a close family member;
- Maintain confidentiality of information within the firm or employing organization;
- Maintain confidentiality of information disclosed by a prospective client/employer;
- Not disclose confidential information acquired as a result of professional and business relationships outside firm or employing organization without proper & specific authority;
- Not use such confidential information for personal or any 3rd party advantage;
- Not use or disclose any such confidential information, after that relationship has ended;
- Take reasonable steps to ensure that personnel under CA's control, and individuals from whom advice and assistance are obtained, respect the accountant's duty of confidentiality.

5) PROFESSIONAL BEHAVIOR

- Should comply with relevant laws and regulations and avoid any action that may bring discredit to the profession (as per the eyes of a reasonable and informed 3rd party).
- A CA shall not knowingly engage in any business, occupation or activity that impairs or might impair the integrity, objectivity or good reputation of the profession, and as a result would be incompatible with the fundamental principles

FRAMEWORKS FOR ETHICAL DECISION MAKING

American Accounting Association (AAA) model

American Accounting Association (AAA) model originates from a report by Langenderfer and Rockness in 1990. In the report, they suggest a, 7-step process for decision making

Step 1- Establishing the facts of the case.

- When decision-making process starts, there is no ambiguity about subject of the case
- Leading questions about the facts will revolved around What? Who? Where? When? How?
- Efforts are made to identify what we know or need to know, to clearly define the problem.

Step 2- Identify the ethical issues in the case.

- Examining the facts of the case and asking what ethical issues are at stake.
- All threats to compliance with fundamental principles are identified and explained.

Step 3- An identification of the norms, principles and values related to the case.

- Placing the decision in its social, ethical and (sometimes) professional behaviour context.
- In last context, professional codes of ethics or the social expectations of the profession are taken to be the norms, principles and values.

Step 4- Each alternative course of action is identified.

- Compiling a complete set of major practical alternatives one can make in a given situation.
- Alternatives should not consider the norms, principles and values identified in Step 3.
- It is expected that in these alternatives one may feel or see some form of compromise

Step 5- Matching norms, principles, and values to options

- Norms, principles & values (Step 3) are matched with different alternate options (Step 4)

Step 6- The consequences of the outcomes are considered.

- An analysis of implications and consequences of each possible alternate course of action.
- Should be analyzed in all respects: short and long run, positive and negative.

Step 7- The decision is taken.

- Final decision requires application of professional judgment
  (i.e. an application of accumulated knowledge and experience gained during initial professional development and through continuing professional development)
- Decision taken should demonstrate that selected option is well-informed ethical decision.

Tucker provides a 5-question model

Model is used to identify best possible choice to make for shareholders and other stakeholders
These questions are to be responded in following order to assess the value shown against each:

Questions	Values
Is it profitable?	Market values
Is it legal?	Legal values
Is it fair?	Social values
Is it right?	Personal values
Is it sustainable development?	Environmental values

- Generally, it happens that we immediately think of an obvious course of action that comes first to our mind (first order thinking)
- The Model leads us to second-order thinking.
- We re-think the facts and reframe the problem and create more than 1 course of actions

Value judgment

- This value analysis helps us to make a balanced decision for all stakeholders.
- The Tucker Model may be explained by understanding the following two approaches:

  1) Utilitarianism (or End-Point Ethics)

  - To determine whether an action is right or wrong, one must concentrate on its likely consequences, the end point or end result.
  - Seek the greatest benefit for the greatest number of stakeholders.
  - This obviously requires some compromises for certain segments of stakeholder.
  - The first question of the Model is directed to see the problem in the context of utility of the decision, before analysing it on ground rules and ethical principles.
  - If we look at a problem from perspective of each of 5 boxes on the chart, we might get some creative alternatives which might not come to mind if only 1st box is considered.

  2) Rule ethics

  - Rule ethics intends to follow the duty and norms relevant to the problem.
  - Intended decision is assessed on the basis of law of the land, or company's stated policies or any professional code applicable on the matter.
  - It appears easier to see the decisions as right or wrong on the basis of its legal value.
  - All legally right decisions may not produce social, personal, value for ethical decisions.