Effect Of Environmental Factors on Business Performance

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Abstract

This paper examines the effect of external and internal environments on business performance, with specific reference to the Nigerian business environment. The methodology adopted was basically theoretical and narrative based on aggregative and specific strength, weakness, opportunity and Treat (SWOT) Matrix and political, Ecological, social, Technology, legal and economic factors (PESTLE) Analysis models, respectively. A review of related literature and exploration of theoretical framework provided more insight into the various effects of the factors of the environments on business performance. The appraisal showed that both external and internal factors exert influence on and shape the life, growth and development of the business; external environment bears more relevance to strategic management, and businesses adjust to external environment. It further revealed that the government now plays more of regulatory role in the business environment in some sectors of the economy, and that, though certain measures had been put in place at various levels to engender conducive business environment for private sector participation, external factors such as multiple tax system, policy summersault, non-passage of the Freedom of Information (FOI) Bill into law, high cost of capital, high interest and inflation rates, terrorism, culture, religion, volatile exchange rates, susceptibility of the economy to external shocks, infrastructure decay, dismal power supply, etc., escalated cost of doing business in Nigeria and, thus, posed serious threats to firms performance. While many business organizations had leveraged on their strengths and explored opportunities in their environment, many more were overwhelmed by their weaknesses and, thus, failed before the growth and maturity stages, with the attendant implication that many small and medium scale enterprises did not grow, develop and transform into large and mega scale corporate businesses. Consequently, reconsideration of such environmental factors that impose unnecessary constraints on businesses in Nigeria was recommended.

Keywords: Environments of Businesses, Nigeria, Appraisal
Key words: Social Relevance, Social Integration, Profitability, 5-Star Hotel, Nigeria

1. Introduction

The modern business manager operates in more dynamic and turbulent environment. The change in the environment has been rapid and unpredictable. Economic variables have been complex both in form and impact on the practice of business in Nigeria. Consumers and clients have been showing complex behaviours both in local and international markets. The most dramatic change has been that exhibited by competitive pressures. Competitors have been applying one strategy or the other to adapt to the dynamic and unpredictable nature of the business environment.

The dynamic environment in which a business operates provides opportunities for it to grow develop and create value and wealth. It also poses some threats to the business. The primary concern is how the business affects people and natural environment as it produces and sells products necessary to satisfy customers, stakeholders and other constituents. By building key stakeholder relationships among government agencies, consumer entities, environmental groups and other constituents, a business can anticipate and manage issues and concerns that might otherwise have gone undetected until they had grown into major problems (Rainey, 2008). These entail conscientious analysis of both external and internal environment by the business.

Businesses are faced with challenges of social considerations which focus on specific issues that relate to their activities and transactions with employees, customers, shareholders, suppliers, etc. Further, social considerations include protecting the health and safety of the general population, avoiding harm to the natural environment, developing and deploying ethical standards and practices, meeting cultural and social norms, balancing interest of the business with the interests of the society, and being a proactive entity (Rainey, 2008). Political considerations are also of significant relevance as they have direct impact on the functioning and success of the business. Political and regulatory changes are usually manifestations of the social and economic conditions and issues. Equally of primary concern to the businesses, their customers and stakeholders are economic considerations which often focus on the direct effects of the exchange of goods and services, the flow of money and the relationships between the participants. Customers are either satisfied, dissatisfied or have a neutral opinion (KPN Report, 2007). Economic considerations also cover indirect implications of economic activities such as hidden costs of transactions and the externalities borne by the society. In this regard, the most crucial economic questions often pertain to environmental-related impacts. Usually, they are some of the multifaceted negative and unintended outcomes of products, processes and operations.

The foregoing implies that the environment of a business is the pattern of all the external and internal conditions and influences that affect its life, growth and development. Consequently, since growth and development through conspicuous industry and market positions are central to mission statement and vision of a thriving business, it is onerous on the corporate strategist to keep abreast with the factors of the business environment and the evolving trends of their features over time. In nature, the environmental factors and their influences are economic, political-legal, socio-cultural and technological. Since strategy formulation process incorporates futuristic tendencies in terms of business environment, business executives who simulate the process must be conversant with such factors in the environment, especially the external environment, which can potentially and significantly exert effects on their business and its future.

This paper is an attempt at appraising the external and internal environments of a typical business entity in Nigeria, with the generic objective of establishing the relative significance of the environments to business strategic management process. In the pursuit of this and other objectives, the following questions will be addressed, among others: What constitutes the external environment of a business? What are the peculiar features and driving forces? What constitutes the internal environment of a business? What are the unique features and driving forces? Which of these environments bears more relevance to strategic management process of a business entity? What specific environmental factors constrain growth and development of businesses in Nigeria? What measures are needed to enhance business activities in Nigeria?

The paper is structured into five sections. Following this introduction is section two which is conceptual clarification and literature review/theoretical framework. Section three discusses business environments and factors. Section four dwells on appraisal, pointing out the implications, of external and internal environmental factors to survival, growth and development of a business in relation to its mission statement, vision and the drive for prominence in industry and market place, while section five concludes the paper and proffers appropriate recommendations.

2. Conceptual Clarification and Literature Review/Theoretical Framework

The environment of a business is the aggregation of the pattern of all the external and internal conditions and influences that affect the existence, growth and development of the business. Analysis of business environment is the examination and appraisal of the opportunities and threats provided by the environment as well as the potential strengths and weaknesses the business possesses. Opportunities and threats are associated with external environment of a business while strengths and weaknesses are associated with internal environment of the business. Consequently, external analysis examines opportunities and threats that exist in the environment while internal analysis examines strengths and weaknesses within the business. Both opportunities and threats exist independently of the firm. If an issue would exist when a given business did not exist, then such an issue must be a factor in the external environment; otherwise, it is an internal environmental factor. Alternatively, an issue is an external environmental factor if it coexists with a business but the business cannot control or influence the issue. Opportunities are favorable conditions in the external environment that could produce rewards for the organization if acted upon properly. That is, they exist but must be acted on if the business is to benefit from them. Threats are conditions or barriers that may prevent the business unit from reaching its objectives.

Several studies have attempted to analyse or appraise the effects of environmental factors on various aspects of business organizations. These include Narver and Slater (1990); Jaworski and Kohli (1993); Nwokah (2008). Norzalita and Norjaya (2010), investigated the role of the external environment in the market orientation-performance linkage among SMEs in the agro-food sector in Malaysia and found that market-technology turbulence and competitive intensity did not moderate the relationship between market orientation and business performance.

Pulendran, Speed and Widing (2000) observe that the external environment in which organizations operate is complex and constantly changing; a significant characteristic of the external environment is competition. Organizations that recognize the presence and intensity of competition have a greater tendency to seek out information about customers for the purpose of evaluation and to use such information to their advantage (Slater and Narver, 1994). Recognition of the threat from competition drives business organizations to look to their customers for better ways to meet their needs, wants, and thereby enhances organizational performance (Bhuian, 1997). Accordingly, when competition is perceived as a threat by the organization, there is a greater tendency to adopt a market orientation (Pulendran et al.,2000). There has been a long tradition of support for the assumption that environmental factors influence the effectiveness of organizational variables (Appiah-Adu, 1998). Indeed, several studies have investigated the association between different environmental factors and established the effects of moderating influences on organizational variables (e.g., Slater and Narver,1994; Jaworski and Kohli, 1993; Greenley, 1995 and Han, Kim and Srivastava, 1998). Researchers have argued that firms should monitor their external environment when considering the development of a strong market-oriented culture (Kohli and Jaworski, 1990). To determine the influence of the external environment on business performance in transition economies, Golden et al. (1995), as cited in Appiah-Adu (2998), examined four factors: demand changes, product obsolescence, competitive pressures and product technology. These variables appear to mirror, respectively, four external factors, namely market growth - demand, market turbulence, competitive intensity and technological turbulence, which were identified as potential moderators of the market orientation–performance link by Kohli and Jaworski (1990).

In a study on the impact of external environment and self-serving motivation on physician's organizational citizenship behaviours, Ming-Chang and Tzu-Chuan (2006) found that external environment does not have significant impacts on job satisfaction, but does have significant negative effect on organizational citizenship behaviours. They also found out that self-serving motivation and job satisfaction also have positive effects on organizational citizenship behaviours, and that the meditative effect of job satisfaction is also significant. In a related study, Ghani, Nayan, Izaddin, Ghazali, Shafie Nayan (2010) analysed the critical internal and external factors that affect firms strategic planning in Malaysia. The internal and external factors examined in their study included strengths, weaknesses, opportunities and threats. They also analysed some dimensions that represented these variables. Their study showed that firm's strengths are related to their financial resources and the weaknesses are related to the firms' management. The study further revealed that the external factors which become opportunities to the firms are support and encouragement from the government, and that threats are the bureaucratic procedures that firms have to face in order to get plan approval and certificate of fitness. Thus, they emphasized that while firm's internal analysis is important to identify its strengths and weaknesses, its external analysis is important in order to identify current and future threats and opportunities, know its position and performance so that it can plan, compete and stay in business.

3. Business Environments and Factors

In analyzing and appraising Nigeria business environments and factors, we adapt the SWOT Matrix used by Wheelen Hungar (2010). The SWOT Matrix analysis technique combines firm's internal and external environments and their factors and, thus, helps visualize the analysis of business environment and enhance understanding of how environmental factors work together, culminating in the synthesis that when a business entity matched internal strengths to external opportunities, it creates core competencies in meeting the needs of its customers, and emphasizes that business should act to convert internal weaknesses into strengths and external threats into opportunities. However, we anchor detail analysis of external environment on PESTLE Model adapted from Wikipedia encyclopedia (www.wikipedia.org, 2010).

SWOT MATRIX

INTERNAL	**EXTERNAL**
Strength	Opportunities
Weakness	Treats

External Environment and its Factors (PESTLE Analysis Mode

Source: *www.wikipedia.org*

External Environment and its Factors (PESTLE Analysis Model)

The external environment of a business consists of a set of conditions and influences outside the business but which shape the life and continued existence of the business. These conditions and influences are outside the firm as a business unit, but which effect changes in the organization and the business entity cannot control but only adjusts to them.

The elements of the business external environment constitute the external environmental factors. Since strategy formulation is futuristic, it is pertinent for strategic managers to keep abreast with the external environmental factors and align their strategic processes with the dynamism of such external factors. The external environmental factors can be captured with the acronym PESTLE. This describes a framework of macro-environmental factors used in the environmental scanning component of strategic management (www.wikipedia.org). Therefore, in this paper, analysis of external environment and its factors is referred to as PESTLE Analysis Model, where:

P Political Factors;
E Economic Factors;
S Social Factors;
T Technological Factors;
L Legal Factors; and
E Ecological Factors.

Political Factors: These entail the extent and process of government direct or indirect intervention and influence on businesses in an economy. Specifically, political factors include such areas as tax policy, labour law, environmental law, trade restrictions, tariffs, incentives, other encouragements and political stability. Political factors may also include goods and services which the government wants to provide or be provided (merit goods) and those that the government does not want to be provided (demerit goods or merit bads). Furthermore, governments have great influence on the health, education, and infrastructure of a nation

Economic Factors: These includes, exchange rate, unemployment, demand and supply trend, economic growth, lending rates, exchange rates and the inflation rate. These factors have major impacts on how businesses operate and make decisions. For example, lending rates affect a firm's cost of capital and therefore the extent to which a business grows and expands. Exchange rates affect the costs of exporting goods and the supply and price of imported goods in an economy.

Social Factors: These are the cultural aspects and include health consciousness, population growth rate, age distribution, career attitudes and emphasis on safety nets. Trends in social factors affect the demand for a company's products and how that company operates. For example, an aging population may imply a smaller and less-willing workforce (thus increasing the cost of labour); government enhanced social insurance scheme may increase the demand for insurance services in a country. Furthermore, companies may change various management strategies to adapt to these social trends (such as recruiting older workers).

Technological Factors: This component of external environment includes technological aspects such as Research and Development (R&D) activity, automation, technology incentives and the rate of technological change. They can determine barriers to entry, minimum efficient production level and influence outsourcing decisions. Technological shifts can affect costs, quality, and stimulate further invention, innovation and competition.

Legal Factors: Included in this component are discrimination law, consumer law, antitrust law, environmental law which result to the establishment of (NESERA), employment and labour law, and health and safety law. These factors can affect how a company operates, its costs, and the demand for its products.

Ecological Factors: These include environmental aspects such as weather, climate, and climate change, drought; earthquake, and erosion which may affect industries like tourism, farming, and insurance. Growing awareness of the potential impacts of climate change is affecting how companies operate and the products they offer, both creating new markets and diminishing or destroying existing ones.

Internal Environment and its Factors (SWOT Analysis Model)

The internal environment of a business consists of a set of conditions, influences and elements within the business which are directly controlled and influenced by management of the business to shape the life and continued existence of the business in the direction of attainment of organizational goals and objectives. These conditions and influences are within the firm as a business unit, and it can control them.

The elements of the business internal environment constitute the internal environmental factors. Essentially, they are the employee attitudes, new equipment, processes, strategy, work environment, etc, which are encapsulated in the strengths and weaknesses of the business. The organization has the control of these matters because they happen within the organization unlike external environmental factors. Thompson and Strickland (2001) state that "Developing strategies is one of the tasks needed to achieve unity and coherence between the firm's internal ability, sources and skills with the external factors which are related to the firm". In line with this, David (1999) submits that any strategic should match firm's strengths and weaknesses with the surrounding to identify the best effective alternative strategy to be implemented. Therefore, the SWOT analysis technique can be explored to enhance firm's strengths and weaknesses so as to prepare for threats and opportunities provided by the external environment.

In this subsection, however, the thrust is on the internal environment of a business and its factors analysed within the framework of Strength, Weaknesses, Opportunities and Threats (SWOT) Matrix Analysis Model. Information regarding firm's strengths and weaknesses is generated from within the firm itself. Therefore, we emphasize strengths and weaknesses here as the aggregate components of internal environmental factors of a business entity, though SWOT analysis technique combines firm's internal and external environments and their factors. A firm's internal analysis involve examination and appraisal of such factors as its management, marketing, finance, operational/production and human resource. Ghani et al (2010) identify strength variables or factors of the business entity to include:

Experienced and skillful work force (Paulson, Fondahl and Parker, 1992): This enhances rational decisions and fulfillment of project requirement (Abdul and Abdul, 1999).

Feasible Objectives: The business should have achievable strong short and long term objectives, and strategic managers could analyze the performance of any projects undertaken and at the same time plan for potential future development projects.

Strong Financial Sources: These facilitate further expansion of the business, allow the business to invest in more modern and sophisticated product concepts to satisfy customers' needs, satisfy the firm's constituents and abide by the government policy.

Effective and Efficient Management and Administration System: This ensures smooth operation.

Good Image and Reputation: This attracts potential investors and confers competitive and market position advantages on the firm.

Currency of Techniques, Technology and Processes: The use of current technique, technology and processes confers competitive advantage of unequal measure on the firm in its procurement projects, design, concept and quality of inputs and products.

Timely Information: This enables a firm to explore a competitive opportunity relative to its competitors in the industry. A good example is Zenith Bank's Initial Public Offer in 2004 shortly before the Central Bank of Nigeria's N25 billion bank recapitalization policy. Weakness variables or factors of the firm include:

Under Capacity Utilization: This results to suboptimal allocation of firm's scarce resources, competitive disadvantage and unattained organizational objectives. Inadequate Experience and Technical Skills: This leads to low quality of strategy, concept, design, processes and products.

Inadequate Financial Resource and inefficiency in financial management: This results to loss of opportunities and increases susceptibility to threats.

Inadequate know-how on evolution and application of current technology: This leads to inappropriate strategies, designs and processes and culminates to inability to explore opportunities.

Inability to attract Skilled and Professional Indigenous Workers: This leaves the firm with the alternative of parading low profile work force with its attendance competitive disadvantage.

4. Appraisal and Implications

The above factors are present in the external business environment in Nigeria, and firms have evolved various strategic management approaches in adjusting to them. Priori to the privatization and commercialization programmes, the Nigerian government was directly and significantly involved in businesses. But the programmes have relegated the government more to its expected regulatory role and indirect influence in the Nigerian business environment. Examples are in the businesses of telecommunication, banking and insurance, transportation and, in the past decade, tertiary education. These have opened windows of opportunities to businesses in the country. However, infrastructure (power, roads, water, health care, quality education, credit accessibility, etc) and multiple tax system remain serious external environmental challenges to businesses in Nigeria. Other threats emanate from high cost of capital (i.e., high interest rate), exchange rate volatility, high rate of inflation, weak domestic currency, frequent policy summersault, etc. Further, social safety nets have not been given desired attention in policies and programmes of the government, and this poses a threat to businesses in the country. Further, the highly skewed income distribution pattern in which over 70% of Nigerians live below the poverty line has negative effects on demand for companies' products, although firms have adopted micro and mini unit packaging (e.g. sachets) at appropriate prices as strategic approach to this threat.

On the technological front, investment has been very minimal in research and development, and the process of automation hampered by the near-zero public power supply to drive and accelerate the technological process and adequately stimulate invention, innovation and competition and engender value for money. Alternative power supply increases the cost of doing business and retards the investment in research and development. For the environmental factors, especially those associated with the vagaries of weather conditions, efforts are being made to control and minimize their adverse effects on the environment and business. On business level, some firms switch products in line with weather dictates as strategic approaches, while on national, the government agency, national Emergency Management Agency (NEMA) is charged with this strategic policy responsibility. However, much has not been achieved in this direction. On the legal factors, most existing laws seem obsolete in the current democratic dispensation. This is one of the reasons for the heightened pressure on the National Assemble to pass the Freedom of Information (FOI) Bill into law. This will go a long way in strengthening business external environment in Nigeria, reduce the threats posed, and increases the opportunities provided, by legal factors to the businesses.

Many business organizations in Nigeria have leveraged on their internal factors (strengths) to explore opportunities in the Nigerian business environment. Examples are the market leaders and emerging firms in the communications, banking, entertainment, fast food, talent hunt and service industries. However, many more businesses fail before the growth and maturity stage due mainly to negative internal factors (weaknesses). This has accounted for the inability of many small and medium scale enterprises to grow, develop and transform into large and mega scale corporate businesses. Even incorporated businesses have failed due to internal factors. Examples abound in banking business in Nigeria and government-floated transportation, downstream oil, communications businesses, etc. In the case of incorporated businesses, failure of the corporate governance has been the major internal factor responsible for high failure rate. Current corporate health of some banks in Nigeria today, where the unrealistic salaries and allowances paid to employees and the management staff of these banks signify corporate and strategic management inadequacy, speaks volume in this regard. Also influence of culture on business ethics has substituted 'best-man-for-the-job' with 'relation-for-the-job' and enthronement of mediocrity in management composition and competence thereby escalating the weaknesses of many businesses and their eventual closure.

Furthermore, many businesses are incapacitated by inadequate financial resources and bedeviled with fraudulent reporting, greed and recklessness, short termism, executive compensation, poor risk attitude, etc.

5. Conclusion and Recommendations

This paper has analysed and appraised business external and internal environments, with specific reference to the Nigerian business environment. The analysis has shown that both external and internal environmental factors exert influence on and shape the life, growth and development of the business. It has also shown that external environment and its factors bear more relevance to business strategic management. Specifically, the analysis has shown that businesses have no direct control or influence over their external environment, unlike their internal environment. Therefore, strategic management skill and expertise are sine quo none to appropriate and rewarding analysis of external environment if a business must successfully explore opportunities provided by the environment to achieve its mission goal in the face of threats inherent in the environment.

At present, the government plays more of regulatory role in the business environment in some sectors of the economy, without direct intervention or involvement in economic enterprises. Although, certain measures have been put in place at various levels to engender conducive business environment for private sector participation, the paper notes that certain external environmental factors such as multiple tax system, policy summersault, non-passage of the Freedom of Information (FOI) Bill into law, high cost of capital, high interest and inflation rates, volatile exchange rates, infrastructure decay, dismal power supply, etc., escalates cost of doing business in Nigeria and, thus, poses a serious threat to business firms and industries.

The analysis further revealed that while many business organizations had leveraged on their strengths and explored opportunities in their external environment, many more were overwhelmed by their weaknesses and, thus failed before the growth and maturity stage, with the attendant implication that many small and medium scale enterprises do not grow, develop and transform into large and mega scale corporate businesses. Weaknesses have also obliterated many incorporated businesses into oblivion, even after attaining growth and maturity stages. Among such weaknesses or negative internal factors are mediocrity, influence of culture on business ethics, short term business horizon resulting from poor risk attitude, inadequate financial resources and sharp practices; all culminating to management incompetence, inefficiency and strategic management misalignment.

Consequently, this paper recommends for reconsideration of such environmental factors that impose unnecessary constraints on businesses in Nigeria. Specifically, multiple tax system should be jettisoned; exchange rate stability should be pursued; the passage of Freedom of Information Bill into law should be hastened; infrastructure, especially electricity, should be strengthened. Businesses should minimize their weaknesses by paradigm shift from internal factors that weaken management inefficiencies.

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