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BUSN 11

INTRODUCTION TO BUSINESS

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INTRODUCTION TO BUSINESS

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With love and
appreciation
to Kathy,
the best friend imaginable!

—Marce Kelly

To Jenny,
the book is done, let's play!

—Chuck Williams

LETTER TO STUDENTS

The idea for this book—a whole new way of learning—began with students like you across the country. We paid attention to students who wanted to learn about business without slogging through endless pages of dry text. We listened to students who wanted to sit through class without craving a triple espresso. We responded to students who wanted to use their favorite gadgets to prepare for tests.

So we are confident that BUSN will meet your needs. The short, lively text covers all the key concepts without the fluff. The examples are relevant and engaging, and the visual style makes the book fun to read. But the text is only part of the package. You can access a rich variety of study tools via computer or iPad—the choice is yours.

Marce Kelly

© Brent Smith, Butler University

Chuck Williams

We did one other thing we hope you'll like. We paid a lot of attention to students' concerns about the high price of college textbooks. We made it our mission to ensure that our package not only meets your needs but does so without busting your budget!

This innovative, student-focused package was developed by the authors—Marce Kelly and Chuck Williams—and the experienced Cengage Learning publishers. The Cengage team contributed a deep understanding of students and professors across the nation, and the authors brought years of teaching and business experience.

Marce Kelly, who earned her MBA from UCLA's Anderson School of Management, spent the first 14 years of her career in marketing, building brands for Neutrogena and The Walt Disney Corporation. But her true love is teaching, so in 2000 she accepted a full-time teaching position at Santa Monica College. Professor Kelly has received seven Outstanding Instructor awards from the International Education Center and has been named four times to *Who's Who Among American Teachers*.

Chuck Williams' interests include employee recruitment and turnover, performance appraisal, and employee training and goal setting. Most recently, he was the Dean of Butler University's College of Business. He has taught in executive development programs at Oklahoma State University, the University of Oklahoma, Texas Christian University, and the University of the Pacific. Dr. Williams was honored by TCU's M.J. Neeley School of Business with the undergraduate Outstanding Faculty Teaching Award, was a recipient of TCU's Dean's Teaching Award, and was TCU's nominee for the U.S. Professor of the Year competition sponsored by the Carnegie Foundation for the Advancement of Teaching. He has written three other textbooks: *Management, Effective Management: A Multimedia Approach,* and *MGMT*.

We would appreciate any comments or suggestions you want to offer about this package. You can reach Chuck Williams at crwillia@butler.edu, and Marce Kelly at marcella.kelly@gmail.com. We wish you a fun, positive, productive term, and look forward to your feedback!

1 Business Now: Change Is the Only Constant


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LEARNING OBJECTIVES

After studying this chapter, you will be able to:

- **1-1** Define business and discuss the role of business in the economy
- **1-2** Explain the evolution of modern business
- **1-3** Discuss the role of nonprofit organizations in the economy
- **1-4** Outline the core factors of production and how they affect the economy
- **1-5** Describe today's business environment and discuss each key dimension
- **1-6** Explain how current business trends might affect your career choices

Remember to visit **PAGE 17** for additional **STUDY TOOLS**

1-1 BUSINESS NOW: MOVING AT BREAKNECK SPEED

Day by day, the business world simply spins faster. Industries rise—and sometimes fall—in the course of a few short months. Technologies forge instant connections across the globe. Powerful new trends surface and submerge, sometimes within less than a year. In this fast-paced, fluid environment, change is the only constant. According to Charles Darwin, it is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to change. And so it is with business.

Successful firms lean forward and embrace the change. They seek the opportunities and avoid the pitfalls. They carefully evaluate risks. They completely understand their market, and they adhere to ethical practices. Their core goal: to generate long-term profits by delivering unsurpassed **value** to their customers.

value The relationship between the price of a good or a service and the benefits that it offers its customers.

Over the past decade, the explosive growth in social media has played a pivotal new role for businesses and consumers alike in today's dynamic business environment. Digging deeper into current culture, several leading-edge trendspotting experts have recently identified an array of key trends likely to shape the world's economies as we close out the turbulent teenage years of the twenty-first century. A few highlights:

- **Instant Skills:** Remember how the rise of Instagram made all of us into pseudo professional photographers? Well, Trendwatching.com predicts that hundreds of millions of status-hungry

"consumers will care less about what they *have or buy* and more about what they can *do or create*"—seeking services that eliminate time and learning barriers to their creation of professional quality output.

- **Fun and Games:** Research suggests that the average human attention span, currently only slightly longer than that of a goldfish, is decreasing rapidly. Not surprisingly, capturing and retaining the attention of customers, employees, and investors is more challenging than ever. In spite of declining attention spans, creating a sense of fun is gaining momentum as an effective tool for engaging audiences. It's fairly easy to understand why—wouldn't you rather do something fun than something boring? Swedish amusement park Liseberg recently released an app to accompany its new Helix roller coaster. Attendees standing in line for the attraction could use the app to play a free Helix-themed game, and every 15 minutes, the player with the highest score got a pass to skip the line. This strategy was not only creative, but it also increased visitors' fun! Similarly, workplace messaging app Slack became one of the fastest growing business applications in history due, in part, to its playful sense of humor. For instance, Slack allows users to create custom emojis using colleagues' faces and displays error messages such as, "We've seen this problem clear up with a restart of your browser, a solution which we suggest to you now only with great regret and self-loathing."

> "You miss 100% of the shots you don't take."
>
> —WAYNE GRETZKY. HOCKEY STAR

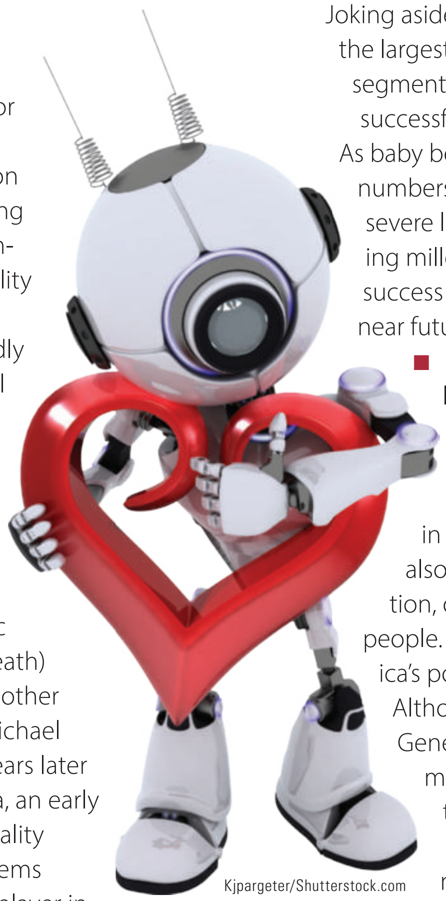
- **Robolove:** Everyone knows that robots can save time and money—and who doesn't like efficiency? But do we like the robots themselves? Many people imagine a bleak robotic future with robocops out of control and robo-workers putting human workers out of work. That may well happen, but Trendwatching.com predicts that many of us will thoroughly enjoy our early contacts with robots. For instance, Düsseldorf Airport in Germany recently unveiled the world's first robotic parking valet. Customers leave their car, and a robot picks it up and positions the vehicle in one of 249 dedicated spaces. The system connects to the airport's flight database, meaning that customers find their vehicle ready and waiting for them upon their return. Hard to get more convenient than that—and the robotic valet doesn't even expect a tip![1]

- **Virtual Experience Economy:** Anyone who was nearly plowed over in 2016 by someone with his or her head down—totally engrossed in the search for an elusive Pokemon (or maybe you were the one plowing people down)—knows just how immersive a virtual or augmented reality experience can be. Trendspotting experts at Trendwatching.com boldly project that "digital experiences will quickly come to carry a status-weight equal to 'real' experiences, if not become more sought-after and prized." Take music concerts for example. The holographic "performance" of rapper Tupac's Shakur at the 2012 Coachella music festival (15 years after the artist's death) garnered more headlines than any other concert that year. A holographic Michael Jackson made similar waves two years later at the 2014 Billboard Awards. China, an early developer and adopter of virtual reality games and shopping programs, seems poised to become a leading-edge player in the virtual experience economy.[2]

- **Taking Millennials Seriously:** The millennial generation—comprised of people born between 1980 and 1995—likely includes many of the students reading this text. Millennials have been at the butt end of a lot of jokes about their outsized sense of entitlement, large number of meaningless trophies, and "addiction" to their cell phones. The *Los Angeles Times*, for example, recently published a "Millennial Pledge" that it suggested all millennials affirm before they qualify for actual adulthood. A few excerpts:

    - Just once, I will try eating without texting.
    - I will not consider the cilantro on my taco to be a vegetable.
    - Each year, I will pen at least one thank-you note using what's left of my cursive writing skills.
    - I will vote. Always.
    - I will force myself to finally make a phone call.
    - If my first-born is a boy, I promise not to name him Uber.

    Joking aside, millennials now represent both the largest customer and the largest employee segment of the population, which means that successful businesses must take them seriously. As baby boomers continue to retire in record numbers, businesses will soon begin to face a severe leadership gap. Training and developing millennials to fill that gap will be a critical success factor for many businesses in the very near future.



Kjpargeter/Shutterstock.com

- **Preparing for Generation Z:** As the last millennials move through college and enter the workforce, Generation Z—comprised of people born between 1996 and 2011—is rolling in right behind them. Generation Z, also known as the Digital Native generation, outnumbers millennials by one million people. In fact, more than a quarter of America's population belongs to this generation. Although it would be easy to characterize Generation Z as an exaggerated version of millennials, it wouldn't do them justice—they are fundamentally different. Millennials shaped the Internet, but digital natives can't remember a world without it. The defining event of generation Z was the Great Recession, which means that many of them don't trust business. While their millennial counterparts were glad to be "walking billboards" for trendy brands such as Hollister, Abercrombie & Fitch, and Supreme, the most stylish digital natives are likely to sport vintage clothing from thrift stores. Digital natives don't feel entitled to a great job when they graduate college; they think they'll be lucky to get one. In the meantime, they are saving their money, only spending when a business offers them *value*. Digital natives use their considerable technical prowess to seek out the best possible values; no-frills, only-pay-for-what-you-use businesses are highly appealing to them. Similar to millennials, digital natives tend to be extremely tolerant and inclusive, with little understanding of or room in their lives for bigotry of any kind. They also tend to have very short attention spans (8 seconds on average), in part because they juggle their lives among an

OOPS! WHAT WERE THEY THINKING?

Not Every Dumb Move Is an Utter Disaster…

In the wake of disastrous mistakes and outrageous mismanagement across our economy, it might be tough to remember that some mistakes are actually pretty amusing. Several examples might help remind you.

- **Bad fabric, not fat thighs:** In early 2013, Lululemon Athletica was forced to recall its popular (and expensive) yoga pants, because many women found them utterly see-through. Later in the year, the founder of the firm was forced to resign after blaming the problem on women with fat thighs who rubbed the fabric too sheer with multiple uses.[3]
- **Apple angst:** In a rare display of new product development weakness, Apple released its Maps program before it was ready for the Big Time. Mostly harmless, the program baffled millions of trusting consumers. But in Fairbanks, Alaska, it directed hapless users onto active runways of the international airport. Fortunately, there were no collisions—the worst harm done was to Siri's reputation as a navigator.[4]
- **Geography lessons needed:** In 2016, Coca-Cola sent a promotional tweet featuring an outdated map of Russia. Offended Russian patriots responded with pictures of themselves pouring the soft drink into toilets with the hashtag #BanCocaCola.[5]
- **Thank you, Captain Obvious!** A surprising number of firms just can't seem to credit their customers with even basic intelligence. Marks & Spencer's labeled one of their Bread Puddings, PRODUCT WILL BE HOT AFTER HEATING. On a Sears hairdryer, DO NOT USE WHILE SLEEPING. And on packaging for a Rowenta iron, DO NOT IRON CLOTHES ON BODY. While these warnings most likely have a legal backstory, it's hard for a reasonable consumer not to see them as silly goofs.[6]

average of five different screens. In sum, millennials approached adulthood hoping to be discovered, while digital natives approach adulthood planning to work for success.[7]

1-1a Business Basics: Some Key Definitions

While you can certainly recognize a business when you see one, more formal definitions may help as you read through this book. A **business** is any organization or activity that provides goods and services in an effort to earn a **Profit** is the financial reward that comes from starting and running a business. More specifically, profit is the money that a business earns in sales (or revenue), minus expenses such as the cost of goods and the cost of salaries. But clearly, not every business earns a profit all the time. When a business brings in less money than it needs to cover expenses, it incurs a **loss**. If you launch a music label, for instance, you'll need to pay your artists, lease a studio, and purchase equipment, among other expenses. If your label generates hits, you'll earn more than enough to cover all your expenses and make yourself rich. But a series of duds could leave you holding the bag. Just the possibility of earning a profit provides a powerful incentive for people of all backgrounds to launch their own enterprises. But unfortunately, the rate of new business start-ups has been decreasing over the past few years. As the economy has finally emerged from the Great Recession, and unemployment and financial ruin are less of a threat, fewer people have been motivated to risk starting new businesses.[8] People who do risk their time, money, and other resources to start and manage a business are called **entrepreneurs**.

Interestingly, as entrepreneurs create wealth for themselves, they produce a ripple effect that enriches everyone around them. For instance, if your new website becomes the next Facebook, who will benefit? Clearly, *you* will. And you'll probably spend at least some of that money enriching your local clubs, clothing stores, and car dealerships. But others will benefit, too, including your members, advertisers on your site and the staff who support them, contractors who build your facilities, and the government that collects your taxes. The impact of one successful entrepreneur can extend to the far reaches of the economy. In fact, fast-growing new firms generate about 10% of all new jobs in any given year.[9] Multiply the impact by thousands of entrepreneurs—each

business Any organization or activity that provides goods and services in an effort to earn a profit.

profit The money that a business earns in sales (or revenue), minus expenses, such as the cost of goods and the cost of salaries. Revenue − Expenses = Profit (or Loss).

loss When a business incurs expenses that are greater than its revenue.

entrepreneurs People who risk their time, money, and other resources to start and manage a business.

working in his or her own self-interest—and you can see how the profit motive benefits virtually everyone.

From a bigger-picture perspective, business drives up the **standard of living** for people worldwide, contributing to a higher **quality of life**. Businesses not only provide the products and services that people enjoy but also provide the jobs that people need. Beyond the obvious, business contributes to society through innovation—think cars, TVs, and tablet computers. Business also helps raise the standard of living through taxes, which the government spends on projects that range from streetlights to environmental cleanup. Socially responsible firms contribute even more by actively advocating for the well-being of the society that feeds their success.

1-2 THE HISTORY OF BUSINESS: PUTTING IT ALL IN CONTEXT

You may be surprised to learn that—unlike today—business hasn't always been focused on what the customer wants. In fact, business in the United States has changed rather dramatically over the past 200–300 years. Most business historians divide the history of American business into five distinct eras, which overlap during the periods of transition:

- **The Industrial Revolution:** Technological advances fueled a period of rapid industrialization in America from the mid-1700s to the mid-1800s. As mass production took hold, huge factories replaced skilled artisan workshops. The factories hired large numbers of semiskilled workers who specialized in a limited number of tasks. The result was unprecedented production efficiency but also a loss of individual ownership and personal pride in the production process.
- **The Entrepreneurship Era:** Building on the foundation of the Industrial Revolution, large-scale entrepreneurs emerged in the second half of the 1800s, building business empires. These industrial titans created enormous wealth, raising the overall standard of living across the country. But many also dominated their markets, forcing out competitors, manipulating prices, exploiting workers, and decimating the environment. Toward the end of the 1800s, the government stepped into the business realm, passing laws to regulate business and protect consumers and workers, creating more balance in the economy.
- **The Production Era:** In the early part of the 1900s, major businesses focused on further refining the production process and creating greater efficiencies. Jobs became even more specialized, increasing productivity and lowering costs and prices. In 1913, Henry Ford introduced the assembly line, which quickly became standard across major manufacturing industries. With managers focused on efficiency, the customer was an afterthought. But when customers tightened their belts during the Great Depression and World War II, businesses took notice. The "hard sell" emerged: aggressive persuasion designed to separate consumers from their cash.
- **The Marketing Era:** After World War II, the balance of power shifted away from producers and toward consumers, flooding the market with enticing choices. To differentiate themselves from their competitors, businesses began to develop brands, or distinctive identities, to help consumers understand the differences among various products. The *marketing concept* emerged: a consumer focus that permeates successful companies in every department, at every level. This approach continues to influence business decisions today as global competition heats up to unprecedented levels.
- **The Relationship Era:** Building on the marketing concept, today, leading-edge firms look beyond each

standard of living The quality and quantity of goods and services available to a population.

quality of life The overall sense of well-being experienced by either an individual or a group.

Hulton Collection/Hulton Archive/Getty Images

Henry Ford's assembly line began operation on December 1, 1913. Initially developed for the Model T, this new production system allowed manufacturers of all kinds to output products like never before.

The Connection Economy

Success today no longer requires building great things, although there will always be big rewards for building the *best* new things (see Apple, Tesla, and Virgin, among other success stories). According to industry leaders, the most successful firms of the present rely on connection—either connecting buyers and sellers or connecting consumers and information. Uber, the largest ride-sharing company, owns no vehicles but connects people to rides and drivers to customers. Airbnb, the largest provider of accommodations, owns no real estate but connects people to lodging. Kickstarter and Indiegogo, both giants of crowdfunding, have no money to invest but may soon surpass traditional venture capital firms by connecting investors to opportunities. According to entrepreneur and author Seth Godin, the connection economy works best when the following four conditions are met:

1. ***Coordination.* Without coordination, connections can't happen. In fact, the most significant business opportunities may lie in areas that currently appear chaotic.**
2. ***Trust.* Finding ways to connect and create value only works when the players share basic trust.**
3. ***Permission.* When you offer ideas to people who give you permission to do so, it's a resource. Without that permission, it's an annoyance. What's new and significant is that the permission must be earned, and not requested.**
4. ***The exchange of ideas.* True value emerges when people exchange ideas deliberately and with established purpose (at a meet-up or conference, for instance).**

Godin also emphases the importance of generosity and art. No one wants to connect with a person who always takes but never gives back. You must add value to all of your interactions to make the connection worthwhile. Art is important, according to Godin, because forward-thinking people are looking for the extraordinary. Traditional systems are inherently boring and unremarkable. In the connection economy, people are seeking the *remarkable*—the things that are truly worthy of remark.[10]

immediate transaction with a customer and aim to build long-term relationships. Satisfied customers can become advocates for a business, spreading the word with more speed and credibility than even the best promotional campaign. And cultivating current customers is more profitable than constantly seeking new ones. One key tool is technology. Using the Web and other digital resources, businesses gather detailed information about their customers and use these data to serve them better, "bringing a level of customer centricity that we've never seen before," according to Graeme Noseworthy, marketing director for IBM.

1-3 NONPROFITS AND THE ECONOMY: THE BUSINESS OF DOING GOOD

Nonprofit organizations play a critical role in the economy, often working hand in hand with businesses to improve the quality of life in our society. Focusing on areas such as health, human services, education, art, religion, and culture, **nonprofits** are business-*like* establishments, but their primary goals do not include profits. Chuck Bean, executive director of the Nonprofit Roundtable, explains: "By definition, nonprofits are not in the business of financial gain. We're in the business of doing good. However, nonprofits are still businesses in every other sense—they employ people, they take in revenue, they produce goods and services and contribute in significant ways to our region's economic stability and growth." Nationwide, nonprofits employ about one in ten workers, accounting for more paid workers than the entire construction industry and more than the finance, insurance, and real-estate sectors combined. And nonprofit museums, schools, theaters, and orchestras have become economic magnets for many communities, drawing additional investment.[11]

1-4 FACTORS OF PRODUCTION: THE BASIC BUILDING BLOCKS

Both businesses and nonprofits rely on **factors of production**—four fundamental resources—to achieve their objectives. Some combination of these factors is crucial for an economic system to work and create wealth. As you read through the factors, keep in mind that they don't come free of charge. Human resources, for instance, require wages, while entrepreneurs need a profit incentive.

- **Natural Resources:** This factor includes all inputs that offer value in their natural state, such as land, fresh water, wind, and mineral deposits. Most natural

nonprofits Business-like establishments that employ people and produce goods and services with the fundamental goal of contributing to the community rather than generating financial gain.

factors of production Four fundamental elements—natural resources, capital, human resources, and entrepreneurship—that businesses need to achieve their objectives.

kojoku/Shutterstock.com

Many businesses work with nonprofits to boost their impact in the community.

resources must be extracted, purified, or harnessed; people cannot actually create them. (Note that agricultural products, which people do create through planting and tending, are not a natural resource.) The value of all natural resources tends to rise with high demand, low supply, or both.

- **Capital:** This factor includes machines, tools, buildings, information, and technology—the synthetic resources that a business needs to produce goods or services. Computers and telecommunications capability have become pivotal elements of capital across a surprising range of industries, from financial services to professional sports. You may be surprised to learn that in this context, capital does not include money, but, clearly, businesses use money to acquire, maintain, and upgrade their capital.
- **Human Resources:** This factor encompasses the physical, intellectual, and creative contributions of everyone who works within an economy. As technology replaces a growing number of manual labor jobs, education and motivation have become increasingly important to human resource development. Given the importance of knowledge to workforce effectiveness, some business experts, such as management guru Peter Drucker, break out knowledge as its own category, separate from human resources.

business environment The setting in which business operates. The five key components are economic environment, competitive environment, technological environment, social environment, and global environment.

- **Entrepreneurship:** Entrepreneurs are people who take the risk of launching and operating their own businesses, largely in response to the profit incentive. They tend to see opportunities where others don't, and they use their own resources to capitalize on that potential. Entrepreneurial enterprises can kick-start an economy, creating a tidal wave of opportunity by harnessing the other factors of production. But entrepreneurs don't thrive in an environment that doesn't support them. The key ingredient is economic freedom: freedom of choice (whom to hire, for instance, or what to produce), freedom from excess regulation, and freedom from too much taxation. Protection from corruption and unfair competition is another entrepreneurial "must."

Clearly, all of these factors must be in place for an economy to thrive. But which factor is most important? One way to answer that question is to examine current economies around the world. Russia and China are both rich in natural resources and human resources, and both countries have a solid level of capital (growing in China, and deteriorating in Russia). Yet, neither country is wealthy; both rank relatively low in terms of gross national income per person. The missing ingredient seems to be entrepreneurship, limited in Russia largely through corruption and in China through government interference and taxes. Contrast those examples with, say, Hong Kong. The population is small, and the natural resources are severely limited, yet Hong Kong has consistently ranked among the richest regions in Asia. The reason: operating for many years under the British legal and economic system, the government actively encouraged entrepreneurship, which fueled the creation of wealth. Recognizing the potential of entrepreneurship, China has recently done more to relax regulations and support free enterprise. The result has been tremendous growth, which may yet bring China into the ranks of the wealthier nations.[12]

1-5 THE BUSINESS ENVIRONMENT: THE CONTEXT FOR SUCCESS

No business operates in a vacuum. Outside factors play a vital role in determining whether each individual business succeeds or fails. Likewise, the broader **business environment** can make the critical difference in whether an overall economy thrives or disintegrates. The five key dimensions of the business environment are the economic environment, the competitive environment, the technological environment, the social environment, and the global environment, as shown in Exhibit 1.1.

1-5a The Economic Environment

In September 2008, the U.S. economy plunged into the worst fiscal crisis since the Great Depression. Huge, venerable financial institutions faced collapse, spurring unprecedented bailouts by the federal government and the Federal Reserve. By the end of the year, the stock market had lost more than a third of its value, and 11.1 million Americans were out of work. Housing prices fell precipitously, and foreclosure rates reached record levels. As fear swept through the banking industry, neither businesses nor individuals could borrow money to meet their needs. Economic turmoil in the United States spread quickly around the world, fueling a global economic crisis.

The U.S. economy continued to stagger through 2010 and 2011, with unemployment remaining stubbornly high, although signs of recovery began to emerge in late 2012, and certainly in 2013. The Federal Reserve—the U.S. central banking system—took unprecedented, proactive steps to encourage an economic turnaround. And President Barack Obama spearheaded passage of a massive economic stimulus package, designed not only to create jobs but also to build infrastructure—with a focus on renewable energy—to position the U.S. economy for stability and growth in the decades to come. (The price, of course, was more national debt, which will ultimately counterbalance some of the benefits.) Although the U.S. economic recovery continued through 2015, the entire world economy began to stagger in early 2016 as economic instability in China caused frightening ripples around the globe.

The government also takes active steps on an ongoing basis to reduce the risks of starting and running a business. The result: free enterprise and fair competition flourish. Despite the economic crisis, research suggests that most budding entrepreneurs still plan to launch their firms in the next three years. One government policy that supports business is the relatively low federal tax rate, both for individuals and businesses. A number of states—from Alabama to Nevada—make their local economies even more appealing by providing special tax deals to attract new firms. The federal government also runs entire agencies that support business, such as the Small Business Administration. Other branches of the government, such as the Federal Trade Commission, actively promote fair competitive practices, which help give every enterprise a chance to succeed.

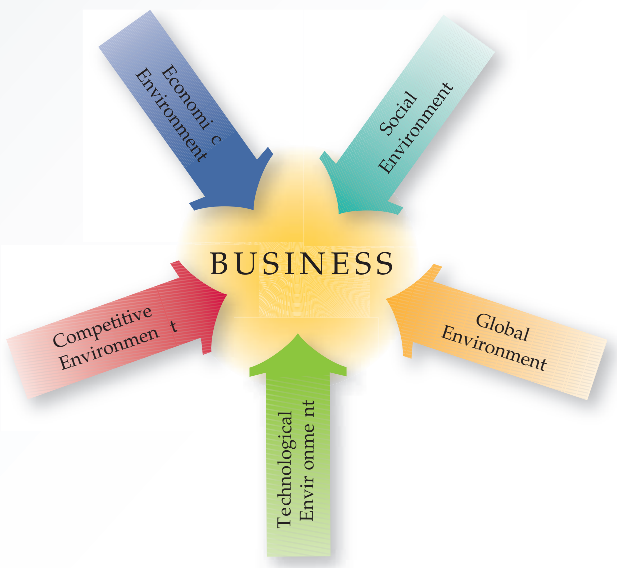
Another key element of the U.S. economic environment is legislation that supports enforceable contracts. For instance, if you contract a baker to supply your health food company with 10,000 pounds of raw kale chips at $1.00 per pound, that firm must comply or face legal consequences. The firm can't wait until a day before delivery and jack up the price to $10.00 per pound because you would almost certainly respond with a successful lawsuit. Many U.S. businesspeople take enforceable contracts for granted, but in a number of developing countries—which offer some of today's largest business opportunities—contracts are often not enforceable (at least not in day-to-day practice).

Corruption also affects the economic environment. A low level of corruption and bribery dramatically reduces the risks of running a business by ensuring that everyone plays by the same set of rules—rules that are

> "A banker is a fellow who lends you his umbrella when the sun is shining, but wants it back the minute it begins to rain."
>
> —MARK TWAIN, AMERICAN AUTHOR

Exhibit 1.1

The Business Environment



Each dimension of the business environment affects both individual businesses and the economy in general.

clearly visible to every player. Fortunately, U.S. laws keep domestic corruption mostly—but not completely—at bay. Other ethical lapses, such as shady accounting, can also increase the cost of doing business for everyone involved. But in the wake of corporate ethical meltdowns such as Enron, the federal government has passed tough-minded new regulations to increase corporate accountability. If the new legislation effectively curbs illegal and unethical practices, every business will have a fair chance at success.

Upcoming chapters on economics and ethics will address these economic challenges and their significance in more depth. But bottom line, we have reason for cautious (some would say very cautious) optimism. The American economy has a proven track record of flexibility and resilience, which will surely help us navigate this crisis and uncover new opportunities.

1-5b The Competitive Environment

As global competition intensifies yet further, leading-edge companies have focused on customer satisfaction like never before. The goal: to develop long-term, mutually beneficial relationships with customers. Getting current customers to buy more of your product is a lot less expensive than convincing potential customers to try your product for the first time. And if you transform your current customers into loyal advocates—vocal promoters of your product or service—they'll get those new customers for you more effectively than any advertising or discount program. Companies such as Amazon, Coca-Cola, and Northwestern Mutual life insurance lead their industries in customer satisfaction, which translates into higher profits even when the competition is tough.[13]

Customer satisfaction comes in large part from delivering unsurpassed value. The best measure of value is the size of the gap between product benefits and price. A product has value when its benefits to the customer are equal to or greater than the price that the customer pays. Keep in mind that the cheapest product doesn't necessarily represent the best value. If a 99-cent toy from Big Lots breaks in a day, customers may be willing to pay several dollars more for a similar toy from somewhere else. But if that 99-cent toy lasts all year, customers will be delighted by the value and will likely encourage their friends and family to shop at Big Lots. The key to value is quality, and virtually all successful firms offer top-quality products relative to their direct competitors.

speed-to-market The rate at which a new product moves from conception to commercialization.

A recent ranking study by consulting firm Interbrand highlights brands that use imagination and innovation to deliver value to their customers. Exhibit 1.2 shows the winners and the up-and-comers in the race to capture the hearts, minds, and dollars of consumers around the world.

EXHIBIT 1.2 2016 GLOBAL BRAND CHAMPIONS AND THE ONES TO WATCH, INTERBRAND

Most Valuable	Biggest Gainer	Percentage Growth
Apple	Facebook	+48%
Google	Amazon	+33%
Coca-Cola	Lego	+25%
Microsoft	Nissan	+22%
Toyota	Adobe	+21%
IBM	Starbucks	+20%
Samsung	Zara	+19%
Amazon	Mercedes-Benz	+18%
Mercedes-Benz	Porsche	+18%
GE	Hermes	+17%

Source: Best Global Brands 2016, Interbrand, http://interbrand.com/best-brands/best-global-brands/2016/ranking/, accessed January 23, 2017.

Leading Edge versus Bleeding Edge **Speed-to-market**—the rate at which a firm transforms concepts into actual products—can be another key source of competitive advantage. And the pace of change just keeps getting faster. In this tumultuous setting, companies that stay ahead of the pack often enjoy a distinct advantage. But keep in mind that there's a difference between leading edge and bleeding edge. Bleeding-edge firms launch products that fail because they're too far ahead of the market. During the late 1990s, for example, in the heart of the dot.com boom, Webvan, a grocery delivery service, launched to huge fanfare. But the firm went bankrupt just a few years later in 2001, partly because customers weren't yet ready to dump traditional grocery stores in favor of cyber-shopping. Leading-edge firms, on the other hand, offer products just as the market becomes ready to embrace them.[14]

Apple provides an excellent example of leading edge. You may be surprised to learn that Apple—which controls about 70%[15] of the digital music player market—did not offer the first MP3 player. Instead, it surveyed the existing market to help develop a new product, the iPod, which was far superior in terms of design and ease-of-use. But Apple didn't stop with one successful MP3 player. Racing

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Workforce Magazine named American Express as its top company for HR management in 2016. Google, Accenture, USAA, and AT&T rounded out the rest of the top five.

to stay ahead, they soon introduced the colorful, more affordable iPod mini. And before sales reached their peak, they launched the iPod Nano, which essentially pulled the rug from under the blockbuster iPod mini just a few short months before the holiday selling season. Why? If they hadn't done it, someone else may well have done it instead. And Apple is almost maniacally focused on maintaining its competitive lead.[16]

1-5c The Workforce Advantage

Employees can contribute another key dimension to a firm's competitive edge. Recent research suggests that investing in worker satisfaction yields tangible, bottom-line results. The researchers evaluated the stock price of *Fortune* magazine's annual list of the "100 Best Companies to Work for in America" to the S&P 500, which reflects the overall market. From 2009 to 2014, cumulative stock market returns for the "100 Best" were up +205%, compared to +121% for the S&P 500. On an annualized basis, this translates to a return of about +20.4% per year for the "100 Best," and about +14.1% per year for the S&P 500 over the same time period. While the critical difference in performance most likely stemmed from employee satisfaction, other factors—such as excellent product and superb top management—likely *also* played a role in both employee satisfaction and strong stock performance.[17]

Finding and holding the best talent will likely become a crucial competitive issue in the next decade as the baby boom generation begins to retire. The 500 largest U.S. companies anticipate losing about half of their senior managers over the next five to six years. Since January 1, 2011, approximately 10,000 baby boomers began to turn 65 (the traditional retirement age) every day, and the Pew Research Center anticipates that this trend will continue for 19 years. Replacing the skills and experience these workers bring to their jobs may be tough: baby boomers include about 77 million people, while the generation that follows includes only 46 million. Firms that cultivate human resources now will find themselves better able to compete as the market for top talent tightens.[18] However, job market contraction may not be an issue, because a growing number of baby boomers opt to either postpone retirement or continue working part-time during retirement, in the face of inadequate financial resources.

1-5d The Technological Environment

The broad definition of **business technology** includes any tools that businesses can use to become more efficient and effective. But more specifically, in today's world, business technology usually refers to computers, telecommunications, and other digital tools. Over the past few decades, the impact of digital technology on business has been utterly transformative. New industries have emerged, while others have disappeared. And some fields—such as travel, banking, and music—have changed dramatically. Even in categories with relatively

business technology Any tools—especially computers, telecommunications, and other digital products—that businesses can use to become more efficient and effective.

The Uber Syndrome

No doubt about it—senior executives make the most money in business. They also have the most to worry about, however. In a 2015 study of senior executives, one participant described her firm's biggest worry as "the 'Uber Syndrome'—where a competitor with a completely different business model enters your industry and flattens you." In today's tumultuous business world, this concern is completely understandable. Analyzing the research, *Fortune* magazine editor Geoff Colvin noticed that this year, for the first time, most business leaders expected new competitors to be outsiders. Business leaders know they must disrupt—or be disrupted. The solution to this impending threat, according to the small cohort of highly successful firms that the research dubs "torchbearers," seems to be to focus more on customers and less on competitors. When a disruptive player makes its move, loyal customers are less likely to defect and destroy your business.

According to a separate survey of CEOs released in 2016, the two largest concerns among chief executives around the world are the global economic environment and geopolitical tensions. The global economy is more integrated today than ever before, and a crisis within any major country can quickly spread around the world. We've seen this time and time again in recent years, from the Grecian debt crisis of 2009 to the Chinese stock market plunge of early 2016. Dennis Nally, global chairman of PwC Consultancy, explains why geopolitical tension is a threat to the global economy: "[If] you've got hot spots anywhere in the world, it creates instability . . . business leaders hate instability." The latest PwC survey of CEOs shows that among American CEOs in particular, there is widespread recognition that a strong corporate purpose is vital in the digital world. In addition, CEOs are focused on building stronger trust with employees and customers alike. So if your life goal is to reach the top rung at a major corporation, don't expect to leave your worries behind. It would seem that the higher you go, the more pressing the worries.[19]

unchanged products, companies have leveraged technology to streamline production and create new efficiencies. Examples include new processes such as computerized billing, digital animation, and robotic manufacturing. For fast-moving firms, the technological environment represents a rich source of competitive advantage, but it clearly can be a major threat for companies that are slow to adopt or to integrate new approaches.

The creation of the **World Wide Web** has transformed not only business but also people's lives. Anyone, anywhere, anytime can use the Web to send and receive images and data (as long as access is available). One result is the rise of **e-commerce** or online sales, which allow businesses to tap into a worldwide community of potential customers. In the wake of the global economic crisis, e-commerce has slowed from the breakneck 20%+ growth rates of the past five years, but even so, analysts predict that solid growth will continue. Business-to-business selling comprises the vast majority of total e-commerce sales (and an even larger share of the profits). A growing number of businesses have also connected their digital networks with suppliers and distributors to create a more seamless flow of goods and services.[20]

World Wide Web The service that allows computer users to easily access and share information on the Internet in the form of text, graphics, video, apps, and animation.

e-commerce Business transactions conducted online, typically via the Internet.

demographics The measurable characteristics of a population. Demographic factors include population size and density, as well as specific traits such as age, gender, and race.

Alternative selling strategies thrive on the Internet, giving rise to a more individualized buying experience. If you've browsed seller reviews on eBay or received shopping recommendations from Amazon, you'll have a sense of how personal web marketing can feel. Online technology also allows leading-edge firms to offer customized products at prices that are comparable to standardized products. On the Burton website, for instance, customers can "custom build" professional quality "Custom X" snowboards while sitting at home in their pajamas. Nike offers a similar service for NikeID shoes, clothing, and gear.

As technology continues to evolve at breakneck speed, the scope of change—both in everyday life and business operations—is almost unimaginable. In this environment, companies that welcome change and manage it well will clearly be the winners.

1-5e The Social Environment

The social environment embodies the values, attitudes, customs, and beliefs shared by groups of people. It also covers **demographics**, or the measurable characteristics of a population. Demographic factors include population size and density and specific traits such as age, gender, race, education, and income. Clearly, given all these influences, the social environment changes dramatically from country to country. And a nation as diverse as the United States features a number of different social environments. Rather than cover the

Do You Do It?

More than 1,000 times a minute, someone in America bites into a Jack in the Box taco—one of more than a million Jack in the Box tacos sold every day. With such numbers, you might think that Jack unearthed the secret to the perfect-tasting taco . . . but you'd be wrong. Jack's taco has been variously described by its fans as:

- **"a wet envelope of cat food"**
- **"vile and amazing"**
- **"disgusting and delectable"**
- **"repulsive and yet irresistible"**

So why does the Jack in the Box taco do so well? Food writer Sophie Egan offers three possible reasons. First, it's cheap. At two for $.99 it's a real deal. Second, it's fried. As much as we like the idea of fruits and vegetables—fried stuff tastes good! Finally, it's a metaphorical flip of the bird to the "food police," who many believe are attempting to exert too much control over our rights to eat whatever we please.[21]

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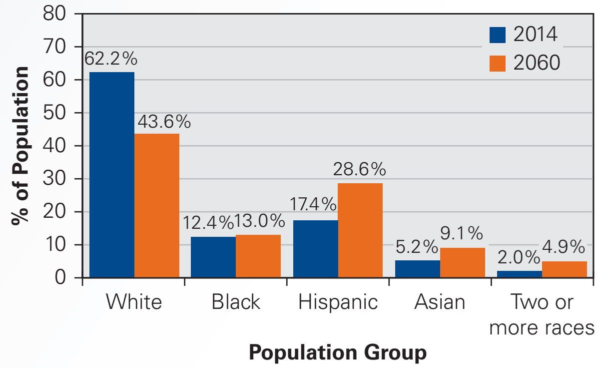
full spectrum, this section focuses on the broad social trends that have the strongest impact on American business. Understanding the various dimensions of the social environment is crucial since successful businesses must offer goods and services that respond to it.

Diversity While the American population has always included an array of different cultures, the United States has become more ethnically diverse in recent years. Caucasians continue to represent the largest chunk of the population at 63%, but according to the director of the U.S. Census Bureau, "The next half century marks a turning point in continuing trends—the U.S. will become a plurality nation, where the non-Hispanic white population remains the largest single group, but no group is in the majority." This will probably happen in about 2043. The Hispanic and Asian populations will probably continue to grow faster than any other ethnic groups. By 2060, nearly one in three U.S. residents will be Hispanic, up from about one in six today. This will happen even though the overwhelming wave of immigration from Mexico to the United States has stalled and even begun to reverse in the past few years; nevertheless, among Mexican-born people worldwide, one in ten currently lives in the United States.[22] Exhibit 1.3 demonstrates the shifting population breakdown.

But the national statistics are somewhat misleading, since ethnic groups tend to cluster together. African Americans, for example, currently comprise about 37% of the Mississippi population, Asians comprise about 39% of the Hawaii population, and Hispanics comprise about 47% of the New Mexico population.[23]

So what does this mean for business? Growing ethnic populations offer robust profit potential for firms that pursue them. For instance, a number of major brands such as Coca-Cola, General Mills, Ford, Nestlé, Purina, and Walmart have invested heavily in the Hispanic market over the past five years. Recognizing the potential of the Hispanic market, Japanese automakers have begun actively targeting Latino customers. Because of these efforts, Hispanic customers are reportedly 15% more likely than any other group to buy a Japanese-made car. Toyota,

Exhibit 1.3
U.S. Population Estimates



Source: Projections of the Size and Composition of the U.S. Population: 2014 to 2060, U.S. Census Bureau, March 2015, https://www.census.gov/content/dam/Census/library/publications/2015/demo /p25-1143 .pdf, accessed May 9, 2016.

in particular, has been the top-selling brand among Latinos for more than ten years thanks to its highly targeted marketing. Targeting an ethnic market can also yield remarkable results for products that cross over into mainstream culture. Music mogul and entrepreneur Russell Simmons, for example, initially targeted his music and clothing to the African American market, but his success quickly spilled over to mainstream culture, helping him build a hip-hop empire.[24]

Growing diversity also affects the workforce. A diverse staff—one that reflects an increasingly diverse marketplace—can yield a powerful competitive advantage in terms of both innovation and ability to reach a broad customer base. From global behemoths, such as Coca-Cola and Verizon, to local corner stores, companies have taken proactive steps to hire and nurture people from a broad range of backgrounds. And that doesn't just reflect racial or ethnic roots. True diversity also includes differences in gender, age, religion, and nationality, among other areas. Leading-edge firms have also taken proactive steps to train their entire workforce to manage diversity for top performance.[25]

Effectively managing diversity should only become easier as time goes by. Multiple studies demonstrate that young American adults are the most tolerant age group, and they are moving in a more tolerant direction than earlier generations regarding racial differences, immigrants, and homosexuality. As this generation gathers influence and experience in the workforce, they are likely to leverage diversity in their organizations to hone their edge in a fiercely competitive marketplace.[26]

Aging Population As life spans increase and birthrates decrease, the American population is rapidly aging. The U.S. Census Bureau projects that the nation's population age 65 and older will more than double between 2005 and 2060. By 2060, older Americans will represent just over one in five residents, up from one in seven today. Also, the number of working-age Americans will shrink from 63% to 57% of the population, dramatically increasing the number of people who are depending on each working American. And the United States isn't alone in this trend. The population is aging across the developed world, from Western Europe to Japan. China faces the same issue, magnified by its huge population. Demographers estimate that in the next 20 years the number of people in China over the age of 60 will double, leading to a nation where the retired will outnumber the entire population of Western Europe. There are currently six workers to every retiree, but China's one-child policy suggests that the number of people providing for the old will rapidly collapse.[27]

The rapidly aging population brings opportunities and threats for business. Companies in fields that cater to the elderly—such as healthcare, pharmaceuticals, travel, recreation, and financial management—will clearly boom. But creative companies in other fields will capitalize on the trend as well by reimagining their current products to serve older clients. Possibilities include books and movies—maybe even video games—with mature characters; low-impact fitness programs such as water aerobics; and cell phones and PDAs with more readable screens. Again, the potential payoff of age diversity is clear: companies with older employees are more likely to find innovative ways to reach the aging consumer market.

But the larger numbers of retired people also pose significant threats to overall business success. With a smaller labor pool, companies will need to compete even harder for top talent, driving up recruitment and payroll costs. As state and federal governments stretch to serve the aging population, taxes may increase, putting an additional burden on business. And as mid-career workers spend more on elder care, they may find themselves with less to spend on other goods and services, shrinking the size of the consumer market.

Rising Worker Expectations Workers of all ages continue to seek flexibility from their employers. Moreover, following massive corporate layoffs in the early 2000s, employees are much less apt to be loyal to their firms. A study released in 2013 showed that on average, employees in Fortune 500 firms have a median tenure of only 3.68 years. As young people today enter the workforce, they bring higher expectations for their employers in terms of salary, job responsibility, and flexibility—and less willingness to pay dues by working extra-long hours or doing a high volume of "grunt work." Smart firms are responding to the change in worker expectations by forging a new partnership with their employees. The goal is a greater level of mutual respect through open communication, information sharing, and training. And the not-so-hidden agenda, of course, is stronger long-term performance.[28]

> In Asia, the average person's living standards are currently set to rise by 10,000% in one lifetime!
>
> —NEWSWEEK