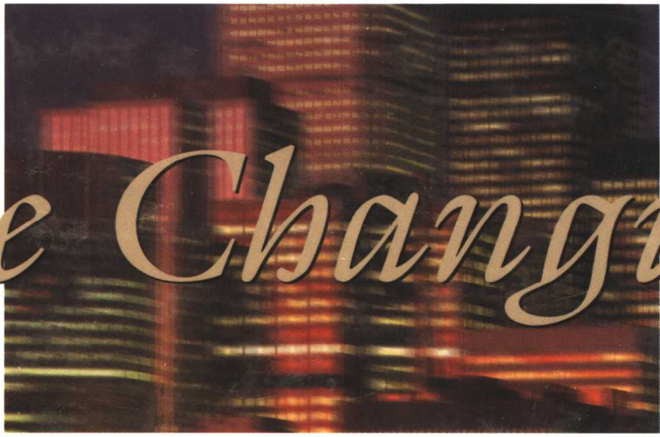

The Changing

4TH EDITION

Environment

GROVER STARLING

# of Business

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GROVER STARLING
University of Houston–Clear Lake

of Business

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Preface

Once, a long time ago, Adam must have said, "Eve, we're living in an age of transition." Change certainly has been the norm in the last few decades, even though each generation thinks its period of change unique. Nevertheless, I must say that as students of business, we are fortunate to live in a time when almost every aspect of the business environment brims with new insights, challenges, and discoveries. I feel privileged to be able to introduce this subject and to convey some of the excitement of these times.

Quite a few studies of business–society interrelations now exist. It has not been my purpose merely to add one to their number. My purpose is to exhibit the business environment as an integral part of business administration; not as isolated speculations and facts, but as a coherent body of knowledge and a set of managerial skills essential to the well-run organization. This purpose demands a more thorough account of the larger environment of business than is usually given.

It is not a good strategy to focus exclusively on public policy for the simple reason that trends in the social, political, economic, technological, and international environments profoundly shape the policymaking process. Without some knowledge of these environments, managers can hardly understand public policy except in the most superficial sense, and those who seek to *anticipate* change in public policy will find themselves at a serious disadvantage. An only slightly better approach is focus on social issues. The problem here, simply put, is that the issues change. Only some of the issues that are "hot" this year will still be critical in 5 or 10 years. And who knows what new issues will emerge? While we cannot afford to neglect current public policies and social issues, we must also be aware of the dynamics of change and have a general framework for coping with new policies and issues.

The fourth edition of this book is by far the most extensive revision yet. The entire book was reconsidered, sentence by sentence, then rewritten to a large extent, and finally, to some degree, reorganized. The same questions had to be answered in writing all editions: How does one accurately characterize business–society relations? What do students *have* to know? (One need not know about source-drain spacing in MOS transistors to grasp what is at stake in the semiconductor technology competition between the United States and Japan.) What should they remember ten years from now? What will still be true ten years from now? As suggested above, one of the biggest mistakes we can make as scholars or managers is to assume that trends continue.

As for the book as a whole, I will forego a chapter-by-chapter description because Chapter 1 provides a more adequate overview than I could ever squeeze into a preface. But among the many new additions in this edition, we might note these:

- New cases dealing with specific situations, specific problems, and specific decisions at the end of every chapter.
- Greater attention throughout to the problem of organizational effectiveness (as opposed to organizational efficiency).
- An analysis of the various ways in which managers perceive their environments and how this affects their strategies for dealing with government and other external organizations and groups. (Chapter 1)
- A review of a dozen "killer technologies" which have the potential for destroying certain companies or industries. (Chapter 2)
- Greater emphasis on the relationship between ecology and economics. (Chapter 3)
- A framework for making sense of economic news. (Chapter 3)
- An overview of non-intuitive strategies effective executives have used during economic downturns. (Chapter 3)
- An environmental scan of demographic, institutional, and cultural trends in the United States. (Chapter 4)
- A synthesis of the best recent theories of the policy making process. (Chapter 5)
- Expanded discussion of business law (contracts, torts, etc.) and alternative dispute resolution methods. (Chapters 5, 6, and 14)
- A concise discussion of 25 public policies that every manager better know about. (Chapter 7)
- A critical analysis of the "regulatory weapons" available to government. (Chapter 8)
- A comprehensive model of how companies can decide to enter, or not enter, the new international environment. (Chapter 9)
- Greater attention to the ethical dilemmas a manager faces and an expanded discussion of Aristotle's virtue-based approach to ethics. (Chapter 10)
- A framework by which non technical managers can make decisions about equipment and process technology. (Chapter 11)
- Action planning for nonmarket activities. (Chapter 12)
- An inventory of corporate political strategies. (Chapter 13)
- Techniques for testifying with impact. (Chapter 14)
- A discussion of how capitalism seems to be evolving and what the managerial implications of this transformation are likely to be. (Chapter 15)

Business and society courses range from fast-paced surveys to more intensive treatments and, of course, the interests of instructors and students vary widely from course of course. This textbook has been carefully designed to meet all situations. Some materials have been put in chapter supplements or in specially designed boxed inserts. These will appeal to both curious students and to the instructors of demanding courses who want to survey thoroughly the entire field.

Courses based on some of the material treated in this book are rarely found in either MBA or undergraduate business programs—for example, the logic of design, the social construction of reality, the political economy of Japan, and the productivity of knowledge. Some of the book's topics are included in economic courses—rent seeking, moral hazards, Coase's Theorem, and "Tobin's *q*." Seldom, however, are these treated in a unified and systematic way with the other major issues of a business and society course. This is, I believe, the first attempt to adopt a thoroughgoing interdisciplinary point of view and to use the powerful insights of rigorous, relevant theory about politics, economics, technological innovation, ethics, human behavior, and history to derive the underlying principles that are at work in the external environment of business.

The most important feature of this edition is its emphasis on the skills required for effectively *managing* business–society interrelations. Where possible, I have encouraged the reader to think in terms of personal involvement. The cases and exercises at the end of each chapter are designed to show how the material in the chapter can be applied. The goal has been to make the subject of business and society, of business *within* society more coherent and more relevant to business administration—but not more difficult.

Sometimes I think that the most difficult question that an author can be asked is, "What's your book about?" It is a fair question and one to which only recently have I found the answer. In the final analysis, *The Changing Environment of Business* is not really about business, government, and society—it is about leadership. A sense of the future is a key element of leadership, a means of inspiring the organization. Like the person in the bow of a sailboat, managers should be the first to see what is ahead. This book, if it does anything, tries to show managers how they can use this leadership tool more effectively.

Once again, I have had the benefit of productive (and I hope *mutually* beneficial) relationships with reviewers, editors, colleagues, and consultants. In addition, I wish to thank the following individuals who were kind enough to comment on and make valuable suggestions concerning the fourth edition of *The Changing Environment of Business:* Robert Dolan, David M. Flynn, George J. Gore, D. Jeffrey Lenn, and Kathleen Rehbein. I would also like to thank all those who reviewed earlier editions of the book: Lathef N. Ahmad, Roland F. Aubin, Paul Bernstein, Guy Black, Dharma deSilva, G. Dale Meyer, Ian Maitland, Howard E. Reed, Raymond W. Vegso, Jim Weber, James M. Owens, John T. Redington, and Patrick A. Taylor.

Finally, I owe a word of explanation and apology to those who specialize in any part of this enormous subject. I have no doubt that most topics I have discussed, with one or two exceptions, are better known by the experts in the field than by me. It is obviously impossible to know as much about each topic as a specialist in that topic will know. If, however, this were considered a sufficient reason for respectful silence, then it would follow that no solitary writer should ever undertake to examine more than some small facet of the vast interaction between business and society. In that case, no overview would ever be provided to students in the field.

GROVER STARLING

Contents

. . . antes los hombres podían dividirse, sencillamente, en sabios e ignorantes, en más o menos sabios y más o menos ignorantes. Pero el especialista no puede ser subsumido bajo ninguna de esas dos categorías. No es un sabio, porque ignora formalmente cuanto no entra en su especialidad; pero tampoco es un ignorante, porque es "un hombre de ciencia" y conoce muy bien su porciúncula del universo. Habremos de decir que es un sabio-ignorante, cosa sobremanera grave, pues significa que es un señor el cual se comportará en todas las cuestiones que ignora, no como un ignorante, sino con toda la petulancia de quien en su cuestión especial es un sabio.

[. . . previously, men could be divided simply into the learned and the ignorant, those more or less the one, and those more or less the other. But your specialist cannot be brought in under either of these two categories. He is not learned, for he is formally ignorant of all that does not enter into his speciality; but neither is he ignorant, because he is "a scientist," and "knows" very well his own tiny portion of the universe. We shall have to say that he is a learned ignoramus, which is a very serious matter, as it implies that he is a person who is ignorant, not in the fashion of the ignorant man, but with all the petulance of one who is learned in his own special line.]

—*José Ortega y Gasset,* La Rebellion de las Masas
[The Revolt of the Masses]

In my company's American subsidiary, the American managers are so committed to working long hours at operating problems in business that they have no time to broaden their perspectives. They don't read; rarely keep up with the news from abroad. They have no context of general knowledge about the world in which to contribute to broad business decisions.

—*A German manager, after four years of assignments in the United States, quoted in D. Quinn Mills,* The New Competitors *(Wiley, 1985)*

1

Introduction

It is not the lofty sails but the unseen wind that moves the ship.
—W. MacNeile Dixon

It is change, continuing change, inevitable change, that is the dominant factor in society today. No sensible decision can be made any longer without taking into account not only the world as it is, but the world as it will be.
—Isaac Asimov

This book is about how the external environment affects and constrains organizations and how organizations respond to these pressures. It is also a guide to designing and managing business enterprises in a period of rapid, turbulent change.

No metaphor better explains what is happening in the world of business today than Dixon's opening quote. Management textbooks and training programs focus on the "sails" of management—that is, marketing, control, finance, and the rest. Important as these functions are, they are not the "unseen wind" that really moves business enterprises in fresh directions. If management today seems difficult, it is because virtually all of a manager's time is spent tending to the sails with too little time devoted to considering shifts in the wind, that is, the external environment.

The purpose of this introductory chapter is to lay some groundwork for our analysis. The first section will discuss a pair of problems that you may not have given much thought to: **organizational effectiveness** (as opposed to organizational efficiency) and **managerial obsolescence.** In a very real sense, this book is an extended inquiry into what can be done about these two problems.

In the second section, we will begin, in a preliminary sort of way, to sketch an answer to that question by offering an overview of the concept of the macroenvironment and distinguishing it from the immediate or market environment of business.

In the third section, we will turn from considering how the macroenvironment affects business to how business affects the society within which it is embedded.

A. CENTRAL CONCERNS OF THIS BOOK

Organizational Effectiveness

Most books about organizations acknowledge the importance of the external environment, but the acknowledgment usually comes early and ends quickly. Then begins pursuit of the real quarry: how to achieve greater **efficiency** within the organization. Indeed, the central question driving most theory building about organizational structure and behavior is: How can organizations achieve a better ratio of output to input? Motivate workers to produce more goods in the same number of hours and at the same wage rate, and you have increased efficiency. Slash operating expenses while maintaining the same level of output, and again you have increased efficiency.

But efficiency is essentially an *internal* standard of performance, involving how one deploys a given set of resources within an organization. It is a necessary but not a sufficient condition for ensuring a business organization's survival—a point often missed by even experienced executives.

The late Edward Deming, the world famous authority on quality control, recalled a conversation he had with such an executive. The executive was very excited about the state-of-the-art automation that his plant had installed and expressed his disappointment that Deming would be unable to visit it. Deming's response was terse:

> Have you ever heard of a plant that closed? Why did it close? Poor workmanship? Low productivity? Mistakes? Faults? Never! It closed because it was producing the wrong product. One that has no market. Not enough market. ***Management didn't look ahead.*** (*Wall Street Journal*, June 4, 1990. Emphasis added.)

Toward a Definition. Clearly, organizations also need an external standard—a standard that involves more than just doing better what the organization already does. Pfeffer and Salancik (1978) argue that **effectiveness** should be that standard. Like efficiency, effectiveness means producing or capable of producing results. But the two terms are not freely interchangeable in idiomatic use. As previously indicated, efficiency suggests operating in such a manner as to minimize the loss or waste of resources in producing an output. Effectiveness, on the other hand, emphasizes the actual production of acceptable outcomes and actions. For an organization, "acceptable outcomes and actions" must be those that meet the demands and expectations of groups, organizations, and individuals outside the organization that are affected by its decisions, policies, and operations.

The members of these groups, which we call **stakeholders,** include not only the obvious ones like employees, customers, shareholders, creditors, suppliers, competitors, wholesalers, and retailers. In recent years, businesses increasingly have had to factor into their decision making the possible reactions of local communities, social activists, media, trade associations, governments, and the general public.

Thus, effectiveness requires a keen awareness of who these groups are, how powerful they are, how they are interrelated, and how to deal with them. Consider the case of the company Burroughs Wellcome. In 1987, just three years after scientists learned what caused AIDS, the company won approval for AZT—the first drug authorized for use against the disease. Burroughs pushed AZT from the laboratory to the marketplace in a fraction of the usual time. Despite this remarkable innovation, Burroughs proved ill-prepared for the explosive emotions and rough politics surrounding AIDS. The company's decision to charge an expensive price for AZT was entirely rational from a purely economic perspective. As pharmaceutical companies normally do, it wanted to cover the cost of developing the drug and recoup losses for other research that had failed to produce profitable products. But given the stakeholders in this decision, Burroughs probably made the wrong decision. Within days of the price announcement, Congress was investigating and angry demonstrators were appearing on the evening news. An *effective* drug company would likely have handled the pricing decision differently.

A Matter of Survival. Before turning to the other central concerns of this book, let us clarify an earlier statement, "Efficiency is a necessary but not a sufficient condition for ensuring a business organization's survival." It is a matter for astonishment, when one comes to think of it, how little books on business talk about survival. Apparently, it is taken for granted. Yet, the cold fact is that a typical U.S. company has about a one in a one hundred chance of not surviving through the year (Table 1.1). If a physician gave us those kinds of odds, we would be inclined to worry. One might object that these fatalities are concentrated among puny mom-and-pop enterprises; big, robust companies need not worry. Not so. The number of U.S. manufacturing firms with sales of more than $10 million was 1,928 in 1977; nearly 1,200 of these had disappeared by 1989 (Taylor, 1992).

Table 1.1 **Business Failure Rates by Industry in United States**

INDUSTRY	RATE PER 10,000 FIRMS				
	1985	1990	1991	1992	1993 prel.
Total	**115**	**74**	**107**	**109**	**90**
Agriculture, forestry, fishing	197	50	65	80	63
Mining	193	88	95	99	72
Construction	109	91	128	129	109
Manufacturing	119	92	127	131	114
Transportation, public utilities	151	94	134	126	75
Wholesale trade	102	77	109	113	99
Retail trade	109	65	90	76	62
Finance, insurance, real estate	62	60	90	87	67
Services	115	49	87	93	71

Source: Adapted from *Statistical Abstract of the United States,* 1994, p. 548.

Part of this change was of course driven by the 1980s fad of financial engineering—mergers, acquisitions, divestitures, firms going public, firms going private, and so on. But the more durable forces of technological change and intensifying international competition were also at work.

Once these now departed companies were in a crisis, the need for change was probably obvious to everyone. The only problem was that by then, it was too late. The companies had little time and few options. So, the challenge is to recognize and react to external change as early as possible. That is what effective companies do.

Small businesses, which create the majority of new jobs, are also responsible for most of the jobs that are lost because 60 to 80 percent fail within five years of starting up. But it should be emphasized that *all* companies are mortal, and most have not been around as long as you think. At about $22 billion, the market value of Microsoft, a 17-year-old computer software company, is now as great as that of General Motors, the world's biggest manufacturer. GM is still big, but no longer quite so mighty. Many investors are betting that it is Microsoft, not the vast manufacturing empire of GM, that has the best chance of surviving into the next century.

To be sure, big companies like GM, IBM, and Sears appear solid and permanent—sort of like the Rockies. But the most remarkable things about big companies is not their longevity but their transience. Of the 100 firms heading *Fortune*'s first list of America's 500 biggest companies, published in 1956, only 29 can still be found in the top 100. (*Fortune,* April 4, 1992) Thus, within the span of one working life, over two-thirds of the biggest U.S. companies were pushed out of the way by faster-growing ones. Many lost their place after being acquired; some simply fell behind; others disappeared altogether.

The disconcerting truth is that, in business, past success counts for little. A new technology can rapidly shift the ground beneath the best-known and most respected firm. A change in demographics or values in a society can cause the decline and fall of a corporate empire. And governments everywhere shred presumptions of invincibility:

- The business of making small airplanes is all but dead in the United States, wiped out mainly by product-liability lawsuits.
- A federal judge overturned in 1991 Exxon's plea bargain with the United States partly because of all the letters he got saying Exxon should suffer more for the Valdez oil spill. Judge Holland's comments from the bench should send a chill through every corporate executive: "I'm afraid these fines send the wrong message, suggesting that spills are a cost of doing business *that can be absorbed*" (*The Wall Street Journal,* May 2, 1992. Emphasis added). Apparently, this means that the law requires the accidents result in *unabsorbable* fines.
- Banks must battle Congressional attempts to limit the interest rates they charge on credit cards, one of their most profitable businesses. In the background of the political battling is a longstanding hostility toward banks in the United States. As one banking analyst explains it: "Banks have histori-