MODULE : 5

SOCIO-POLITICAL-ECONOMIC ENVIRONMENT

Economic systems

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

An economic system is a type of social system. The mode of production is a related concept. All economic systems must confront and solve the three fundamental economic problems:

- What kinds and quantities of goods shall be produced?
- How goods shall be produced.
- How the output will be distributed.

Types of Economic Systems

There are many types of economies around the world. Each has its own distinguishing characteristics, although they all share some basic features. Each economy functions based on a unique set of conditions and assumptions. Economic systems can be categorized into four main types: traditional economies, command economies, mixed economies, and market economies.

1. Traditional economic system

The traditional economic system is based on goods, services, and work, all of which follow certain established trends. It relies a lot on people, and there is very little division of labor or specialization. In essence, the traditional economy is very basic and the most ancient of the four types.

Some parts of the world still function with a traditional economic system. It is commonly found in rural settings in second and third world nations, where economic activities are predominantly farming or other traditional income-generating activities.

There are usually very few resources to share in communities with traditional economic systems. Either few resources occur naturally in the region or access to them is restricted in some way. Thus, the traditional system, unlike the other three, lacks the potential to generate a surplus. Nevertheless, precisely because of its primitive nature, the traditional economic system is highly sustainable. In addition, due to its small output, there is very little wastage compared to the other three systems.

2. Command economic system

In a command system, there is a dominant centralized authority – usually the government – that controls a significant portion of the economic structure. Also known as a planned system, the command economic system is common in communist societies since production decisions are the preserve of the government.

If an economy enjoys access to many resources, chances are that it may lean towards a command economic structure. In such a case, the government comes in and exercises control over the resources. Ideally, centralized control covers valuable resources such as gold or oil. The people regulate other less important sectors of the economy, such as agriculture.

In theory, the command system works very well as long as the central authority exercises control with the general population's best interests in mind. However, that rarely seems to be the case. Command economies are rigid compared to other systems. They react slowly to change because power is centralized. That makes them vulnerable to economic crises or emergencies, as they cannot quickly adjust to changing conditions.

3. Market economic system

Market economic systems are based on the concept of free markets. In other words, there is very little government interference. The government exercises little control over resources, and it does not interfere with important segments of the economy. Instead, regulation comes from the people and the relationship between supply and demand.

Financial System

A financial system is a set of institutions, such as banks, insurance companies, and stock exchanges that permit the exchange of funds. Financial systems exist on firm, regional, and global levels. Borrowers, lenders, and investors exchange current funds to finance projects, either for consumption or productive investments, and to pursue a return on their financial assets. The financial system also includes sets of rules and practices that borrowers and lenders use to decide which projects get financed, who finances projects, and terms of financial deals.

- ❑ A financial system is the set of global, regional, or firm-specific institutions and practices used to facilitate the exchange of funds.
- ❑ Financial systems can be organized using market principles, central planning, or a hybrid of both.
- ❑ Institutions within a financial system include everything from banks to stock exchanges and government treasuries.

Roles of financial system in the economic development of a country

1. **Savings-investment relationship**
   To attain economic development, a country needs more investment and production. This can happen only when there is a facility for savings. As, such savings are channelized to productive resources in the form of investment. Here, the role of financial institutions is important, since they induce the public to save by offering attractive interest rates. These savings are channelized by lending to various business concerns which are involved in production and distribution.
2. **Financial systems help in growth of capital market**
   Any business requires two types of capital namely, fixed capital and working capital. Fixed capital is used for investment in fixed assets, like plant and machinery. While working capital is used for the day-to-day running of business. It is also used for purchase of raw materials and converting them into finished products.
   - **Fixed capital** is raised through capital market by the issue of debentures and shares. Public and other financial institutions invest in them in order to get a good return with minimized risks.
   - For **working capital**, we have money market, where short-term loans could be raised by the businessmen through the issue of various credit instruments such as bills, promissory notes, etc.

   Foreign exchange market enables exporters and importers to receive and raise funds for settling transactions. It also enables banks to borrow from and lend to different types of customers in various foreign currencies. The market also provides opportunities for the banks to invest their short term idle funds to earn profits. Even governments are benefited as they can meet their foreign exchange requirements through this market.

3. **Government Securities market**
   Financial system enables the state and central governments to raise both short-term and long-term funds through the issue of bills and bonds which carry attractive rates of interest along with tax concessions. The budgetary gap is filled only with the help of government securities market. Thus, the capital market, money market along with foreign exchange market and government securities market enable businessmen, industrialists as well as governments to meet their credit requirements. In this way, the development of the economy is ensured by the financial system.
4. **Financial system helps in Infrastructure and Growth**
   Economic development of any country depends on the infrastructure facility available in the country. In the absence of key industries like coal, power and oil, development of other industries will be hampered. It is here that the financial services play a crucial role by providing funds for the growth of infrastructure industries. Private sector will find it difficult to raise the huge capital needed for setting up infrastructure industries. For a long time, infrastructure industries were started only by the government in India. But now, with the policy of economic liberalization, more private sector industries have come forward to start infrastructure industry. The Development Banks and the Merchant banks help in raising capital for these industries.
5. **Financial system helps in development of Trade**
   The financial system helps in the promotion of both domestic and foreign trade. The financial institutions finance traders and the financial market helps in discounting financial instruments such as bills. Foreign trade is promoted due to per-shipment and post-shipment finance by commercial banks. They also issue Letter of Credit in favor of the importer. Thus, the precious foreign exchange is earned by the country because of the presence of financial system. The best part of the financial system is that the seller or the buyer do not meet each other and the documents are negotiated through the bank. In this manner, the financial system not only helps the traders but also various financial institutions. Some of the capital goods are sold through hire purchase and installment system, both in the domestic and foreign trade. As a result of all these, the growth of the country is speeded up.
6. **Employment Growth is boosted by financial system**
   The presence of financial system will generate more employment opportunities in the country. The money market which is a part of financial system, provides working capital to the businessmen and manufacturers due to which production increases, resulting in generating more employment opportunities. With competition picking up in various sectors, the service sector such as sales, marketing, advertisement, etc., also pick up, leading to more employment opportunities. Various financial services such as leasing, factoring, merchant banking, etc., will also generate more employment. The growth of trade in the country also induces employment opportunities.
7. **Financial system ensures balanced growth**
   Economic development requires a balanced growth which means growth in all the sectors simultaneously. Primary sector, secondary sector and tertiary sector require adequate funds for their growth. The financial system in the country will be geared up by the authorities in such a way that the available funds will be distributed to all the sectors in such a manner, that there will be a balanced growth in industries, agriculture and service sectors.

8. **Role of financial system in attracting foreign capital**
   Financial system promotes capital market. A dynamic capital market is capable of attracting funds both from domestic and abroad. With more capital, investment will expand and this will speed up the economic development of a country.
9. **Role of financial system in Political stability**
   The political conditions in all the countries with a developed financial system will be stable. Unstable political environment will not only affect their financial system but also their economic development.
10. **Financial system role in Electronic development:**
    Due to the development of technology and the introduction of computers in the financial system, the transactions have increased manifold bringing in changes for the all-round development of the country. The promotion of World Trade Organization (WTO) has further improved international trade and the financial system in all its member countries.

Macroeconomics

Macroeconomics is a branch of economics that studies how an overall economy—the market or other systems that operate on a large scale—behaves. Macroeconomics studies economy-wide phenomena such as inflation, price levels, rate of economic growth, national income, gross domestic product (GDP), and changes in unemployment.

- Macroeconomics is the branch of economics that deals with the structure, performance, behavior, and decision-making of the whole, or aggregate, economy.
- The two main areas of macroeconomic research are long-term economic growth and shorter-term business cycles.
- In contrast to macroeconomics, microeconomics is more focused on the influences on and choices made by individual actors in the economy (people, companies, industries, etc.).

There are two sides to the study of economics: macroeconomics and microeconomics. As the term implies, macroeconomics looks at the overall, big-picture scenario of the economy. Put simply, it focuses on the way the economy performs as a whole and then analyzes how different sectors of the economy relate to one another to understand how the aggregate functions. This includes looking at variables like unemployment, GDP, and inflation. Macroeconomists develop models explaining relationships between these factors. Such macroeconomic models, and the forecasts they produce, are used by government entities to aid in the construction and evaluation of economic, monetary, and fiscal policy; by businesses to set strategy in domestic and global markets; and by investors to predict and plan for movements in various asset classes.

Constitutional Provisions

In the Indian Constitution, the provisions regarding the freedom of trade, commerce and intercourse were adopted from the Constitution of Australia. According to Section 92 of the Australian Constitution, there should be freedom of trade, commerce and intercourse which may be carried out by ocean navigation or internal carriage.

While India had borrowed this provision, it also made sure to include the provision that the free flow of goods is allowed not only between different States but also within a State as well. Thus, in the Indian Constitution Inter-State trade as well as Intra-State trade is allowed in the country

Freedom of Trade

Article 301 of the Indian Constitution provides that the trade, commerce and intercourse in the country should be free throughout the country.

In commerce, the focus is more towards the element of transmission of goods as well as that of men and animals.

The three main words used in this article are:

1. **Trade: -** Trade means buying and selling of goods for profit-making purposes. Under Article 301, the word trade means an actual, organized & structured activity with a definite motive or purpose. For the motive of Article 301, the word trade is interchangeably used with business. In trade, goods and services are exchanged between the buyer and the seller and it also includes the transportation of these goods.
2. **Commerce: -** Commerce means transmission or movement by air, water, telephone, telegraph or any other medium; what is essential for commerce under Article 301 is transportation or transmission and not gain or profit.
3. **Intercourse: -** It means the movement of goods from one place to another. It includes both commercial and non-commercial movements and dealings. It would include travel and all forms of dealing with others. The word "intercourse" was included to remove any ambiguity about the intention of the Constitution makers and thus it has been used to express the intention that, free flow of goods throughout the country is part of the freedom under Article 301 of the Indian Constitution.

The use of the word 'free' in Article 301 does not mean freedom from laws and rules governing the country. There is a clear distinction between the laws obstructing freedom and laws containing rules and regulations for the proper conduction of trade activities in a smooth and easy manner.

Reasonable Restrictions

The fundamental rights guaranteed under the Constitution of India are non-absolute rights. This means that the extent to which these rights could be exercised may be limited by the State. This is where the concept of Reasonable Restrictions come in Article 19 of the constitution deals with freedoms and their respective grounds of restrictions.

Under Article 19(1), six freedoms have been laid down namely, freedom of speech and expression, freedom to assemble peacefully without arms, freedom to form associations and unions, freedom to move freely throughout the territory of India, freedom to reside and settle in any part of the territory in India, freedom to practice any profession or carry on any occupation, trade or business.

Corresponding to these freedoms, certain grounds have been mentioned under article 19(2) to 19(6) on which the state may impose reasonable restrictions. However, the term "reasonable" has not been defined under the constitution and no tests were laid down either. It is in this regard, the role of the Supreme Court to interpret the constitution comes into play.

Freedom of speech and expression

Article 19(2)– Article 19(2) allows the government to impose restrictions upon the freedom of speech and expression as ensured under article 19(1)(a). There are a lot of controversial cases revolving around Article 19(2) as freedom of speech and expression is one of the most basic rights an individual shall hold. Any restriction or any law that seems to restrict free speech have always been questioned and challenged.

The fact that freedom of press falls within the ambit of Article 19(1)(a) adds to the list of cases challenging the restrictions imposed on free speech. Free Speech and expression encompass an individual's right to express his own opinion without fear of sanctions from the government.
Article 19(2) draws a line of division between permissible speech and impermissible speech. It lays down a number of grounds under which the government may interfere and impose restrictions upon free speech which have been mentioned earlier at the beginning of this article.

Freedom to assemble peacefully without arms
Restrictions on the freedom of assembly Article 19 (3) of the Constitution provides that nothing in the right to assemble peaceably shall affect the operation of any existing law in so far as it imposes, or prevents the State from making any law imposing, in the interests of the sovereignty and integrity of India or public order, reasonable restrictions on the exercise of that right. The restrictions pertaining to sovereignty and integrity were added after the adoption of the Constitution.
Section 141 holds an assembly of 5 or more individuals illegal if the common objective is to overthrow the government by criminal force, to resist the execution of any law or legal process, to commit any mischief or criminal trespass or other offence, to unlawfully obtain possession of any property or the use of water or to compel any person to do what he is not legally bound to do or to omit to do what he is legally entitled to do.
The section also holds that an assembly which was lawful when assembled may subsequently become an unlawful assembly. Under section 144 of the Criminal Procedure Code, the magistrate is empowered to restrain an assembly if there is a risk of obstruction, annoyance or injury to any person legally employed or danger to human life, health or safety or disturbance to public tranquility or riot or any affray.

Freedom to form associations and unions
By virtue of Article 19(4) the governments are empowered to impose restrictions upon the freedom to form associations in the interest of public order or morality or sovereignty and integrity of India. The government may declare an association to be unlawful by notification in the official gazette if there are sufficient reasons to believe that it would interfere with the administration of law, maintenance of law and order and would constitute a danger to the public peace.

Freedom to move freely throughout the territory of India
Article 19(5) - In the interest of the general public and the interest of the Scheduled Tribes, the government may impose reasonable restrictions upon the freedom to move freely in the territory of India and the freedom to reside and settle in the territory of India. The intention of the makers of the constitution was to enhance the unity of India as India was a "Union of States" despite the administration having a well-established division of powers between states and the Centre.
E.g. With respect to the interest of Scheduled Tribes, the Guwahati High Court held in Dhan Bahadur GhortI v State of Assam that the allowing individuals to move into and reside in the premises of Scheduled Tribes would affect their very existence they are a sensitive society that needed to be preserved from the interference of the outside world.

Freedom to reside and settle in any part of the territory in India
Article 19(6) – Reasonable restrictions may be imposed by the government on the freedom of profession, occupation, trade or business on grounds of public order. Apart from the abovementioned ground, any

restriction upon the freedom of profession would be unconstitutional and it is not necessary that the restriction have to destroy the industry or business perse, but even if it creates a situation wherein it is impossible to carry on the business except in onerous conditions, such a restriction shall be held unconstitutional.

E.g. In State of Kerala v Joseph Antony, the State government had imposed a ban on mechanized nets and mid-water trawlers in territorial waters. This was challenged before the court on grounds that it imposed unreasonable restrictions on freedom of profession. The court observed that the object of the government was to promote the livelihood of poor other poor fishermen who could not afford such expensive machinery. The Supreme Court held that the restriction was constitutional.

Economic role / functions of government

1. Protection of private property / national security. If a country has a problem with crime, then it will discourage investment and the quality of life. The role of the government is to ensure basic law and order, through ensuring the rule of law. This involves protecting the rights to private property. In a free market, there is an incentive to free ride on the provision of law and order, therefore it tends to be under-provided. A government can pay for policing through general taxation. A similar function of the government is to provide for national defense – paying for an army. It is military spending which often was the primary cause of the first taxes. Kings raising taxes to pay for his army.

Policing and courts are an example of a public good – which usually require government provision.

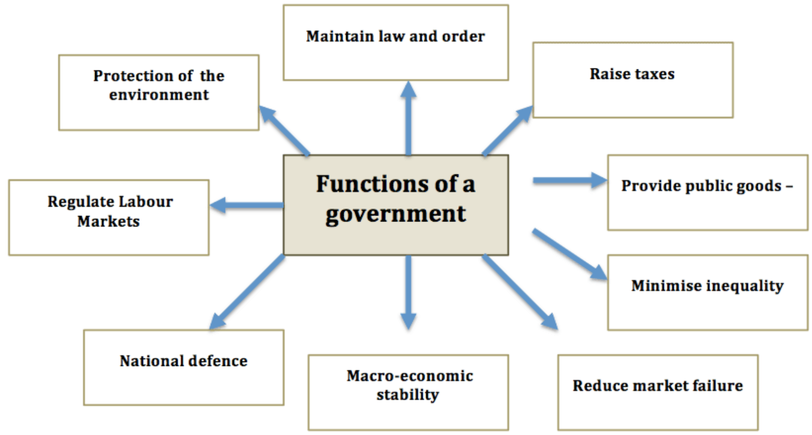
2. Raising taxes. To provide public goods and public services, the government needs to raise tax. They can do this in a variety of ways – taxes on goods (customs duties), taxes on income, taxes on people (poll tax) and tax on property and land. The government has to consider the best way of raising taxes. A good tax is efficient (doesn't distort economic activity); easy to collect (hard to avoid); fair (may involve taking a higher proportion of high earners). If the government run a budget deficit, they will need to raise the shortfall through borrowing and selling government bonds.

3. Providing public services. Public goods tend to be not provided in a free market because of the free rider problem. Therefore, these goods and services need to be provided by the government. Examples of public goods include street lighting, roads and law and order. There are also public services which are provided piecemeal in a free market, like education and healthcare. However, the government may feel that these merit goods are important for equality and improving labour productivity. Therefore, most governments provide some form of state provided education and health care.

4. Regulation of markets. Adam Smith in '*Wealth of Nations* 'noted that in a free market, firms were often able to create monopoly power. This enables them to charge excessive prices to consumers. The government may need to regulate monopoly power, e.g. prohibiting mergers or setting price limits in natural monopolies (industries like tap water and railways).

Also, firms may develop monophony power, where they are able to pay low wages and provide poor working conditions for workers. In this case, the government may need certain regulations on labor markets, such as minimum wages, minimum age of working and provide basic levels of health and safety.

5. Macroeconomic management. Capitalist economies can be subject to economic cycles – economic booms and recession. Recessions can lead to lost output and higher unemployment. In this case, the government may use fiscal policy to influence aggregate demand. The government may also use monetary policy, though, in recent years, many governments have delegated monetary policy to an independent Central Bank. In addition to trying to solve recessions, the government will also try to avoid inflation. This can involve higher taxes and higher interest rates.



6. Reducing inequality/poverty. In a capitalist economy, we may see a growth in inequality and poverty. This can be due to inherited wealth and opportunity. It can also be due to monopoly power. The government may feel the need to ensure everyone has an equal opportunity, for example providing education so even those from poor family have the opportunity to get qualifications. It may also involve redistributing income from high earners to low-income earners, e.g. progressive taxes such as higher rate of income tax and providing means-tested benefits such as income support/housing benefit and state pensions.

Demographic structure of India

Demography—the systematic study of the population of a country, area, community, etc. The term is of Greek origin and is composed of the two words, demos (people) and graphein (describe). There are two types of demography—

1. **Formal Demography:** statistical analysis of population i.e., total population, number of males, number of females, number of youth, working population, rural urban (quantitative data)
2. **Social Demography:** birth rate, death rate and migration that happens in a particular society.
   Consists of four processes.
   (i) Demographic Structure: number of people in an area,
   (ii) Demographic Processes: birth rate, death rate, migration,
   (iii) Social structure: composition of an area,
   (iv) Social processes: Processes by which individuals learn to live together in peace and harmony in society e.g. Cooperation, accommodation, mediation etc.

Socio-Cultural environment of India

Socio-cultural Environment: Socio-cultural en fecting a business and includes social traditions, value ethical standards and state of society, the extent of soc d so forth.

Socio-cultural environment consists of factors relate to human relationships and the impact of social attiudes and cultural values on the business of the organisation.

The beliefs, values and norms of a society determine how individuals and organisations should be

The core beliefs of a particular society tend to be rigid. It is difficult for businesses to change these core values, which become a determinant of its functioning. Some of the important factors and influences operating in this environment are as follows:

1. Social concerns, such as the role of business in society, environmental pollution, corruption, use of mass media and consumerism.

2. social attitudes and values, such as expectations of society from business, social customs, beliefs, rituals and practices, changing lifestyle patterns and materialism.
Family structure and the changes in its attitude towards and within the family and family values.
Role of women in society, position of children and adolescents in family and society.

Socio-cultural dynamics would mean the change in the social and cultural attributes of a society. Though in really these two attributes are inseparable like the two sides of a coin but for analytic convenience that can be treated separately.

Social denotes structural aspects i.e. it emphasizes on the nature of patterned interaction actually obtaining within and among various types of groups that exist in society. Some examples of such group being family, caste, economic organization and distribution of power and dominance.

Cultural aspects denote the collectively shared values, ideas and symbols that are associated with these groups and the pattern of social interactions existing therein. Some of the example being the value of inequality or hierarchy conveyed through the idea of purity-pollution, the idea of unity or holism meaning that different parts are united in one body, social. The fatalistic belief in the ideas of rebirth and various themes conveyed through literature of different periods.

Socio-cultural dynamics is a universal process. All societies at all-time are subject to this process of change. At the same time, it is a highly complex phenomena. To facilitate understanding, the change in the above mentioned aspect can be further divided into two categories. The criterion being, where the forces bringing above change are located.

Effects of socio-culture on business

The Effects of Socio-culture on Business: Businesses do not exist in a vacuum and even the most successful business must be aware of changes in the cultures and societies in which it does Dumness. AS Society and culture change, businesses must adapt to stay ahead of their competitors and stay relevant in the minds of their consumers. Various effects of socio-culture are:

1. Changing Preferences: A major socio-cultural factor influencing businesses and business decisions is changing consumer preferences. What was popular and fashionable 20 years ago may not be popular today or 10 years down the road. Different styles and priorities can undermine long successful products and services. For example, a clothing company must constantly be aware of changing preferences when creating new products or it will quickly become outdated.

2. Demographics: Changes in demographics are also a significant factor in the business world. As populations age, for example, markets for popular music and fashions may shrink while markets for luxury goods and health products may increase. Additionally, changes in the proportion of genders and different racial, religious and ethnic groups within a society may also have a significant impact on the way a company does business.

3. Advertising Techniques: Advertising is perhaps the area of business most closely in touch with socio-cultural changes. Advertising often seeks to be hip and trendsetting, and to do this, advertising agencies and departments cannot lose track of the pulse of societies in which they engage in business. Changes in morals, values and fashions must all be considered when creating outward facing advertising.

4. Internal Environment: In addition to a company's interactions with the market and its customers, socio-cultural factors also impact a company's internal decision-making process. For example, changing gender roles and increasing emphasis on family life have led to increased respect for maternity and even paternity leave with organisations. Additionally, attitudes towards racial discrimination and sexual harassment have changed drastically over the years as a result of sociocultural change.

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