

# PESTLE Analysis

## Strategy Skills

Team FME

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## Preface

The PESTLE Analysis is a useful method to use in order to identify the external factors that influence an organization.

You will learn:

- How the PESTLE Analysis can be used in conjunction with other strategy tools
- How the six factors of a PESTLE Analysis are classified
- How to carry out a PESTLE Analysis
- How to evaluate the relevance of a PESTLE Analysis
- How to avoid the pitfalls associated with using this strategy tool

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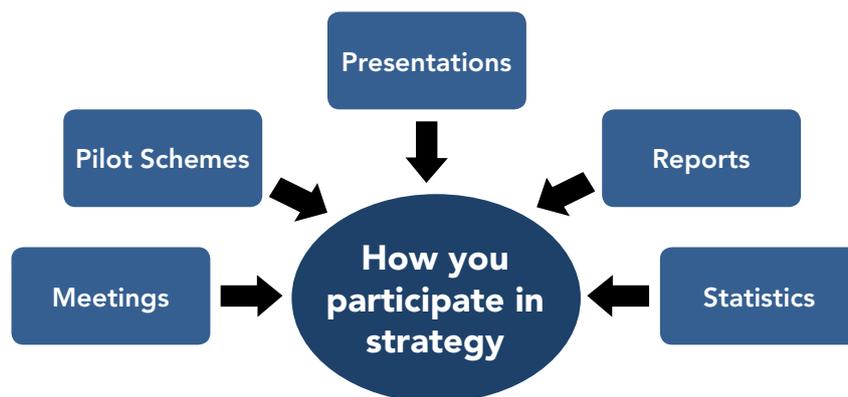
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## Introduction

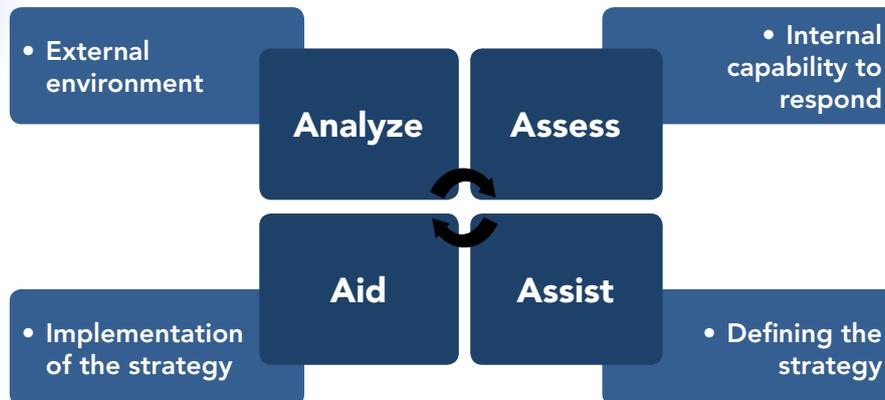
Today's organizations find themselves operating in an environment that is changing faster than ever before. The process of analyzing the implications of these changes and modifying the way that the organization reacts to them is known as business strategy.

*'Strategy is the direction and scope of an organization over the long term, which achieves advantage in a changing environment through its configuration of resources and competences' Johnson et al. (2009).*

While your role as a manager is unlikely to require you to make decisions at the strategic level, you may be asked to contribute your expertise to meetings where strategic concerns are being discussed. You may also be asked to comment on pilot schemes, presentations, reports, or statistics that will affect future strategy.

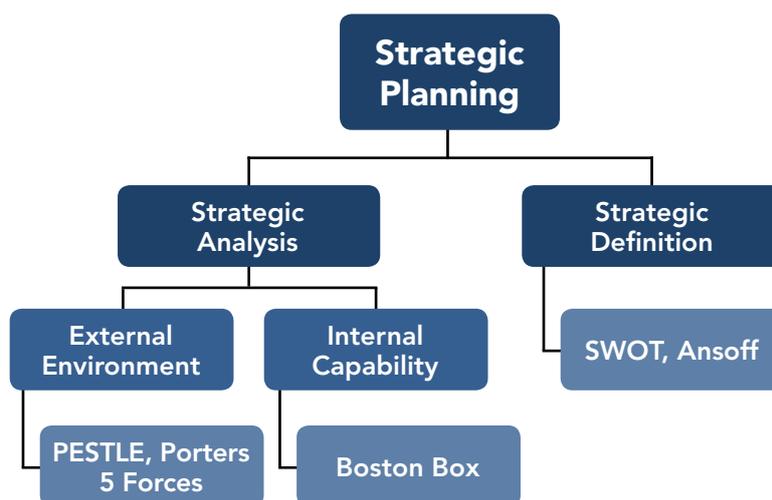


Whether you work in a large multinational corporation or a small organization, a good understanding of the appropriate business analysis techniques and terminology will help you to contribute to the strategic decision-making processes.



Typical scenarios where you could be asked to provide information and data for your organization’s strategic decision making include:

- Analyzing the organization’s external environment.
- Assessing the organization’s internal capabilities and how well it can respond to external forces.
- Assisting with the definition of the organization’s strategy.
- Aiding in the implementation of the organization’s strategy.



The diagram above shows where five widely used business analysis tools fit into the strategic planning process. This series of eBooks will give you a solid understanding of how these tools can be used, as well as an appreciation of their limitations.

This knowledge will enable you to take an active and productive role when asked to participate in the strategic decision-making process.

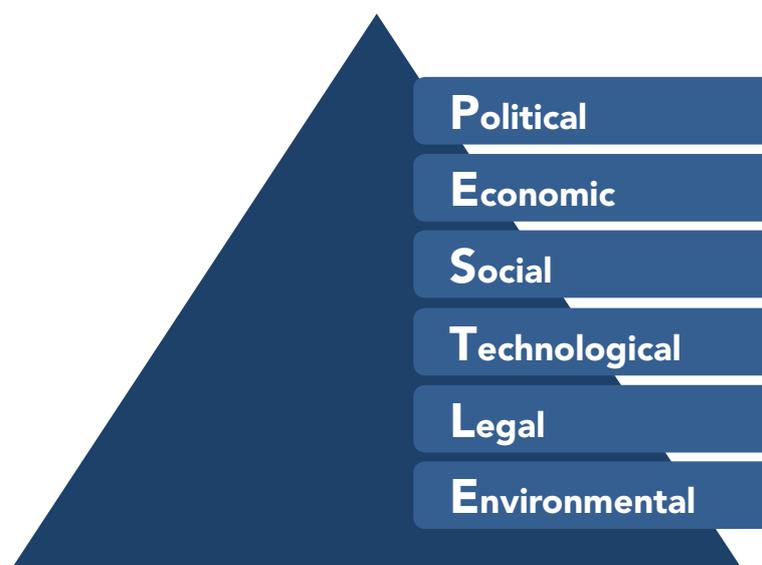
### KEY POINTS

- ✓ You may be asked to contribute your expertise to meetings where strategic concerns are being discussed.
- ✓ Typical scenarios where you could be asked to provide information for strategic decision making include: analyzing the organization's external environment, assessing internal capabilities, assisting strategy definitions, and aiding in the implementation.

## PESTLE Analysis

All organizations need to identify external factors within their environment that could have an impact on their operations. Many of these will be things that the organization has no control over, but the implications of which need to be understood.

A popular tool for identifying these external factors is the PESTLE Analysis, which can be used to help you consider Political, Economic, Social, Technological, Legal, and Environmental issues.



This process of identification should involve a variety of different disciplines across your organization so that a full picture of these external factors can be built up. These factors can then be fully researched and analyzed.

As organizations become more globalized, expanding their existing borders, the PESTLE technique ensures that they thoroughly question each of these factors and consider their impact.

The PESTLE Analysis provides you with a framework that enables you to investigate your external environment by asking questions for each factor and discussing the likely implications. These are the types of questions you would ask:

*What are the key political factors?*

*What are the important economic factors?*

*What cultural aspects are most important?*

*What technological innovations are likely to occur?*

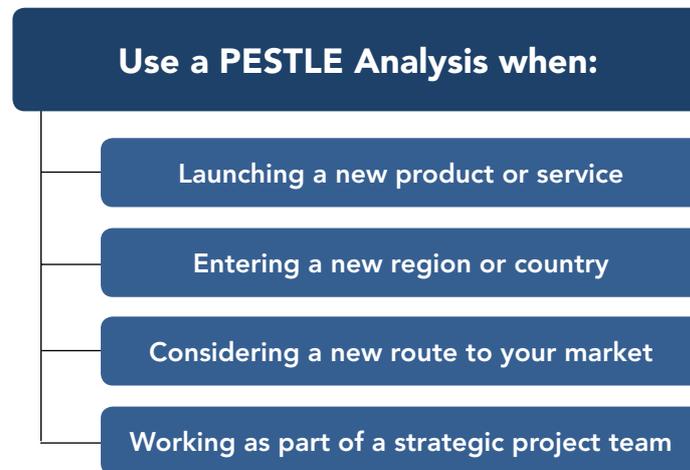
*What current and impending legislation may affect the industry?*

*What are the environmental considerations?*

How you categorize each issue raised is not important when using the PESTLE technique because the aim of this tool is simply to identify as many factors as possible. For example, whether you classify an impending government regulation as a *Political or Legal* issue is not important. The only thing that matters is that it is identified as potentially having an impact on your organization.

The PESTLE tool is a powerful technique for analyzing your environment but it should represent just one component of a comprehensive strategic analysis process.

The PESTLE factors, combined with external micro-environmental factors and internal drivers, can be classified as opportunities and threats in a SWOT Analysis. If the PESTLE analysis identifies factors that require internal changes to your organization, then these will need to be investigated further using tools like the Boston Matrix. If you are unfamiliar with these or would like to understand them in greater detail then visit our website [www.free-management-ebooks.com](http://www.free-management-ebooks.com) and see our range of Strategy Skills eBooks.



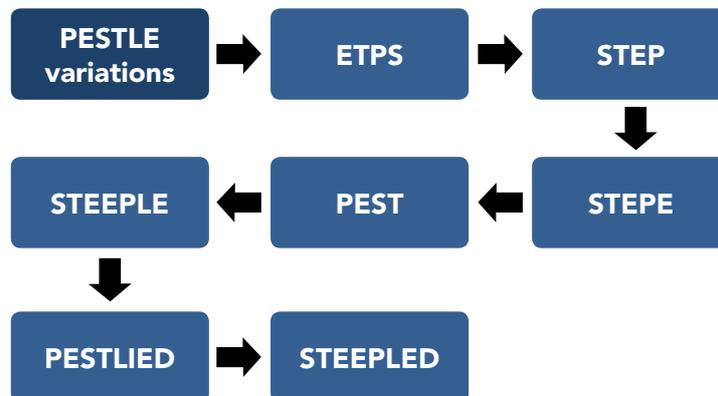
As a manager, you are most likely to be involved in these sorts of discussions when your organization is:

1. Planning to launch a new product or service
2. Exploring a new route to market
3. Selling into a new country or region

It is also a useful technique to know if you are part of a strategic project team. In all of these instances, there is a need to assess the potential impact of external factors on your organization, from both an operational and a market perspective.

The ranking of each of these factors within the six categories may vary because different organizations have different priorities. For example, organizations that sell to consumers tend to be more affected by social factors, whereas a global defense contractor would tend to be more affected by political factors. Additionally, factors that are more likely to change in the future or are more relevant to a given company will carry greater importance. A company that has borrowed heavily, for instance, would need to focus more on the economic factors.

There are several common variations of the PESTLE Analysis, with some using more factors and some using fewer than the six considered by PESTLE.



The most common variations are shown in the diagram above. The important thing to note is that these are all just variations of the one analysis tool; the underlying method is the same in all cases.

*ETPS—Economic, Technical, Political, and Social*

*STEP—Strategic Trend Evaluation Process*

*STEPE—Social, Technological, Economic, Political, and Ecological*

*PEST—Political, Economic, Social, and Technological*

*STEEPLE—Social, Technological, Economic, Ethical, Political, Legal, and Environmental*

*PESTLIED—Political, Economic, Social, Technological, Legal, International, Environmental, and Demographic*

*STEEPLED—Social, Technological, Economic, Environmental, Political, Legal, Educational, and Demographic.*

## KEY POINTS

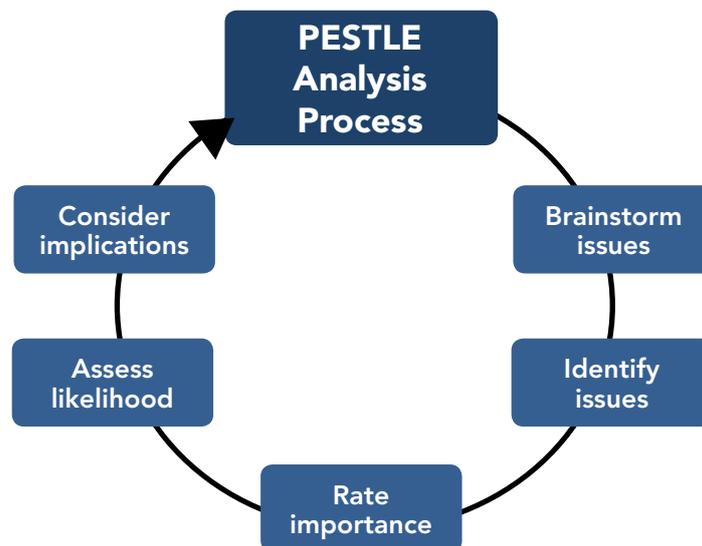
- ✓ A PESTLE Analysis can be used to consider political, economic, social, technological, legal, and environmental issues that may affect your organization.
- ✓ It is often used when launching a new product or service, exploring a new route to market, or selling into a new country or region.
- ✓ There are many different versions of this analysis tool, although the underlying method is the same in all cases.

## PESTLE Factors

The purpose of the PESTLE Analysis is to identify issues that fit two key criteria:

1. They are outside the control of your organization
2. They will have some level of impact on it

All discussions must be carefully controlled to keep the focus on identifying issues rather than trying to resolve them. You will need to consider the implications of any factors you identify as well as the likelihood of them occurring, but you must avoid falling into the trap of debating possible solutions or strategies.



The process you are likely to adopt when using the PESTLE technique is a relatively simple one:

1. Brainstorm and list key issues that are outside the organization's control.
2. Broadly identify the implications of each issue.
3. Rate its relative importance to the organization (e.g. critical, extensive, important, significant, moderate, or insignificant).
4. Rate the likelihood of it occurring (e.g. certainty, extremely likely, likely, potential, remote possibility, or will not transpire).
5. Briefly consider the implications if the issue did occur.

This process should give you a much clearer understanding of your environment. This view of the 'big picture' enables you to assess the potential risks that you face and can also be used to gauge what impact current external factors will have. This is referred to as using the PESTLE as a generic 'orientation' tool.

Remember, the responsibility of suggesting solutions to each issue is outside the scope of the PESTLE Analysis. Its sole purpose is to audit your organization's environment so that strategic decisions can be made once each issue has been fully researched.

As already mentioned, there are six factors that form the framework of this analysis. These Political, Economic, Sociological, Technological, Legal, and Environmental factors are each described next.

### KEY POINTS

- ✓ The PESTLE technique involves the following steps:
    1. Brainstorm and list key issues that are outside the organization's control.
    2. Broadly identify the implications of each issue.
    3. Rate its relative importance to the organization (e.g. critical, extensive, important, significant, moderate, or insignificant).
    4. Rate the likelihood of it occurring (e.g. certainty, extremely likely, likely, potential, remote possibility, or will not transpire).
    5. Briefly consider the implications if the issue did occur.
-

## Political Factors



It is always advisable to keep abreast of potential policy changes in any government because even where the political situation is relatively stable there may be changes in policy at the highest level and these can have serious implications.

This may result in changes in government priorities, which in turn can result in new initiatives being introduced as well as changes to trade regulations or taxation. These can include changes in:

- Employment laws
- Consumer protection laws
- Environmental regulations
- Taxation regulations
- Trade restrictions or reforms
- Health and safety requirements.

The creation of global bodies such as the European Union has led to legislation being introduced into member countries that may have an impact on your organization's operations. For example, the free movement of goods and services throughout the EU allows organizations to operate in 27 different countries with relatively few restrictions.

If your organization is assessing the possibility of operating in the Middle East or in some parts of Asia then the political dimension can be the most serious consideration of all. The organization's entry into the new territory may not be straightforward, either be-

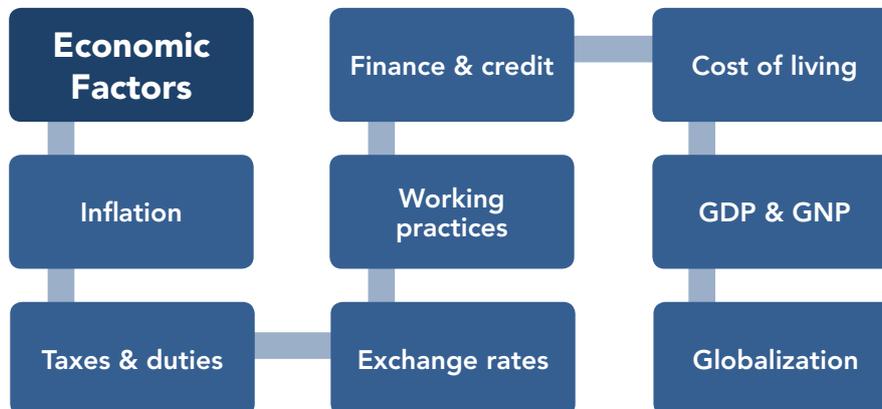
cause of that country's official policy or because the political realities of operating there are onerous.

For example, it may appear as if foreign investment is welcomed but the burden of bureaucracy is too weighty to make it profitable. The level of corruption may not be palatable for practical or ethical reasons. Other broader political issues you should consider are the political stability of neighboring countries, the level of freedom of the press, and the country's overall 'attitude' to foreign investment.

### KEY POINT

- ✓ Political factors include government attitudes to employment, consumer protection, the environment, taxation, trade restrictions, and societal reforms, as well as the burden of bureaucracy and the level of corruption.

### Economic Factors



These issues include: assessing potential changes to an economy's inflation rate, taxes, interest rates, exchange rates, trading regulations, and excise duties.

In terms of your operational efficiency you would also need to consider such factors as unemployment, skills levels, availability of expertise, wage patterns, working practices, and labor cost trends. When trying to determine the economic viability of a market you would also look at such issues as the current cost of living for your target market as well as the availability of credit or finance.

Organizations seek to create strategies that can be modified to fit changes in the economic situation and in particular the financial aspects of the macro-economic situation. This would include such things as the impact of globalization, taxation issues, and potential implications of profitability, as well as any trade tariffs or embargoes.

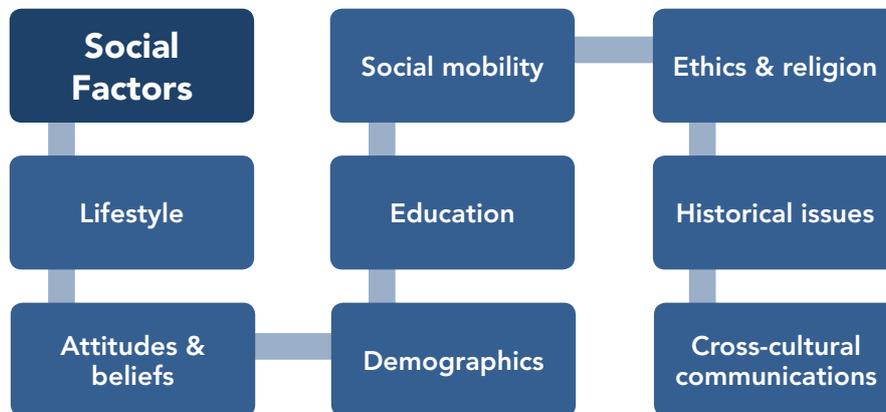
An economy with rising inflation would have an adverse effect on your pricing and the purchasing power of your customers. The rate of growth or the market's confidence in the economy could also be significant factors for your organization.

Official economic indicators, most of which are available online, such as GDP (Gross Domestic Product), GNP (Gross National Product), and consumer-based indices often highlight areas where more detailed information is required. In your PESTLE Analysis such indicators would only be highlighted so that further investigation could take place before a conclusion could be drawn.

### KEY POINTS

- ✓ Economic factors include assessing potential changes to an economy's inflation rate, taxes, interest rates, exchange rates, trading regulations, and excise duties.
  - ✓ Official economic indicators often highlight areas where more detailed information is required.
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## Social Factors



Social factors that need to be considered are those that have an impact on your market. These include:

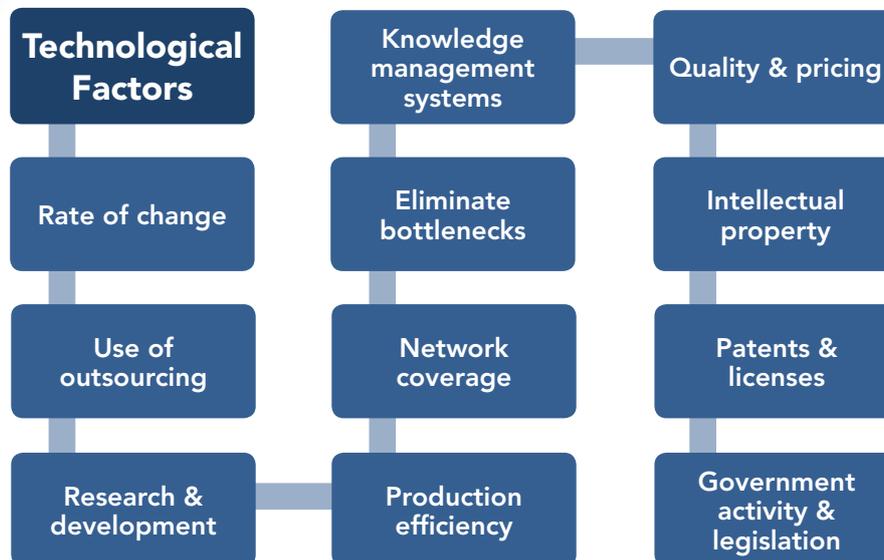
- Age distribution
- Population growth rate
- Employment levels
- Income statistics
- Education and career trends
- Religious beliefs
- Cultural and social conventions.

You should also consider attitudes towards things like health, career, and environmental issues. Social factors and cross-cultural communication play a critical role in international and global markets, and your success will depend on the depth of your research in this area. Getting this wrong is costly and may not come to light until considerable investment has been made by your organization. It can become an issue in managing the local labor force as well as promotional issues.

### KEY POINT

- ✓ Social factors include age distribution, population growth rate, employment levels, income statistics, education and career trends, and religious beliefs, as well as cultural and social conventions.

## Technological Factors



This element has become a key factor for organizations in assessing and listing issues that could have a potential impact on its operations and that could be critical to its long-term future. The pace of change in technology is becoming more rapid, and often changes that impact your market come from unexpected sources.

*For example, could the film industry ten years ago have predicted that people would stream their new releases rather than go to the cinema or buy a DVD?*

It is by using such techniques as PESTLE that organizations will be able to brainstorm even the most bizarre suggestions, because what today seems impossible may become commonplace in just a few years.

Technological factors can be broadly divided into two areas: manufacture and infrastructure. By exploiting opportunities to update or alter their production an organization can gain market share, thereby attaining a strong competitive advantage. Such activities include:

- Automation
- Improved quality of parts and end product
- Incentives
- Significant cost savings
- Use of outsourcing to control costs and offer greater flexibility

Technological advances have also allowed organizations much greater freedom of choice when deciding how best to manage their operations. For example, knowledge-based systems have enabled management to make better and more informed decisions in real-time.

The rapid growth in networking capabilities, both in terms of being more reliable and having extensive coverage internationally, has allowed organizations to streamline their workflow and eliminate operational bottlenecks.

Organizations that fail to keep up with technological advances leave opportunities for a smaller producer or new entrant to enter their market and erode their leadership status.

*This is what happened to mobile phone producers Research in Motion (RIM, the makers of the BlackBerry) and Nokia, who were slow to embrace smart-phone technologies. The result was that they both lost significant market share to Apple and Samsung.*

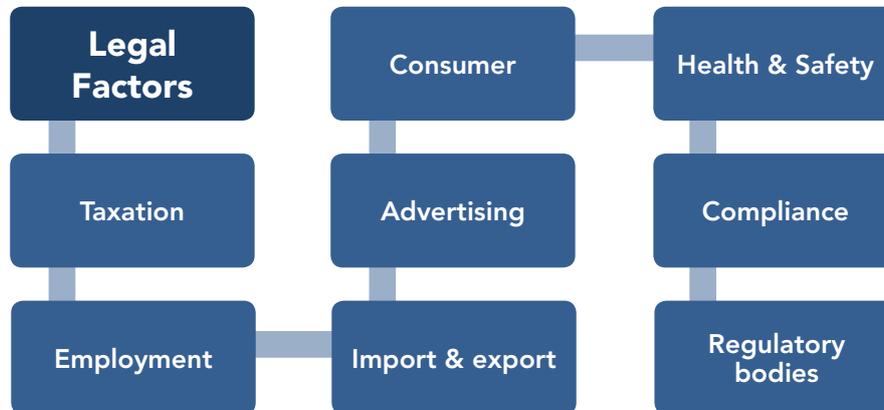
This example clearly illustrates how consumers' preferences and usage change following a technological advance and how this feeds through to market share. Many organizations want to protect their advantage as long as possible, so the use of patents and licensing has become a key strategy for many in protecting their intellectual property.

The impact of technology on the individual has led to legislation being introduced which aims to protect your privacy and ensure organizations have to gain your permission before emailing or contacting you. Organizations need to give careful thought to the type and nature of potential legislation that governments could introduce to curb what is often seen as the invasive side of the rapid growth of technology.

## KEY POINTS

- ✓ The pace of change in technology is becoming more rapid, and often changes that impact your market come from unexpected sources.
- ✓ Technological factors can be broadly divided into two areas: manufacture and infrastructure.
- ✓ Organizations that fail to keep up with technological advances leave opportunities for a smaller producer or new entrant to enter their market.

## Legal Factors



The list of legal factors that should be considered includes current and impending legislation that may affect the industry in areas such as employment, competition, and health and safety. Anticipated changes in legislation in the main trading partner countries should also be investigated.

Recent years have seen a significant rise in the number of regulatory bodies that have been set up to monitor organizations' observance of legislation relating to all areas of operations, including consumer protection, employee welfare, waste disposal, and how their earnings and investments will be taxed. There are also the trading restrictions, quotas, and excise duties to consider.

All these factors affect the way in which an organization functions and have cost implications that need to be taken into account when formulating business strategy. For example,

*Insurance and banking organizations have to demonstrate their legal compliance to the regulatory body, which has implications for how they operate.*

*The level of market share is often restricted (e.g. under the Antitrust laws of America) to prevent organizations having an unhealthy control of a market or obtaining it through acquisition.*

Your PESTLE Analysis should consider the impact of your own national laws as well as those originating in other countries that could have implications for you, for example global accounting regulations, safety compliance, etc. This analysis needs to include

those laws affecting working relationships with other organizations that form part of your overall operations. Examples of this type of legislation include:

*The 2002 US federal law, Sarbanes-Oxley Act. This set out new or enhanced public accounting standards for all American public company boards. This law came about after several major corporate accounting scandals, such as Enron, Peregrine Systems, and WorldCom.*

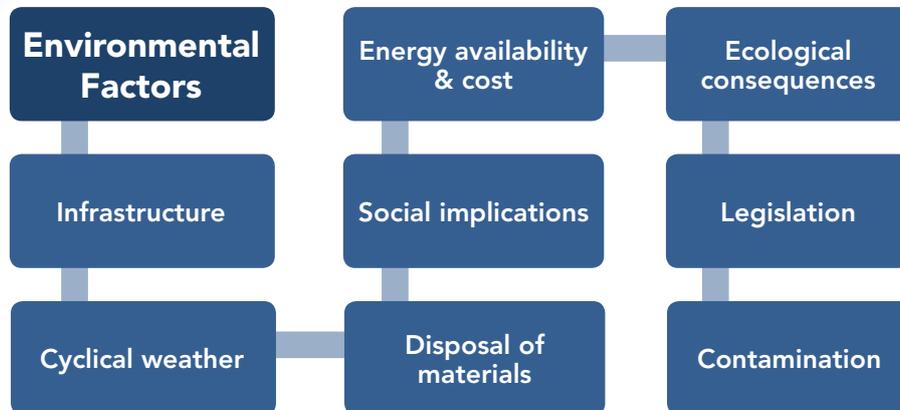
*The Waste Electrical and Electronic Equipment Directive (WEEE Directive) is a European Union directive, which, together with the RoHS Directive, set legally binding collection, recycling, and recovery targets for all types of electrical goods sold in the EU.*

Many regulations are applied at a regional as well as a national level and create another layer of complexity that you must consider when developing your strategy. It is these types of influences that can have a significant impact on the ease of operations and require detailed investigations before any decision is made.

## KEY POINTS

- ✓ Legal factors include current and impending legislation that may affect the industry in areas such as employment, competition, and health and safety.
  - ✓ Your PESTLE Analysis should consider the impact of your own national laws as well as those originating in other countries that could affect you.
-

## Environmental Factors



The issues surrounding environmental protection have become increasingly important in recent years as the implications of under-regulated economic activity are seen today. This has become more significant with globalization as the impact of an organization's actions may be felt outside of its native country and may incur unquantifiable financial penalties.

Other environmental factors are those that relate to the weather, climate, and geographical location. For example,

*Natural disasters or weather cycles such as monsoons may create too high a risk for operating in particular regions.*

*The physical condition, extent, and maturity of a country's infrastructure may impose uneconomic costs on an organization. Weather conditions could also cause logistical problems at certain times of the year.*

*Potential financial penalties resulting from causing contamination of soil or water may be unquantifiable.*

*Before operating in a country with high temperatures and humidity you would want to determine the availability, financial viability, and reliability of air conditioning.*

As with the other PESTLE factors you would look at how the potential changes to weather patterns and climate cycles could have implications for your organization's operations.

These ecological and environmental aspects can have consequences that are felt both on an economic and a social level.

An increasingly important consideration facing organizations is one of packaging and waste disposal and its environmental consequences. Throughout Europe all electrical equipment retailers are required by law to pay a government levy based on their sales volume. The funds generated in this way go towards minimizing the cost and environmental impact of obsolete products.

### KEY POINT

- ✓ Environmental factors include infrastructure, cyclical weather, disposal of materials, energy availability and cost, and the ecological consequences of production processes.
-

## Summary

To maximize the benefit of the PESTLE Analysis it should be used on a regular basis within an organization to enable the identification of any trends. The impact of a certain external factor may have more severe consequences for a particular division or department and the PESTLE technique can help clarify why change is needed and identify potential options. As with all techniques there are advantages and disadvantages to using it to help plan organizational strategy.

### Advantages

- Provides a simple and easy-to-use framework for your analysis.
- Involves cross-functional skills and expertise.
- Helps to reduce the impact and effects of potential threats to your organization.
- Aids and encourages the development of strategic thinking within your organization.
- Provides a mechanism that enables your organization to identify and exploit new opportunities.
- Enables you to assess implications of entering new markets both nationally and globally.

### Disadvantages

- Users can oversimplify the information that is used for making decisions.
- The process has to be conducted regularly to be effective and often organizations do not make this investment.
- Users must not succumb to 'paralysis by analysis' where they gather too much information and forget that the objective of this tool is the identification of issues so that action can be taken.
- Organizations often restrict who is involved due to time and cost considerations. This limits the technique's effectiveness as a key perspective may be missing from the discussions.
- Users' access to quality external information is often restricted because of the cost and time needed to collate it.
- Assumptions often form the basis for most of the data used, making any decision made based on such data subjective.

This analysis technique should be used in conjunction with other tools such as a SWOT and other strategy tools. The objective of using the PESTLE Analysis is to ensure that you have identified the important implications for your organization and that nothing key has been overlooked.

## Other Free Resources

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