



Study of business environment through pest analysis

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Abstract

During the last decade many changes have taken place in the world economy and especially in corporate environment. The business environment today is turbulent and laced with uncertainty which is continuously changing and is full of opportunities and challenges. The companies are necessitated to change their manufacturing practices, technologies and identify the opportunities at the right time and face them with right strategy can only gain competitive advantage. PEST Analysis as a strategic tool may be helpful for success in the business arena.

Keywords: business environment, competitive advantage, environmental analysis, pest analysis, scenario planning

Introduction

The successful companies are no longer competing on single dimension, such as cost. Instead, companies must excel on two or more of the traditional strategic elements. They must not only focus on producing a low cost product but additionally maintain high quality and customer service levels. There is a shift in corporate strategy from 'product driven' to 'market driven' strategy. Customer satisfaction has become the corporate goal to succeed in this business environment. Especially the growing intensity of competition has forced many business enterprises to seek more innovative and communication skills and systems. In the current industrial scenario it becomes difficult in the industry to sustain and survive unless the costs are correctly accounted for, controlled and reduced so as to sustain and remain in the industry. PEST analysis stands for 'Political, Economic, Social and Technological Analysis', developed by Johnson and Scholes to indicate the external influence viz., political, economic, social and technological factors on business firm. PEST analysis is a technique of environmental scanning to analyze the influence of macro environmental factors on business organisation. PEST analysis is basically used as a strategic tool to understand the market share, market growth rate, consumer tastes and habits, political stability of the state, business position, foreign business prospects, environmental opportunities and threats etc.

Pest Analysis: Five Steps Analysis

The PEST analysis consists of the following five steps:

Step 1 Understand a category's relevant trends:

- Research the important variables of the organization's strategy.
- Determine the long-term trends that apply to these variables.
- Research the past behaviour of these variables.
- Analyze the predictability of the trend lines and their fluctuations.
- Assess the impact of these trends on the organization.

Step 2 Understand trend interdependencies

- Analyze which trends are interrelated.
- Determine which trends conflict by understanding movements in opposite directions.

Step 3 Distill likely issues from the identified trends

- Validate the impact of trends on the organization.
- Distill the most critical trends that have the greatest impact given the organization's objectives.

Step 4 forecast the direction of issues

- Determine the fundamental drivers behind a critical trend.
- Assess the behaviour of the critical trend.
- Run a sensitivity test to assess the impact.

Step 5 Derive implications for the organization:

- Assess the affect of critical environmental changes on the industry.
- Assess affect of critical environmental changes on a firm's competitive position.
- Assess the affect of critical environmental changes on a direct copetitor's position.
- Validate a firm's competitive nature.

The PEST analysis may contribute to environmental analysis in three ways. First, it may enable identification of a smaller number of key environmental influences. Secondly, it may also be helpful in identifying long-term drivers of change in environment. Thirdly, it may help to examine the different impact of external influence on organization either historically or in terms of likely future impact. In PEST analysis the external business environment is studies under the following four heads:

Political and Legal Environment

The political environment of a region and country to which the business firm relates will have greater impact on its growth and sustainability. The political and legal environment of the rest of the globe will also have greater impact when the firm has extended its business operations across the globe the government plays a vital role as the planner, promoter and regulator of business firms. The form of government in position is an important aspect of political environment and political stability is an essential factor influencing the growth of business. The political and legal environment has a significant impact on the opportunities and threats for business organizations. The philosophy of political parties in power influence business practices. The legal environment serves to define what organizations can and cannot do at a particular point of time. The pro-business philosophy allows to enter into arrangements like mergers, acquisitions, joint ventures, business alliances, outsourcing arrangements etc. in between the business firms across the globe.

The business and industry operate within the framework of the prevailing legal environment. The legal environment facing organizations is becoming increasingly complex and affecting business more directly. The business firms are expected to have thorough knowledge of the laws of the land, rules and regulations, government policies etc. to reduce the political and legal impact on business firm. The concern for protection and conservation of natural environment has been subject to many regulations and policy changes in the recent past.

The political and legal factors that influence the business firms and industry are:

- Political climate
- Political stability
- Political ideology and philosophy of political party in ruling
- Stand of opposition parties on business
- Level of political morality
- Law and order situation
- Political attitude towards business
- Government's attitude towards foreign business firms
- Corporate and personal taxation rates
- Restrictions on international financial flows
- Legislation that favour business investments
- Controls on business frauds
- Government debt
- Import tariffs and quotas
- Simplicity of tax laws
- Severity of employee welfare legislation
- Environmental protection laws
- Anti-monopoly laws
- Export restrictions
- Copyright and patent protection
- Extent and nature of government regulation in business and economy
- Regulatory calibre of government agencies
- Influence of political pressure groups
- Political influence on trade unions
- Protection of special interest groups like consumers, women, minorities
- Simplicity and understand ability of government legislation
- Consumer protection laws
- Environmental pollution control legislation

- Government's view on globalization and trade liberalization

Economic Environment

The economic environment of business refers to overall state of the country/region's economy.

It has significant impact on the industry structure and profitability of individual firms. Economic factors refers to the character and direction of economic system within which the firm operates. The survival of business and industry largely depends on the purchasing power of people which is dependent on economic environment. The economic factors decide the nature and direction of the economy of the economy in which the firm operates.

The economic variables that impact the business and industry include:

- State of business cycle
- Distribution of income within the population
- Government's monetary and fiscal policies
- Trade restrictions
- Money supply
- Industrial production
- Capacity utilization
- Unemployment
- Inflation
- Growth in GDP
- Institutional lending
- Stock market movements
- Monsoons
- Productivity of factors of production
- Fiscal deficit
- Credit/Deposit Ratio
- Stock of food grains and essential commodities
- Industrial wages
- Foreign trade and balance of payments position
- Infrastructure facilities
- Economic and industrial policies of the government
- Debt recovery and loans outstanding
- Interest rates
- Foreign investments
- Trends in capital market
- Foreign exchange rates
- Government intervention in free market working
- Growth rate of economy etc.

Socio-cultural and Demographic Environment

The socio-cultural environment of business consists factors like social traditions, values and beliefs, level and standards of literacy and education, ethical standards and state of society, extent of social satisfaction, conflict and cohesiveness etc. which influence the industry structure, its success, growth and profitability. The socio-cultural dimension of the environment consists of customs, life-styles and values that characterize the society in which the firm operates. The culture is the result of complex factors such as religion, language, education, ethical beliefs etc.

Demographic factors such as population growth, age composition, family size, family life cycle, income levels, religion, tastes and habits, education levels, birth rate, death rate etc. will have significant bearing on the strategic decision making. A social class is identified by income, occupation, life-

style and class norms. Socio-cultural components of the environment influence the ability of the firm to obtain resources, market its goods and services, and function within the society. Observing the socio-cultural and demographic factors enable to identify the opportunities and threats for the business organization.

Technological Environment

The technological environment includes the changes in technology which can alter the firm's competitive position. Technology and business are interrelated and interdependent. Technological changes bring many new opportunities as well as causing threat by making existing systems obsolete. The changing technology may affect the demand for a firm's products and services, its production processes, and raw materials. The technological developments need a careful and timely strategy formulation, otherwise competitors would take a lead in the market position. The advancement of technology can reduce or improve opportunities for a firm. Technological changes will bring in many new products as well as causing death of many existing products.

Organisations have been influenced by the technological changes and will be continually influenced by breakthrough in future.

- Computing speed has impacted the organizations fundamentally. They have affected the design and manufacture of products, the way organizations communicate with suppliers and customers, and the way organizations are managed internally. CAD, CAM and CIM are classic examples of this.
- Information acquisition and dissemination has been greatly enhanced by the merger of telecommunications and computers. Revolutions are happening in the way Indian companies are communicating with their members, suppliers and customers almost instantly through gadgets.
- Internet technologies are changing the business models and challenging the traditional structures. Net enabled technologies are integrating with the business processes of the modern organizations.

The internet is acting as a national and even global economic engine that is spurring productivity. The internet is saving companies billions of dollars in distribution and transaction costs from direct sales to self-service systems. The internet is changing the very nature of opportunities and threats by altering the life cycles of products, increasing the speed of distribution, creating new products and services, erasing limitations of traditional geographic markets and changing the historical trade-off between production standardization and flexibility. It is also altering economies of scale, changing entry barriers and redefining the relationship between industries and various suppliers, creditors, customers and competitors. An emerging consensus holds that technology management is one of the key responsibilities of strategists.

Conclusion

The four macro environmental factors *viz.* political and legal, economic, socio-cultural and demographic as well as technological factors have significant impact on the survival of business and growth prospects. These factors are external to the business and beyond the control of individual enterprise and their

management. The external environment poses threats to a firm or offers immense opportunities. A firm may be influenced by changes within the general environment but cannot itself influence the environment. The crucial part of the strategic planning process is the appraisal of the environment of an organization. The firm may use scenario planning techniques to forecast in high levels of uncertainty in external environmental conditions.

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