

Tools guide

PEST analysis



The Association of Product Management is a professional membership body that helps you manage your professional development. We produce and maintain a wide range of best-practice guides, tools and templates for our members to use.

What is a PEST analysis?

A PEST (or PESTEL) analysis is a strategic business tool used to capture, organise and analyse the external macro-economic (big picture) factors impacting our customers that in turn impact the success of our business (or product) now and in the future. It is a valuable tool for market research and helps understand and forecast market growth or decline; it highlights opportunities and steers our decision making.

The basic PEST includes four factors:

1. Political
2. Economic
3. Social
4. Technological

There are various extensions of these, the two most used are:

5. Environmental
6. Legal

You can include Environmental under Social and Legal under Political if you prefer a simpler model. Unless these are really key factors for your product, it's easier to keep to the four-box model for clarity.

PEST analysis is segment specific, particularly if you sell into geographically diverse markets (eg USA and the UK) and/or radically different verticals (eg financial services and pharma), so the more specific you are in your market segmentation definitions, the more valuable your PEST analysis will be. If you haven't segmented tightly enough, your PEST analysis will end up being too generic and therefore not very useful. Using the example above, a pharmaceutical company in the UK will have a very different PEST analysis to a bank in the USA, but they may both be viable target segments.

Why should we use a PEST analysis?

As product managers, we need to understand the different worlds that our customers operate in. We use this knowledge in different contexts.

1. Customer research and thought leadership

We need to be able to hold educated conversations at a senior level with our customers about their business strategy, the markets they operate in and how their businesses are affected by external factors both today and in the future. By having these conversations with many customers, we gain deep aggregated knowledge of our markets. Our knowledge improves the depth, breadth and value of the PEST analysis and the PEST analysis in return improves our understanding of our markets, enabling us to have these educated, strategic conversations with customers. And so, we become thought leaders in our industry.

2. Innovation

When we conduct our market research and the impact on customers, we're looking for changes in external factors that are likely to cause problems for them. Customer problems are aggregated to show us market trends. These trends present risks and opportunities that we can analyse. Proactive trend analysis enables us to be proactive in adapting our solutions or creating new solutions to solve those problems.

This is called demand-pull innovation and is one of three main innovation strategies.

3. Manage risk

When assessing whether or not to step into a new segment or expand our presence in a segment (market development growth strategy), we use what we've learned in the PEST analysis combined with other tools such as a Porter's Five Forces analysis and/or a SWOT to assess the attractiveness of that segment. This enables us to not just leverage the opportunities we see, but also identify and mitigate the associated risks.

How do we do it?

We research, read, listen, discuss, analyse (from a wide range of sources) and then we make sense of all the knowledge we're acquiring by organising it into a PEST analysis. These four headings focus us on the big picture of the external environment and prevent us from being too inward facing. Let's have a closer look at what's involved.

1. Political (including Legal)

What government policies could be beneficial (or detrimental) to product success? Is the political environment likely to change?

- Political stability.
- Government policy.
- Legislation (including environmental/ecological).
- Trade/safety/employment/consumer protection regulations.
- Tax policy.
- Trade restrictions.
- Bureaucracy and/or corruption.

2. Economic

What economic factors are likely to affect our product? How does the performance of the economy affect our product? How are things like pricing, revenue, costs impacted?

- Inflation, interest rates, exchange rates.
- Market and trade cycles.
- Home and overseas trends (growth/decline).
- Unemployment rates, consumer disposable income (end user drivers).
- Monetary policy, availability of credit.
- Specific industry factors.
- Labour costs.
- Seasonal factors.

3. Social (including Environmental)

How do social attitudes, beliefs and behaviours influence customer buying habits in our target market? How do cultural trends and human behaviour impact our product?

- Cultural awareness.
- Demographics.
- Lifestyle trends.
- Attitude and shared beliefs about things like money, borrowing, imports, health, work, leisure, immigration, the environment.
- Education.
- Customer buying patterns.
- Ethnic/religious factors.
- Ethical issues.

4. Technological

What technology advancements or innovations are coming? How will they impact our products, our operations and our customers? How will they force change on us or our customers? Can we leverage them?

- Infrastructure.
- Legislation.
- Access.
- Maturity of technology.
- Advancements and emerging technologies.
- Competing technological developments.
- Business and/or consumer buying habits and adoption rates.
- Lifecycles.
- Investment, R&D, incentives.
- Licencing, patents and IP issues.
- Research funding.

Summary

As product managers, we need to understand the different worlds that our customers operate in. A PEST analysis is a strategic business tool used to capture, organise and analyse the external macro-economic factors impacting our customers that in turn impact the success of our product now and in the future. It is a valuable tool for market research and helps understand and forecast market growth or decline; it highlights opportunities, helps mitigate risk and steers our decision making.

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