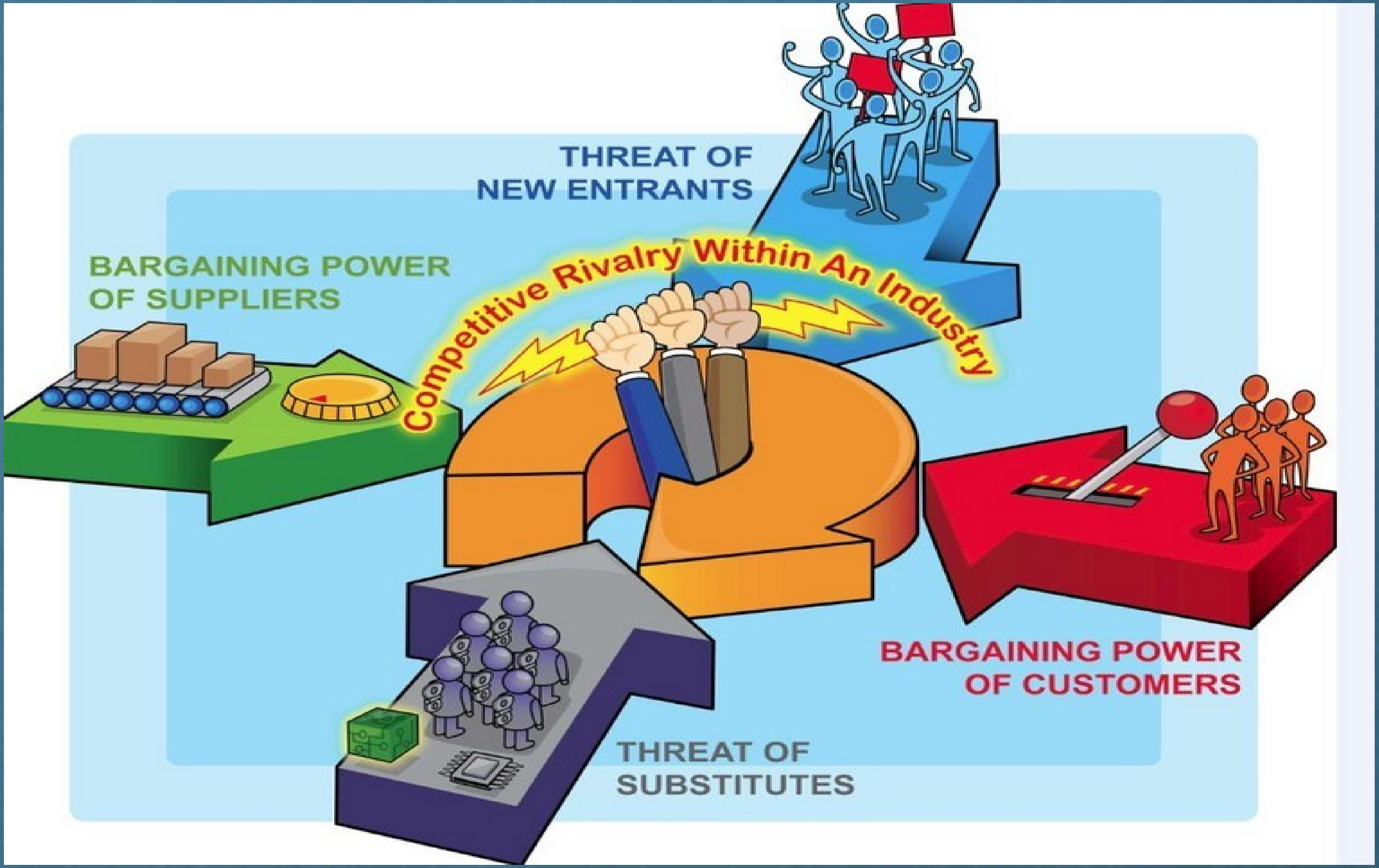
Porter's Five Forces

A MODEL FOR INDUSTRY ANALYSIS

Michael E. Porter

- **Born in 1947.**
- **Professors in Harvard Business School.**
- **Introduced Porter's 5 Forces Model.**
- **Written 18 books & over 125 Articles.**

Porter’s Five Forces Chart



Importance of The 5 Forces

What strategy to use?

Basic knowledge of business strategy & forces that influence the decision making

Industry analysis :
1) Industry relevance
2) Industry players
3) Industry structure
4) Future changes

Strategize :
* Competitive advantage
* Cost advantage
* Market dominance
* New product development
* Contraction / Diversification
* Price leadership
* Global
* Re-engineering
* Downsizing
* De-layering
* Restructuring

Measure and monitor strategy effectiveness

How to deal with competition?

ISOmantra
Aim • Adapt • Achieve

Threats of New Entrants

The easier it is for new companies to enter the industry, the more cutthroat competition there will be. Factors that can limit the threat of new entrants are:

1. How loyal are the end users in this industry?
2. How troublesome or hard is it for the end users to switch and use another product?
3. Does it require a large seed capital to enter this industry?
4. Do entries to this industry regulated by government?
5. How hard is it to gain access to the distribution channels?
6. How long does it take for new staff to acquire the necessary skills to do the work?

Threats of New Entrants :
McDonald’s company analysis

1. The threat of new entrants in the fast food industry is high because there are no legal barriers.
2. The economies of scale and the access of the distribution are the major barriers that firms face in the industry.
3. Firms must spend a large amount of capital on advertising and marketing in order to enjoy successful existence and long life of a fast food outlet.
4. Large established companies with strong brand names such as McDonald’s make it more difficult to enter the market because new entrants are faced with price competition from existing chain restaurants.
5. Thus, it takes a pretty much time for a new business to establish in the fast food industry.

Threat of Substitutes

Threats of Substitute in the Porter's theory actually means goods and services that does similar functions

- How many close substitutes are available?
- How pricy are the substitutes?
- What is the perceived quality of the substitutes?

- When there is one product successful, it also leads to the creation of other products that can perform the same functions as the product of the same industry.

- Porter also mentions that if one industry wishes to follow suit

  producing products with similar function, attention should be given to :
  1. Products that enjoy steady price-performance tread offs with the industry’s product
  2. Would entail minimum switching costs for a buyer.
  3. Are produced by industry earning high profits

- Porter recommends that by doing advertising, product quality improvement, marketing, R&D and product distribution, an industry

  can improve its collective position against the substitute.

Threat of Substitute: Examples

Intensity of rivalry among established firms

1. How many close competitors exist in the industry?
2. What are the sizes of your close competitors?
3. What is the industry structure? Is it a fragmented, consolidated, oligopoly or monopoly industry?
4. What is the current industry growth rate?

4. How high are the exit barriers? Do your competitors have a high committed fixed cost thus they have to operate even at a loss?

5. How diversified are your competitors?

6. How extensively do your direct competitors advertise?

7. Each competitors aim to serve different needs and market segment with different mixes of
   - price
   - products
   - service
   - features

Intensity of rivalry among established firms : Examples

Bargaining power of Customers

1. How large are your buyers' company?
2. How many companies are there for the buyer to choose from?
3. Are the buyers buying a huge volume?
4. Do you depend only on a few buyers to sustain your sales?

5. **How hard is it for the buyers to switch and use a competing product?**

6. **Are the buyers purchasing from you as well as your competitors?**

7. **Do the buyers have the capacity to enter your business and produce the goods themselves?**

Bargaining power of Customers: Example of Coca-Cola Company

Depends on the marketing channel used. or Coca-Cola,

1. Super Markets
2. Convenience Stores
3. Mass Merchandisers
4. Soda Shop
5. vending machine
6. Restaurants and Food stores

Bargaining power of buyer is high for fountain supermarkets and mass merchandising because of the low profitability and strong negotiation power of retail channels but for vending bargaining power is non- existing caused by high profitability.

Bargaining power of Suppliers

- **Are there substitutes for your suppliers' products?**
- **Do your suppliers serve multiple industries? Does the total industry revenue accounting for only a mall portion of the supplier's total revenue?**

- Do you have high switching cost to use another supplier?
- Do suppliers have the capacity to enter your business?
- Does your company capable to enter the supplier’s business?