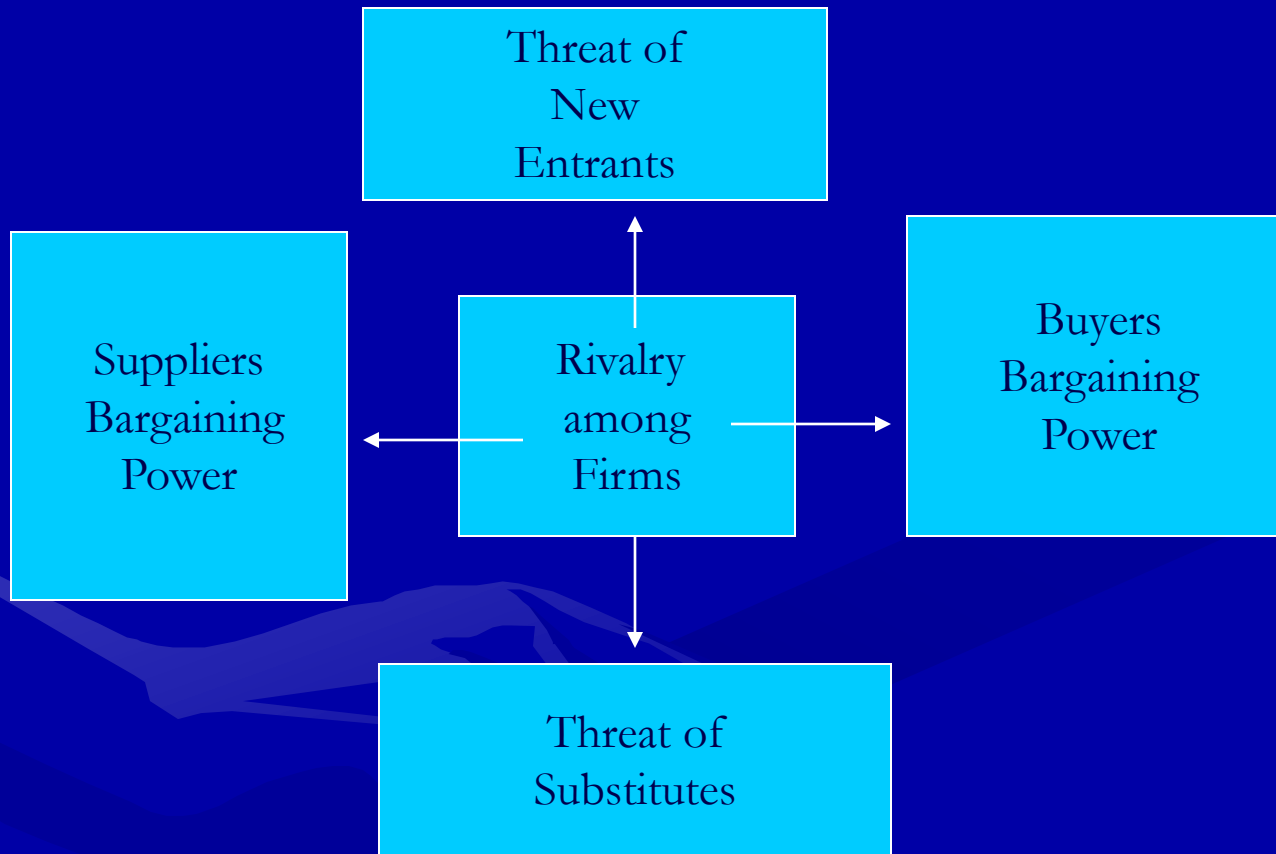


Industry Analysis Through Porter's Five Forces



Porter's Five Forces Framework



- The Five Forces Framework is an analytical tool for assessing the competitive environment.
- The combined strength of these five forces ultimately determine an organisation's ROI or the potential for profits within a given Industry

The Five Forces

- Threat of New Entrants
- Bargaining Power of Buyers
- Bargaining Power of Suppliers
- Threat of Substitute Products or Services
- Intensity of Rivalry among Firms in an Industry

Threat of New Entrants

The Industry in which Organizations earn profits in excess of their cost of capital ,attracts new entrants. The threat of entry will depend on the barriers to entry and the reaction of existing competitors. If the entry barriers are high then the threat of entry to the industry by new organizations will be low. Similarly if a new entrant expects that the existing firms will retaliate, e.g. by lowering their price,this deter new firms from entering into that Industry

Important Barriers to entry

- Economies of Scale
- Capital Requirement
- Product Differentiation
- Switching Costs
- Access to Distribution Channels
- Cost Advantage independent of Scale
 - Proprietary Product Technology, e.g. Gillette
 - Favourable access to Raw Materials
 - Favourable Locations
 - Govt. Subsidies

Bargaining Power of Buyers

- Buyers can affect an Industry through their ability to force down prices, bargain for higher quality or more services and to play competition off against each other. The power of buyers increases in the following circumstances
 - The Buyers are less in number
 - When the Buyers place large orders
 - When Switching costs are low

- When alternative suppliers are present
- When the buyer has the ability to integrate backward
- The products are standardized or undifferentiated
- The buyer earns low profits
- When the quality of the products to the buyer are not important

Bargaining Power of Suppliers

Suppliers can exert pressure over participants in an Industry by raising prices or reducing the quality of purchased goods or services. A high Supplier bargaining power constitutes a negative feature for existing firms or new entrants of an Industry. Suppliers are powerful in the following circumstances.

- When the suppliers are few in number and the buyers are many in number.
- When the products or services are unique and has few substitutes

- When the substitutes of the products or services supplied are not freely available
- When the switching costs of the supplier from one buyer to the other is low.
- When the supplier is not critically dependent on the products or services supplied.
- When the buyer buys in small quantities, and therefore is not important to the supplier.
- When the supplier has the ability to integrate forward

Threat of Substitute Products

- Substitute products or services are those that are though different but satisfy the same set of customer needs. E.g. Tea, Coffee and aerated drinks.
- The availability of close substitutes constitute a negative competitive force in an Industry. Those Industries which have no close substitutes are more attractive than those which have one or more of such substitutes. Thus firms in an Industry having no close substitutes can charge a higher price and earn better returns.

Rivalry Among Competitors

- Competition is normally a game in which one loses at the expense of the other. A move on the part of a player may cause other players to make countermoves or initiate efforts to protect themselves from the danger posed by the initial move. The desire to become the market leader or to corner a larger market share leads to rivalry among competitors. The extent of rivalry among competitors in an Industry affects the competition within that Industry. When the rivalry is weak it will lead to lesser competition and when the rivalry is high the level of competition is higher.

The dimensions of such rivalry among competitors are several. Some of the major ones are as follows:

- **Competitive Structure**

1. **Fragmented Structure**

- Large no. of Companies and none of them are in a position to dominate the Industry.
- Low entry barrier and less or no differentiation leading to products becoming commodities.
- Competition is intense

2.Consolidated Structure-Consists of a few large Companies or just one or two large firm. The intensity of competition may range from being unnoticeable to fierce rivalry.

- Diversity among competitors poses higher potential challenge to existing firms or new entrants.

- Demand Conditions
 - 1.High Demand Condition
 - 2.Stagnant Demand
 - 3.Declining Demand
- Exit Barriers
 - 1.Economic Factors, e.g. High Investment, High Retrenchment Cost, or High severance pay
 - 2.Strategic Factors
 - 3.Emotional Factors