

BU111 Midterm

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Five Forces - Competitors

- Rivalry among existing firms - who sells something very similar to you?
 - o Most powerful force
- Effects: price competition, lower volume, increased costs

Factors:

- Many competitors of equal size/capability
 - o If you're a big company you aren't worrying about competition as much as a company that is smaller
- Low industry growth rate/capacity of competitors:
 - o Rivalry isn't so bad, if the growth rate is low/small you will need to work very hard to attract customers (Example: reduce the price to attract customers)
 - o If companies are well below their capacity, if you can sell more than what you currently sell this reduces costs and gives you an incentive to chase more customers to sell more and produce more than what you are currently producing.
 - o Industry with low growth or capacity running very low: profitability declines
- Low consumer switching costs:
 - o Its easy for consumers to switch from one to the next (example switching shampoos). The rivalry in this industry is very hard and you need to work hard to keep the customers.
- Products are commodities or perishable:
 - o Doesn't matter what gas station you go to it's the same gas. How do you decide what gas station to pull into? You go to the cheapest one
Commodities compete on the basis of price therefore the lowest price wins.

- Exit Barriers:

- When its difficult to exit an industry, when you decide to sell the business, no one wants to buy it. If you cant leave it motivates you to stay and fight, you have businesses that are motivated to fight, this increases intensity and rivalry.

Solutions:

- By growing you reduce the rivalry because consumers know your product.
- Acquisition of competitors: the more competitors that you buy out the less completion you have.
- Create/increase consumer switching costs: Rewards cards (Starbucks, shoppers etc to buy the product to get rewards for it)
- Differentiation: Persuading consumers that there is no other competition like you. You try to differentiate with the product you are competing with.

Five Forces - Substitutes

- Products that do a similar job
- Effects: Creates price ceiling; increases marketing costs because you'll be spending money trying to get the consumers to buy your product and not the competitors.
- Many good substitutes:
 - The more choices consumers have the more likely they are able to make those choices, this reduces the price celining and makes it tougher for you to keep those consumers

Low switching costs:

- The easier it is for consumers to switch the harder it will be able for you to raise your prices.
- Solution:

High buyer propensity to substitute (likelihood):

- If you operate in an industry where people are easily persuaded to buy the substitute product. If people are willing to hunt for your product and go to another store that is a low propensity to substitute, and vice versa. You got to convince consumers not to substitute.

Solutions:

- Strong marketing/differentiation:
 - o You need to invest into strong marketing for example cars will advertise that you want original parts etc.
- Locking people in
 - o For example cable companies make you sign contracts so that you resist switching to streaming etc. When you make it difficult for consumers to switch it helps you.

Five Forces - Potential Entrants

- New and future competitors
- Effects:
 - Can cause big changes & intensify competition
 - The higher the barriers to entry the harder it is for other businesses to enter, this is good because once you are in, its harder for other rivalry to enter.

Lack of capital intensity— how much capital does it cost to start the businesses, or how big do you need to be to sell at a competitive price.

No specialized assets- Do you need patents? Do you need access to big networking distributors? For example when you go to a restaurant and they only have Pepsi and not coke, they have an exclusive agreement to sell that one product.

No regulations/govt. policy- Cant just decide your going to start a uni/bank

Low switching costs: In markets where consumers are passionate to certain brands because of the hassle of changing for example, they don't easily switch. This makes it hard for a new company to come in and attract these companies. If brand loyalty isn't such a big deal then when a new company enters that market it is easy for them to attract those customers.

Solutions: Grow to achieve scale (example Walmart makes it very hard for any other companies to come in and challenge them, example when Target came to Canada and then left)

Five Forces - Suppliers

- Who provides your key inputs?

Effects: Costs of inputs

Few suppliers: Your negotiating to attain your supplies. If suppliers charge you more than your profitability goes down. Their bargaining power goes up which increases the costs of your inputs because they have the upper hand.

Few good substitute suppliers/inputs: They have negotiating power over you

Porter's five forces looks at the competitive market and how it affects firms profitability.

High switching costs: If its going to be good for you to switch suppliers even if there is a lot of suppliers, who has the bargaining power? The supplier has the bargaining power. Therefore even if there is a lot of good suppliers, they know its not easy for you to switch, their bargaining power goes up which increases the cost of your inputs.

Threat of forward integration: The possibility or the likelihood of that supplier to then also become a competitor.

Solutions: ******Think about specifically which of these solutions might be options for addressing one of these factors and one you discover which are possibilities, what's the next step? (I'm just going to become my own internal supplier, what's the next thing you need to think about? Think about Diamond E******

Strategic Alliance: Joining businesses with another company that will not only help your business but help their business grow and increase profitability (example Starbucks and Chapters).

- Internal Supply: Being your own supplier you don't worry about high switching costs or threat of forward integration.
- Long run: Addresses first three factors
- *Compare each individual possible solution, which factors it might address why/how, and apply diamond e *
- Ex: Maybe you have the money to become your own internal supply but when relating it to management maybe you don't want your own internal supply when you can get the supplies at cheap, or what if their like what if we don't like strategic alliances because they have a possibility of not working out.
- Think deeply, think about a particular industry and an actual example

Five Forces - Buyers

- Who pays for your product?
Effects: Reduces price that you can demand; increases costs
- Few/concentrated buyers: If your trying to sell your product where there is very few buyers, who has the bargaining power? The buyers do , and their going to negotiate for lower prices. And as a result they will reduce the price you can charge.
- Discretionary purchase: Threatening to not need the product. When the buyers can say you can take it or leave it, I don't need what your selling, The buyers have the negotiating power therefore they drive your prices down.
- Standardized products: Not unique, for example cell phone chargers are standardized, most cell phone chargers for a specific phone use the same outputs, anyone else who is using the same product can share their charger with you. Not as many after market apple chargers. If it is a standardized product consumers don't need to buy a replacement they can just go get a cheaper one. Consumers have bargaining power, they can negotiate it down.
- Low switching costs: When it is easy for consumers to switch, they have the bargaining power, the first thing buyers will do is negotiate your price down.
Possible solutions:
 - Form alliance with other sellers(forming coalitions can be hard and illegal)(only usually legal in oil and gas where cartels are formed, or farm industry in Canada)
 - Strong marketing/differentiation: Trying to convince the buyers that your product is unique, addresses standardized product b/c trying to convince them its different, not a want it's a need.
Create switching costs,
 - Lock in customers: When you buy a game system, Keurig, type of razor, and the person gets frustrated, they will need to buy new games, buy a new game system, etc. This creates a high switching cost. They put their pricing low and competitive so when you purchase it and get locked in you are stuck buying more. Eliminates discretionary costs and standardized products, because you need that particular input.

Solutions:

Solutions.

- Form alliance with other sellers
- Strong marketing/ differentiation
- Create switching costs; lock in customers

Five Forces Models - Why?

- Predicts industry profitability
- Helps determine whether a firm should enter a particular industry
- Helps determine whether and/or how firm can carve out an attractive position in that industry