**Theme 2 :How competitive forces shape strategy –Michael Porter**

**Intro**

* The essence of strategy formulation is coping with competition.
* Five forces framework determines competition within and industry.

**1.Threat of Entry:**

* New entrants bring new capacity, desire to gain market share and substantial resources.
* Entry depends on barriers to entry, if they are high expect sharp retaliation.
  1. **Economics of scale-** large scale therefore low prices otherwise entrant will be at a cost disadvantage, can also act as hurdles for distribution, financing and nearly everything else.
  2. **Product differentiation-** Brand identification creates barrier as entrant has to spend heavy to overcome customer loyalty. Advertsinging, customer service,being first in industry and product difference create brand idenfification.
  3. **Capital requirements-** need to invest large financial resources to overcome barrier of entry, capital needed for infrastructure and absorbing losses
  4. **Cost disadvantage independent of size-** some companies may have an advantage from effects of learning curve(experience), access to raw material, assets at low prices,favourable locations or government subsidies.
  5. **Access to distribution channels-** entrant needs access to efficient cheap distribution channels. May have to create its own chanel.
  6. **Government policies-** government can limit or even foreclose entry to industries with licence requirements etc
* New entrants unlikely to enter if slow market growth, if incumbents have high capital or will slash prices.

**2.Supplier power:**

* Supplier is powerful if:
* Its dominated by a few companies and is more concentrated than industry it sells to.
* Product is unique or built up switching cost to a different supplier.
* It is not obliged to contend with other products for sale in industry.
* It poses credible threat of integrating forward to industrys business.
* Industry is not import customer of supplier group.

**3.Buyer Powerful:**

* Buyer powerful if:
* It is concentrated or purchases in large volumnes
* Products it purchases from industry are standard or undifferentiated.
* Products it purchases from industry form a component of its procut and represent a significant fraction of its cost
* It earns low profit, incentive to cut costs
* Industrys product is unimportant to quality of buyers produt
* Industry product does not save buyer money.
* Buyers pose a threat of integrating backward to make industrys product.
* Should pick buyers and sellers that pose least powerful influence on price

**4.Substitute products:**

* Substitutes limit the price an industry can charge for a product.
* To gain market share industry must differentiate its product.
* Substitute products that deserve most attention strategically are those that are subject to trends improving their price performance trade of with the indstrys product or are produced by industries earning high profits
* Sutstitutes come into play if competition increases.

**5.Jockeying for position:**

* Intense rivalry is related to the following factors:
  1. Competitors are numerous or equal in size and power
  2. Industry growth is slow, fights will outbreak for gain of market share.
  3. Product lacks differentiation or switching costs, locking buyers in
  4. Fixed costs are high or product is perishable, creating temptation to cut prices.
  5. Capacity is normally augmented in large increments.
  6. Exit barriers are high- keep companies operating even if profits are low
  7. The rivals are diverse in strategies, origins and personalities.
* As industry matures growth rate changes resulting in declineing profits and often a shake out.

**Formulation of strategy:**

* Identify the companies’ strengths and weaknesses from above factors.
* Can try to position company so that its capabilities provide best defence against competitive forces
* Or influencing the balcane of forces through strategic moves
* Or anticipating shifts in factors underlying the forces and respong to them.

**Positioning the company:**

* Strategy can be viewed as building defences against competitive forces or as finding positions in the industry where the forces are weakest.
* Knowledge of company’s capabilities and causes of competitive forces , highlight the areas where the company should confront competition and where to avoid it.
* Dr pepper, small concentrated producers, avoided largest selling drink segment and marketing heavily. **Barriers to entry** include brand identification, large scale marketing, and acess to bottler network. Maximised product differentiation by maintain a narrow line of beverages built around an unusual flavour. Also met pepsi and coke with an advertising onslaught- built brand idenfication.
* Must take the strategy that goes on offensive.

**Exploiting industry change:**

* Evolution brings about changes in sources of competition.
* Potential of industry will depend largely on shape of future barriers to entry, improvement of industrys postion and buyer,seller power.
* The key to growth/survival is to stake out a position that is less vulnerable to attack from head to head opponents whether established or new.
* Establishing such a postion takes many forms, solidifying relationships with favourable customers, differentiation product through marketing, integrating forward or backward or establishing technological leadership.