

Introduction to Management

Assignment No. 04

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**Porter’s Five Forces**

According to Porter, there are five forces within an industry:

* **Competitive Rivalry**

The first of Porter's Five Forces looks at the number and strength of your competitors. Consider how many rivals you have, who they are, and how the quality of their product compares with yours. In an industry where rivalry is intense, companies attract customers by cutting prices aggressively and launching high-impact marketing campaigns. This can make it easy for suppliers and buyers to go elsewhere if they feel that they're not getting a good deal from you.

**Example:**

If you were setting up a haulage business, you'd likely be entering a crowded market. You'd have to consider many potential rivals, how much they charged, and whether they were able to discount deeply. You'd also need to think about their resources: you might be setting up to compete with international logistics companies, as well as local competitors

* **Supplier Power:**

Supplier gain power if they can increase their prices easily, or reduce the quality of their product. If your suppliers are the only ones who can supply a particular service, then they have considerable supplier power. Even if you can switch suppliers, you need to consider how expensive it would be to do so.

The more suppliers you have to choose from, the easier it will be to switch to a cheaper alternative. But if there are fewer suppliers, and you rely heavily on them, the stronger their position – and their ability to charge you more. This can impact your profitability, for example, if you're forced into expensive contracts.

**Example:**

Let's say your business idea was to manufacture electronic devices. You'd have to assess your supply options for a range of specialist components. If one supplier dominated the components market, then they could raise their prices without worrying about their own competitors. This might affect the viability of your product.

* **Buyer Power**

If the number of buyers is low compared to the number of suppliers in an industry, then they have what's known as "buyer power." This means they may find it easy to switch to new, cheaper competitors, which can ultimately drive down prices. Think about how many buyers you have. Consider the size of their orders, how much it would cost them to switch to a rival.

When you deal with only a few savvy customers, they have more power. But if you have many customers and little competition, buyer power decreases.

**Example:**

Buyer power is a significant factor in food retail. Think of large supermarkets that operate in a crowded, highly competitive market. This market has changed dramatically with the arrival of cheap, no-frills food discounters. Shoppers have strong buyer power here. That's why supermarkets have coupon schemes, loyalty cards, and aggressive discounting – to capture the largest share of buyers.

* **Threat of Substitution:**

This refers to the likelihood of your customers finding a different way of doing what you do. It could be cheaper, or better, or both. The threat of substitution rises when customers find it easy to switch to another product, or when a new and desirable product enters the market unexpectedly.

**Example:**

If your organization makes medical instruments, you may find your position being threatened by the rise of 3D printing. This enables instruments to be made from a wide range of materials, sometimes at a fraction of the cost of traditional methods. If a competitor gets it right, it can weaken your position and threaten your profitability.

* **Threat of New Entry:**

Your position can be affected by potential rivals' ability to enter your market. If it takes little money and effort to enter your market and compete effectively, or if you have little protection for your key technologies, then rivals can quickly enter your market and weaken your position.

However, if you have strong and durable barriers to entry, then you can preserve a favorable position and take fair advantage of it. These barriers can include complex distribution networks, high starting capital costs, and difficulties in finding suppliers who are not already committed to competitors.

**Example:**

Even industries that seem to be well protected against new entry can prove to be vulnerable. For many years, high-volume air travel was in the hands of a relatively small number of established airlines. The barriers to entry were formidable. Start-up costs were high, routes and take-off slots were mostly grabbed by the big operators, and the industry was strictly regulated.