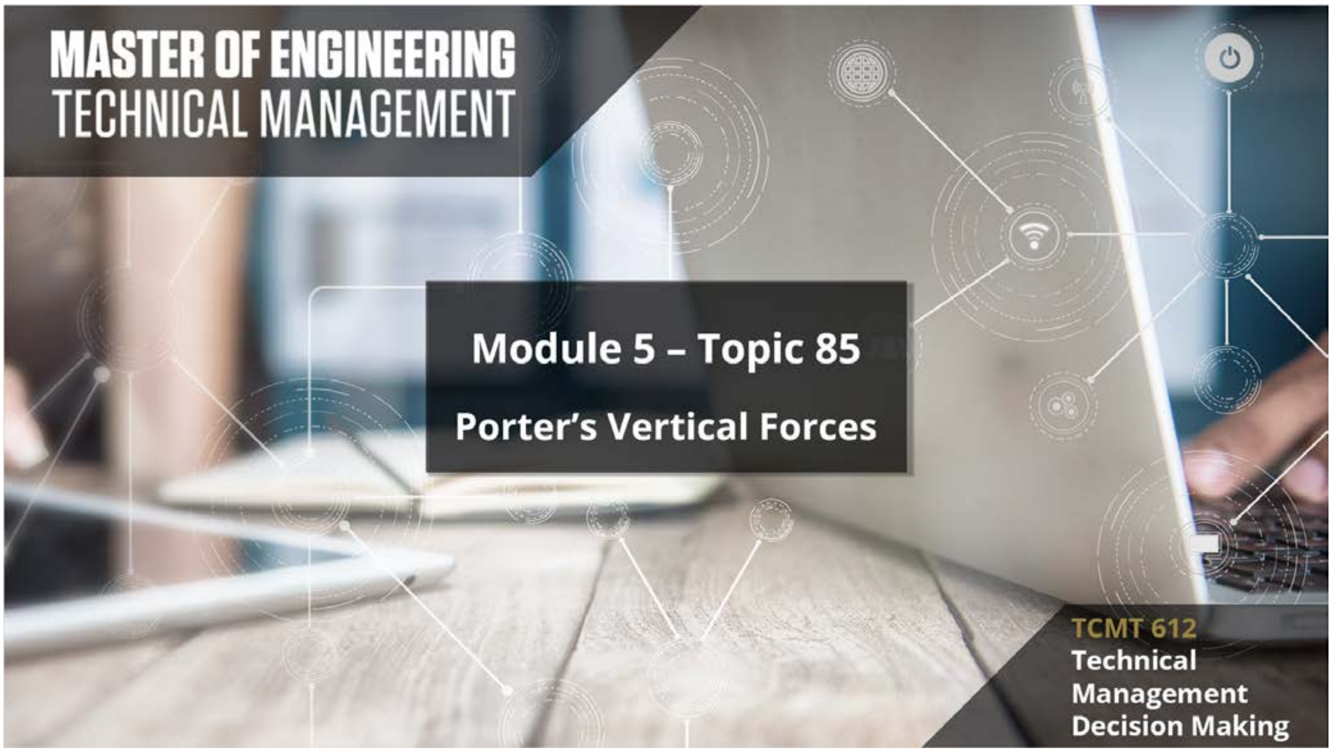
TCMT612_05M_085T_Porter-vertical-forces

1. Main

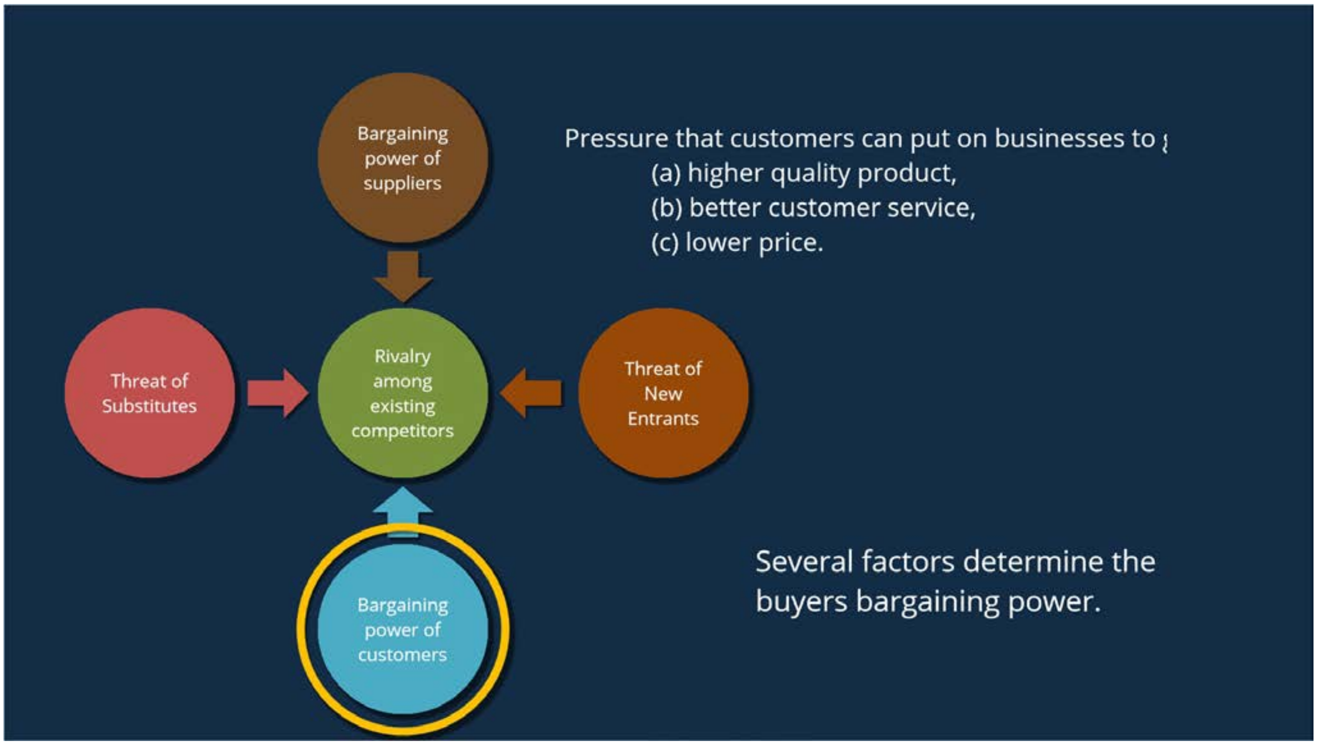
1.2 Topic title



Notes:

In this topic the professor describes Porter's vertical forces: bargaining power of buyers and bargaining power of suppliers.

1.3 Buyers



Notes:

Bargaining power of buyers.

Buyers' bargaining power refers to the pressure customers can put on businesses to get them to provide higher quality product, better customer service, and lower price. According to the Five Force Analysis framework, buyers' power is one of the forces that shape the competitive structure of an industry.

Several factors determine the buyers' bargaining power.

1.4 Factor #1

Notes:

First, obviously large volume buyers are particularly strong force in the industry that requires high fixed cost.

The long-term, large volume orders raise the stakes to keep the production capacity filled.

Some examples are the large volume purchase of refining and bulk chemical industries.

The buyer of bulk chemical is very powerful in the industry.

1.5 Factor #2

Notes:

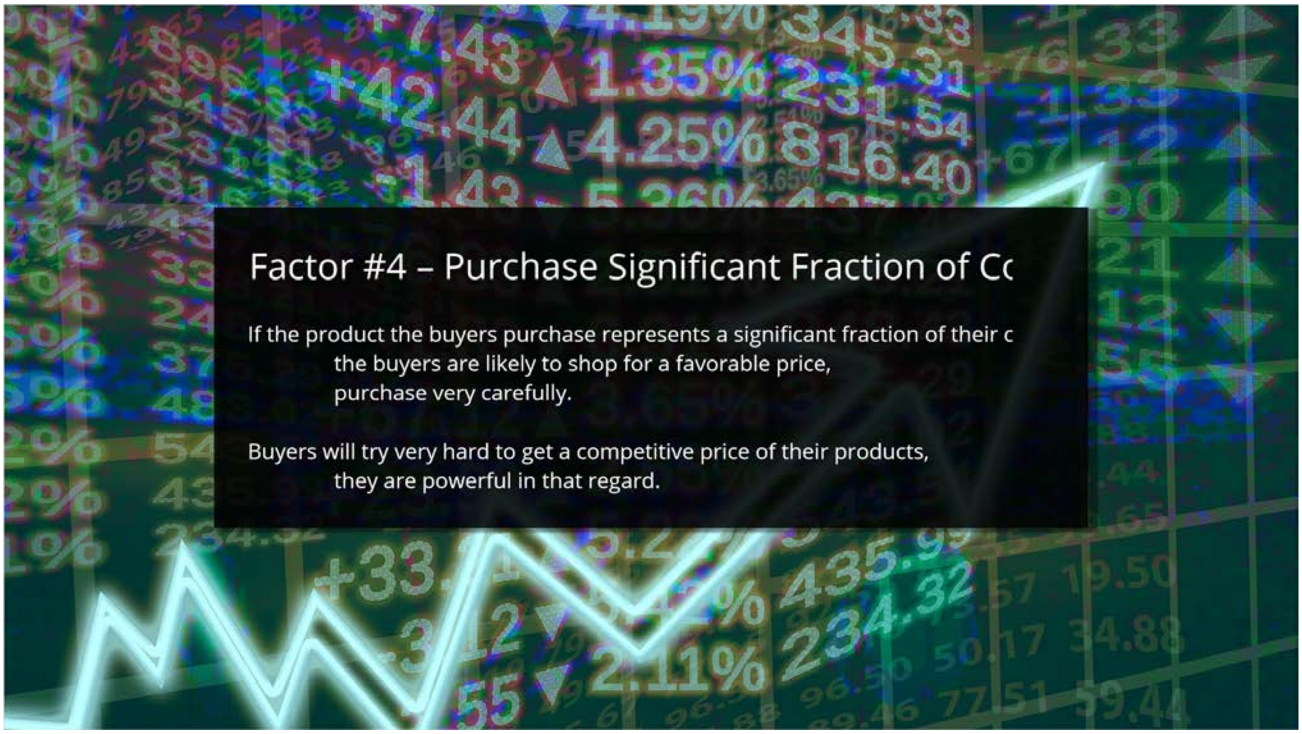
The second, if switching costs are low, the bargaining power of buyers is high because the buyers have more freedom to switch from one product to the other.

1.6 Factor 3

Notes:

The Third: The buyers of standard or undifferentiated products have more power because buyers can play one company against another. The buyers of commodity products are powerful.

1.7 Factor #4

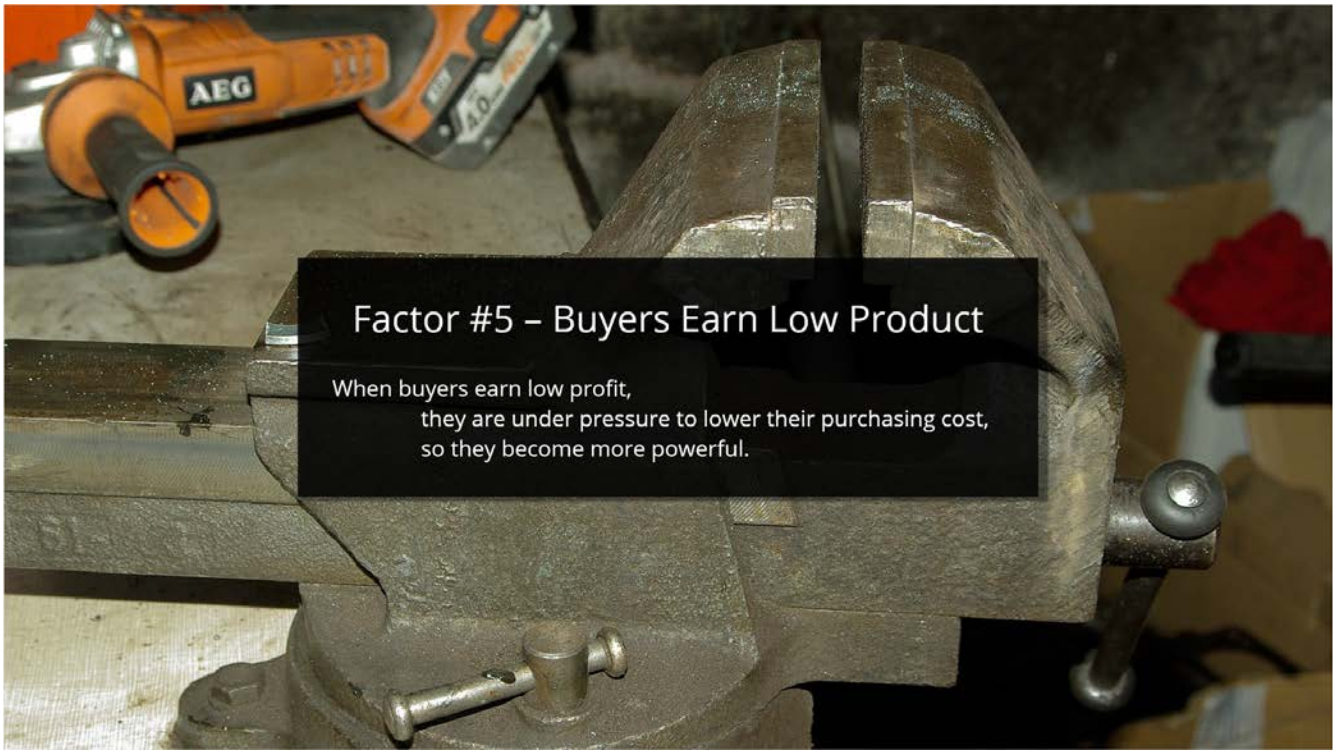


Notes:

Fourth, if the product the buyers purchase represents a significant fraction of their cost, the buyers are likely to shop for a favorable price and they purchase very carefully.

The buyers will try very hard to get a competitive price of their products, and they are powerful in that regard.

1.8 Factor #5



Notes:

The fifth factor is that when buyers earn low profit, they are under pressure to lower their purchasing cost, so they become more powerful.

1.9 Factor #6

Notes:

Six: When the quality of buyers' product is very much affected by the industry's product, buyers are generally less price sensitive.

For example, the oil field operators may be less sensitive to the price of critical equipments because the malfunction of those equipment leads to large losses.

The other example is in the healthcare industry.

The medical instrument manufacturers are less price sensitive to the enclosure type of equipment because the quality of enclosure can influence the users' impression about the quality of equipment inside, and those medical device manufacturers want to pay for the enclosures of high quality.

1.10 Factor #7

Notes:

The seventh factor: when the buyers of a product have the capability to backward integrate the parts, the buyers of those parts have more bargaining power.

For example, in the auto industry those major automakers always threat to make the part themselves when negotiating with the part suppliers about the price and quality of parts.

1.11 Summary buyers

Notes:

In summary, the buyers of a product can be more powerful than the sellers of the product if buyers have more options and sellers have less options.

1.12 Suppliers

Notes:

Suppliers can also exert bargaining power by raising prices or reducing the quality of products.

Powerful suppliers can squeeze the profit out of an industry.

1.13 Factor #1

Notes:

A supplier group is powerful if the market is dominated by a few companies, and if suppliers' industry is more concentrated than the industry that purchases the products from the suppliers.
For example, the airplane industry.

There are only two companies, Boeing and Airbus.

They dominate the whole aircraft industry and there are more buyers.

All the major airlines purchase airplanes from one of those two companies.

So, the suppliers of airplanes are very powerful.

1.14 Factor #2

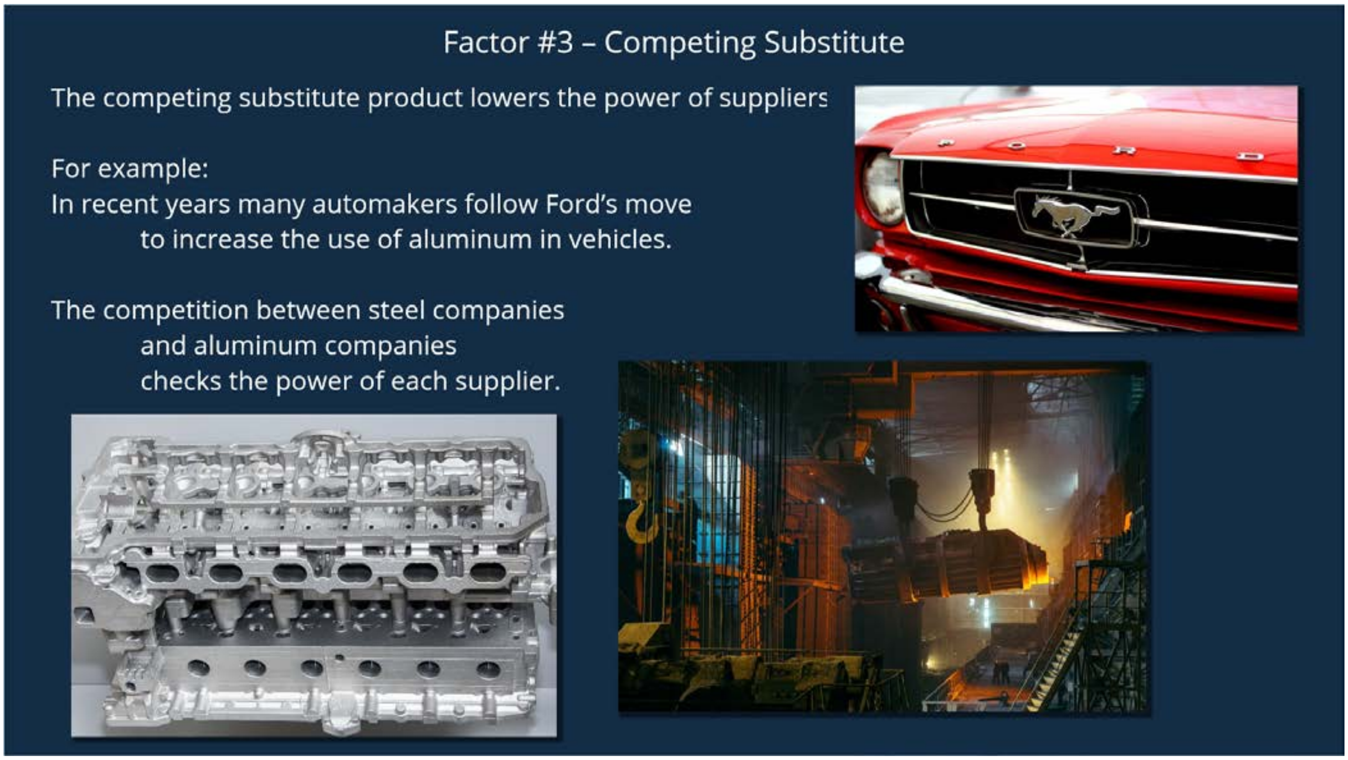
Notes:

The second, is, if a suppliers product is unique or at least differentiated, its customers will incur significant switching cost as a result of changing their product.

Powerful suppliers strategically build up switching cost to strengthen its competitive advantage.

Some examples are: the engineering software providers, the accounting software providers, and some critical equipment providers.

1.15 Factor #3



Notes:

The third factor affecting suppliers' power is the competing substitute.

The competing substitute product lowers the power of suppliers.

For example, in recent years many automakers follow Ford's move to increase the use of aluminum in vehicles.

The competition between steel companies and aluminum companies checks the power of each supplier.

1.16 Factor #4

Notes:

The fourth factor: suppliers also can threat to forward integrate an industry's product.

This kind of forward integration happened a lot in the semiconductor and recently smartphone industries.

The part suppliers learned how to design the cell phone, how to design a semiconductor chip, and they make the cellphone product and chip themselves.

Samsung used to be a supplier of Apple's iPhone parts, the battery and also the screen.

And Samsung quickly learned how to make cell phones and then to introduce new cell phones to compete with Apple.