

Factors that can influence the strength of each of the Five Forces

Threat of new entrants

The ease with which a new business can enter the market is affected by:

- **Economies of scale**

Economies of scale occur where efficient production requires large-scale operation and, hence, funding. It might be possible for a company to enter at a smaller scale, but this is likely to be costly and/or less effective.

- **Product differentiation**

Creating a brand identity that differentiates a product or service from the competition and encourages loyalty can help to create a barrier for others. Brands that enter the market earlier are often perceived to have an advantage.

- **Capital requirements**

The need to invest large financial resources in order to enter the market can create a barrier.

- **Switching costs**

If it is likely to cost customers to switch suppliers, then it is more difficult for new entrants to gain sufficient business.

- **Access to distribution channels**

An inability to gain access to distribution channels can be a major barrier. Existing partnership between retailers and wholesalers can make it difficult for new entrants. The internet, however, has provided many companies with an easily accessible 'virtual shopfront'.

- **Legal and regulatory barriers**

The imposition by governments of regulations and the granting of licences or patents can act as a barrier.

- **Expected retaliation from existing businesses**

Businesses may try to prevent companies entering the market by dramatically reducing their prices to the point where it is not viable for new entrants to compete. When existing companies make announcements about new products well in advance of launch the potential market for new entrants can also be reduced.

Intensity of rivalry

The strength of the competition between firms already in the industry is affected by:

- **Rate of industry growth**

Rivalry may depend upon life stage of industry and whether or not the market is growing fast.

- **Number of competitors and the balance between them**

The more competitors there are the greater the competition tends to be. The intensity of rivalry can also be greater when the industry is dominated by a few large firms.

- **Diversity of competitors**

The nature and strength of the competition may depend on whether or not all competitors are in the same core business. The key activities of the businesses and the existence of alliances or partnerships will also have an impact.

- **Differentiation of rival products/services**

If there are no clear differentiations between the products/services offered, then the competition is likely to be more intense.

- **Switching costs**

If it is likely to cost customers to switch suppliers, competition may be avoided, or conversely, it may be particularly intense (customers will need to be offered many more incentives to switch).

- **Excess capacity and exit barriers**

If there is excess capacity and exit costs are so high that they make exit difficult, rivalry will be intense.

- **Brand equity**

Some brands in the market may have a higher perceived value than others.

- **Level of advertising expenditure**

Some businesses in the market may have access to greater financial resources to spend on advertising.

Bargaining power of buyers

The relative strength of buyers is affected by:

- **Size and concentration of buyers relative to suppliers**

Bargaining power will be influenced by whether it is the buyers or the suppliers in the industry who are more powerful. The number of buyers and the alliances between them will be significant, as will the number of purchases each buyer makes.

- **Buyers' price sensitivity**

Buyers will be stronger if they are able to negotiate prices.

- **Product differentiation**

If some products are more attractive than others then the strength of the buyers will be reduced. If all products are equally acceptable, the strength of the buyers will be greater.

- **Switching costs**

If it is likely to cost buyers to switch suppliers, then their strength will be reduced.

- **Information**

The greater the access that buyers have to information about products and other suppliers, the greater their strength will be.

Bargaining power of suppliers

The relative strength of suppliers is affected by:

- **Number of suppliers**

The power of suppliers will be greatest when there are few suppliers for buyers to choose from.

- **Differentiation of suppliers' products**

If the products offered by suppliers are very different from each other, some suppliers may have an advantage over others.

- **Switching costs**

If it is likely to cost customers to switch suppliers, then the power of suppliers will be greater.

- **Forward integration**

If there are strong alliances between some buyers and some suppliers, then the relative strength of the remaining suppliers will be less.

- **Importance of volume to supplier**

If suppliers are reliant on one, or only a very few, buyers then their strength will be less.

- **Cost of supplies relative to selling price of product**

The margin between the cost of the components and the selling price of the product will impact on the strength of the suppliers.

Threat of substitution

The threat of comparable products will depend upon:

- **Existence of close substitutes**

Substitute products are more common in some industries than in others.

- **Switching costs**

The greater the cost to customers to switch to a substitute product the less the threat of substitution.

- **Perceived level of product differentiation**

People are less likely to switch to an alternative product if they think that it would be difficult to replicate all the features of the original product.

- **Buyers' propensity to substitute**

Customers in some markets are more likely to remain loyal to a product or service. In other markets customer loyalty is rare.