

B. COM. - SEMESTER - VI [6]

→ SOFT SKILL

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— BUSINESS INFORMATION ANALYSIS
(Eng. Med.)

CHAPTER'S INTRODUCTION

The word 'Industry' is used for the units performing the same type of activities. E.g. 'Textile industry' term is used for different mills manufacturing Cloth, for different units manufacturing paper, the term 'Paper Industry' is used. Before selecting any industry for the purpose of business activity, its analysis from the different angles is necessary.

While entering in the industry and for the existence, business has to face different challenges. If analysis is not done regarding this, it will be difficult for any business unit to remain in the competition.

1. ANALYSIS OF COMPETATIVE FORCES (MICHAEL PORTER'S MODEL)

Q. 1. Write short note on : Model of competitive forces in Industry analysis.

(G. U. April-2003)

★ Examine the forces that shape industry in competition. Comment on the major barriers to entry in industry. (G. Uni. April 97)

★ Explain the five factors of Michael Porter in industry analysis.

(G. Uni. April 98)

★ Explain Porter's five forces model for analyzing competitive environment of an Industry. (G. Uni. April 2001)

★ Write Short note on 'Michael Porters Competitive Strategy Model.

1. **Introduction :** The unit which does not consider the competitors, cannot remain for a long time in the market. The customers do not increase to a large extent in the market. So the total demand is almost steady, but the number of competitors fluctuates. Weak competitors cannot stay in the market. On the other side the new competitors enter in the market with new strategies. To enter in the market and to be steady in it is not easy. If the new entrepreneurs are not acquainted with the dealers, customers, alternative products and other controls and hurdles of the market, they will fail to get proper return on their capital investment and will be forced towards bankruptcy. Due to this, with the idea of competitive position in the market weightage is given to framing a proper business strategy. For this, first of all it becomes most important to study the competitive factors.

2. **Competitive forces** : To start any business, the executives have to face some competitive factors. Professor **Michael Porter** (Harvard University) has mentioned five factors as follows :

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|------------------------|----------------------------|
| (A) Threat of entry | (D) Substitute products |
| (B) Powerful suppliers | (E) Jockeying for position |
| (C) Powerful customers | |

Before framing a strategy, the executives must collect the information about the changes occurring and taking place in the five factors mentioned above. In context to these changes what will be the position of the unit, must be estimated after making this analysis. If the strategy is formed, the chances of the success of the business increase. The extent to which the logical analysis of competitive factors is done, to that extent the capacity of the unit to face the competitors of the unit will increase. Not only that but also the profitability will increase continuously. The analysis of five factors affecting the business by **Michael Porter** is as follows:

[A] **Threat of entry** : It is not easy to enter the market with any type of product. The reason is that the product of the new unit is not so much familiar and to make it famous the new unit has to give advertisement continuously. Due to the entry of new business unit the share of the market demand is divided, the competition of attracting the production resources also increases. Due to this, the expert companies create the hurdles to stop the new units from getting the entry into the market, which are as follows :

(1) **Huge capital requirement** : To start the new business, fixed capital for the fixed assets, working capital for liquid assets and for establishment large scale investment is required. Hence, the small units get afraid of entering the market. Foods industry, oceanic research, aeroplane and strip manufacturing industries require a large scale capital investment and due to this the competitors in these fields are very limited.

(2) **Big size of the unit** : The size of the business unit is planned from three point of views : (1) Small size units (2) Large size units (3) Medium size units.

Normally, in the small scale units the new competitors enter in notable number. In medium size units also there are notable number of new competitors entering the market. But for large scale units, the new competitors are very limited. The unit producing the entertainment products and units requiring the latest technology have a very large size in comparison with the other units and this matter makes the entry of new competitors very limited.

(3) **Product speciality** : When the customers accept the particular qualities of the product, the producers also supply the products of the same quality under a particular brand. In these circumstances, the brand oriented customers' group goes on increasing. Through the advertisements customers are continuously inspired to purchase a particular branded product with good qualities. In these circumstances, for the new competitors it becomes very difficult to make an entry in the market with the same type of product. e.g. Taj Brand Tea, Vicks Balm, Rasna soft drinks, Thums up, Coca-Cola, MRF and Ceat Tyres etc.

(4) **Strong channel of distribution** : When the producers have a strong holding on retailers and wholesalers, they are not ready to keep the products of new producers in

their stores. They are even not attracted by the special commission or other attractions like the old business relations with the business units, reputation, facilities, after sales service etc. The businessmen are unable to leave the producers easily. In these circumstances, the chances of the entry of new competitors decreases.

(5) **The lowest cost of production :** As the business unit is older, its experience is more varied and wide. These types of units can decrease the cost of the product to a great extent on the basis of their experience of using raw-materials, fuel and other material nearly economically and by taking special benefits of technology. Besides this, by making production on a large scale also the per unit cost can be decreased. The price at which they are sell their products in the market, at that cost the other units are just able to produce the product. In these circumstances the very low cost restricts the new units to enter the market.

(6) **Research and development expenses :** The business in which the continuous altertness and development are required, less competitors enter. The research and development expenses are at a large scale normally and small scale units are unable to bear such expenses. In the business of computers, electronic items and engineering products based on the advanced technology, there is a huge amount of expense on the research and development. Hence, very limited number of new units enter the market.

(7) **Business combinations :** When there are limited competitors in the business, they take the decisions for production, price or sale unitedly with internal understanding. These types of combinations are famous as Cartels, Gentlemen agreement etc. Due to these types of combinations the entry of the new competitors is restricted and the units which are the members of these combinations enjoy the monopoly or semimonopoly. However, due to these combinations the customers are exploited. That's -why many countries have put controls on them.

(8) **Patent, Trade Mark and Copyright Act :** To encourage the founderers of the new inventions, their inventions are given monopoly for particular number of years (i.e. 10 years to 14 years) through the Patent Act by the government. In the same way under the Trademark and Copyright Act, the trademark, original literature and artistic articles are given protection. As a result in such areas the competitors are unable to enter.

(9) **Government policy :** On one side the government encourages through industrial policies so that in village areas some industries can develop. On other side in the public interest it also makes the provisions to acquire compulsory license to start the business for some particular type of industries. According to the present industrial policy the industries like iron and steel, cement, sugar, medicines, transportation, concentrated chemicals etc. need the licence compulsorily. However, in new policies, the control on them has become liberal. But the number of competitors are limited, where the license is to be acquired on a compulsory basis.

(B) **Powerful suppliers :** Whatever transactions take place between traders and customers about products and services, holding party can make a transaction according to its own terms and condition's. In the situation of monopoly, the limited number of traders have the stock of goods. In other words they hold control on supply. On the other side, there are number of customers. In these circumstances there are full chances with the traders to

get a high price of their goods. In this situation as the traders have a hold on the market, it is known as seller market. The monopolists exploit the customers by increasing the prices, by holding the stocks and creating scarcity, decreasing the quality of the product or by price fluctuations or distribution fluctuations.

If the raw-materials, which are needed by the producer for producing the product are available on a very high price from their traders, cost of production will increase and it will decrease their profit margin. If the market of this product is full of competition, the producer is unable to increase the price of the product and as a result his profit goes down or he even makes loss. In these circumstances, to get protection the executives can form the following strategies :

(1) If the producers are limited in number, by forming the association they can get their demands satisfied through collective bargaining with their traders. (2) An agreement can be made for the whole year with the traders for the raw-materials e.g. For producing the icecream an agreement is done for supply of ice and salt for the whole year. (3) If any item is needed on a large scale and if its production is easy, instead of purchasing it from the traders it must be produced by the company itself. (4) The alternative must be found out for the raw- materials which are to be used.

If the industries have a hold over their own traders, through bargaining or controlling the supply or by increasing the price they can increase their profit. If the demand for industrial products can be increased, by increasing the capital investment the profitability can be increased by increasing the production and sale.

(C) Powerful customers : When there is perfect competition in the market, there are several purchasers and vendors. In this position the customers have full control over the market. By the following way the customers exercise their control :

(1) When the fixed expenses in the industry are in large proportion and if the big customers are very limited, they have a control. (2) When the industries produce a product by assembling the various parts and if they purchase a small part whose price is very less and if it plays a very small part in the total cost of the product, the purchasing of such part can be done by their own terms and conditions. (3) When the quality is not important in the product, to purchase such product, the customer can put a pressure on the traders. (4) When the quality is important for the customers, even on a high price they force the producers to maintain a good quality. (5) When by purchasing the material such product is to be produced on which the profit margin is very less and it is of daily use, the customers expect a low price. (6) If the product is copied and if the producer is unable to create a change in it by brand or by any other way, on the market of such product the customer's hold is more. (7) If the customer is in a position to use the substitute product, he can have a control over the producer.

In short, when the customers are in a position of getting a hold on the traders, they can demand for decreasing the price, improving the quality, increase the production and get the after sales services.

(D) Substitute products : If the product produced by the company, substitute in the market has such unit is unable to get a high price of its product. So the profitability of the unit decreases and due to this its development is also restricted. If the executives decrease the quality or increase the price, the customers will go for the substitute products. In this situation the executives can charge high price by attracting the customers towards their product by making the changes in the quality, by its effective advertisement and by creating the product differentiation. More development, more diversification etc. strategies are also successful in these situations.

(E) Jockeying for position : The units doing the same type of activity are known as industries. e.g. Belapur Paper Mills, Rainbow Paper Co., Orient Paper Co., Shirpur Paper Ltd., Crystle Paper Ltd. etc. companies producing paper are said to be Paper Industry. The demand of all the units of this industry is for same type of raw-materials and machinery. The traders who have these demands, are under a situation of great competition. To compete in this situation, all the businessman mostly accept the idea of price competition, quality maintenance, variations in products, advertisement etc.

In the competition existing among the competitors, every businessman forms mainly the following strategies ;

(1) Efforts to increase the market share : Generally, the total demand of the industry is not much increased. The demand of a product mainly depends on the population and substitute products. As the extent to which they will increase, to that extent the demand will also increase. On the other side, the businessmen make the efforts for pulling the share of other businessmen to their own side.

(2) Effect of the brand : Where the customers give more importance to the brand, it becomes very difficult for a businessman to increase his market share.

(3) Control over expenses : By keeping the control over various expenses the businessman can form the strategy of decreasing price by decreasing the cost.

(4) Equilibrium between demand and supply : For the production of raw-materials, the strategy of maintaining the equilibrium between the demand and supply can be balanced by making maximum use of production capacity.

(5) Business on less profit : Instead of quitting the market, all the businessmen maintain their existence in the situation of competition by earning less profit, even incurring a very nominal loss for their faithful existing customers.

(6) Restricting the entry of new competitors : There is always an increase in the number of competitors. But there is no increase in the demand. As a result the strategy is formed to restrict the new competitors.

(7) More than one strategy : To maintain the existence in the market against the competitors, all the competitors form more than one strategy to maintain their equilibrium in the market.

3. Conclusion : The extent to which the introduction and analysis of the competitive factors is done in a logical manner, to that extent the work of forming proper business strategies becomes simple and effective for executives. To collect the information about these factors, the matters to be considered are the published reports of the companies,

magazines about business matters, business reviews, industrial policies of the government, export-import and tax policies, patents and trademarks, laws, licence rules, current agriculture flows, customers, traders etc.

2. FORMULATION OF STRATEGY BASE

Q. 2. Which type of strategy should be adopted by the business units in the context of competitive forces suggested by Michael Porter.

- ★ How do competitive force shape strategy ? Explain the formation of Strategy.
- ★ Explain, what type of strategy should be adopted by a business unit, in respect of competitive forces, as mentioned by Michael Porter. And also explain the advantages of analysis of competitive forces.
- ★ Discuss formulation of strategy, describing how competitive forces give shape to the strategy. (N. Guj. Uni. April 2000)

1. Introduction : Prof. Michael Porter has submitted concept of analysis of industry, for formulation of business strategy. This analysis has been proved more useful for process of business planning and decision. Five factors of Mr. Michael Porter give a perfect guidance in respect of, how to survive in business competition. Company's comprehensive condition can be known, in competition, by evaluating weaknesses and capabilities of formulator of the strategy in respect of analysis of competitive factors of business competitors. Management can, strategically, think of various problems of product, keeping factors, which are obstacles in the market competition. For this, preference is given to formulate effective strategy, in respect of weaknesses of competitors and strategy of increasing capability for survival against competitors.

2. Competitive forces suggested by Michael Porter : Prof. Michael Porter of Howard University has shown five competitive forces, as under. Strategy should be formulated keeping them into account.

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|-----------------------------------|---|
| (1) Threats of new entrants | (4) Threat of substitute product or services. |
| (2) Bargaining power of customers | (5) Jockeying among current suppliers. |
| (3) Bargaining power of suppliers | |

Unit can maintain its own position, in competition, if strategy is formulated, by making analysis of above stated five forces and observing changes therein. Total demand of the product, manufactured by various units involved altogether in the industry means total demand in the industry. Increase or decrease in the demand is result of competitive factors. If, enough care of such forces is not take it may happen that some units may shut down or some may become weak, whereas other side, there may be considerable increase in the demand of units, which are aware of such forces.

3. Formulation of strategy in respect of competitive forces : Various types of the following strategies can be formulated, keeping internal strength and weaknesses of industry, in respect of competitive forces, into consideration.

- (A) Positioning the company
- (B) Influencing the balance in respect of environment.
- (C) Exploiting the maximum benefits of changes.

(A) Positioning the company : It is very important, strategically, where to put our unit, within various units involved in the industry. Following factors should be taken into account, for this.

(1) Strengths of the company : Company's capabilities in respect of production, sales, research, economical, administration, co-ordination and control etc., have important role in positioning the company.

(2) Weaknesses of the company : Weaknesses of resources, administrative, environmental, co-ordination and control, employees, etc., in the company are obstructive in ascertaining foremost position of the company.

(3) Competitive forces : In competitive forces, price of competitors, quality of product, experience and prestige of competitors, market strategy are matters affecting positioning. If company possesses all these competitive forces in its favour, company would achieve decided foremost position, in comparison to its competitors. Company can adopt following two strategies, for this. – (a) Defensive strategy and (b) Aggressive strategy.

(a) Defensive strategy : Some managerial personnel select to be away from competition, when it is felt that opposing of business competitors, is risky. When management does not desire to be competitive in the market, strategy adopted at that time is known as defensive strategy.

(b) Aggressive strategy : When company has special ability in some matter and to attract large clients of the industry, an extraordinary strategy adopted by the company, is known as aggressive strategy. Generally, such companies prefer to attract clients, by keeping either rates of their product at lower side, or quality of the product kept extraordinary.

(B) Influencing the balance of environment : An industrial unit can influence balance with the environment, when there is any change, in the environment, affecting business activities. In such a case after observing suitable necessary changes in the internal matters a strategy can be framed. Management controls production activities as required, by backward or forward integration. Control on adverse effects of changes in the environment, can be done through process of merger and also by maintaining inter relationship among present units. Management should accept process of influencing balance of environment, not as an event, but as competing company. For this, after analyzing environment, as required, name of the brand of unit to be made popular, changes in the media of advertisement, various plans for sales promotion to be adopted and planning of product development. are adopted. Influencing balance in changed environment and satisfaction to the client is possible. only when necessary changes, in the strategy of production and sales promotion programmes are made according to the habits, fashion, taste of clients in changing environmental factors.

(C) Exploiting the maximum benefits of changes : Development of industry, at the regular intervals, therefore, is known as process of evolution. Generally, industry develops on increase in demand and increase in demand is related to increase in population. India holds second position in the world, in the matter of the population. On increasing the population, demand of products such as of cement, steel, sugar, fertilizers, chemicals,

medicines, electricity, transport service, information and tele-communication, education is increasing and on account of it, such industries are developing. Effects of changes in competitive forces, also fall on production cycle. On account of this, there will be considerable changes in stages of development. Rate of production and development increases. Under such circumstances, some new products enter in the market, whereas certain products fall down in terms of demand. Management should take steps, strategically, as shown under, to get maximum advantages of changes in the environment.

(1) **To make new things** : In respect of changes in the business environment, management should make planning for new products. Such steps are known as product planning. New product should be prepared, keeping concept in mind that it will satisfy new requirement of the customers in respect of new environment. Research and development department of the unit, is required to undertake special efforts and experiments for this.

(2) **Product development plan** : When current product is introduced in the market, in the new form, after making necessary changes, it is called as product development. Product development plans should be implemented, keeping suggestions and complaints of the customers into account, to take maximum benefits out of changes in the industry.

(3) **Horizontal combination** : Industries, which are not able to survive on account of the changes in business environment, are doing horizontal combination. It means, units of similar category and nature are combined with each other and make efforts to take benefit of large-scale production.

(4) **Vertical integration** : Many units accept vertical integration, to take benefits of changes in the industry. Units joined in it are dependent on each other, on standing form. Due to this, they perform manufacturing activities independently. But their sales are made to units, which are dependent on them. Under the circumstances, size of the unit is enlarging, and therefore, entry of new units becomes difficult. If units are weak, either they join to it or they go out of competition.

(5) **Product enrichment** : It is necessary to make efforts for enrichment of current product, according to changes in the industry. If no product enrichment is adopted according to new changes and competitors, it will be difficult to survive such product.

(6) **Product simplification** : Sometimes, due to environmental changes, there may be increase in production cost. Under the circumstances, some avoidable processes of production are removed, without any compromise in quality of the product. This is called a concept of product simplification.

(7) **To develop difference in the brand** : Management should develop the brand according to the changes in the environment, and this should be communicated for the knowledge of the customers, through effective advertisement campaign. In the changed environment, benefit of difference in the brand can be obtained. Strategies of Surf and Super Surf, Colgate and Herbal Colgate, Pepsodent and New Pepsodent are notable examples of brand difference.

(8) **New technology** : Market benefit can be obtained, by accepting new technology, according to new environment. For this, matter of required capital investment,

skilled labour etc, should be taken into account. This can be achieved through long-term strategy.

Above stated various steps are necessary on account of changes in the competitive forces. According to development at regular interval of the industry, changes in the profitability and in the rate of return on invested capital are affected. Therefore, it is necessary to examine the probability of the profitability, before affecting any changes according to changes in the environment.

4. Conclusion : It will be easy for any business unit to survive in the business competition, if strategy is formulated, keeping competitive forces into consideration. Moreover, effective bargaining with supplier of the materials can be done and at other side benefit of bargaining power of the customers can be obtained. In short, study of the competitive forces can be beneficial for increase of total demand of the product and to strengthen one's position among competitors.

3. ADVANTAGES AND LIMITATIONS OF ANALYSIS OF COMPETATIVE FORCES

Q. 3. Explain in details advantages the business unit gains through making the analysis of competitive forces. Explain limitations of the analysis of the competitive forces.

1. Introduction : If profitable business opportunities are to be snatched, return on capital investment is to be increased; considerable increase in productivity is to be made through optimum use of the production resources and new markets are to be developed, it is necessary to make analysis of the competitive forces. Mr. Michael Porter has pointed out five competitive forces. Among these, what threats are to be resisted for new entrant business units and study of the customers' and suppliers' bargaining power etc. are useful for the business units at various angles.

2. Advantages of the analysis of competitive forces : Unit will gain various following advantages, on analyzing of competitive forces.

(1) Awareness of position of the industry : It can be known through competitive forces how much positive or negative effects are made to industry by such forces. Due to this, what would be position of the industry can be known, in respect of various alternate conditions.

(2) Approximation of capacity of the suppliers : What would be effects on abilities of the suppliers in respect of new circumstances, can be known. On account of this, estimation can be done whether sufficient supply would be available in future and accordingly proper strategy would be adopted.

(3) For entry in new market : It can be ascertained, that entry in the new market would be how much easy or adverse, through competitive forces. If new changes in the forces are such, which attract new entrepreneurs, entry in the new market with new product would be obstructive.

(4) Intensity of competition : Main object of analysis of the competitive forces is to maintain balance of business unit, after getting estimate of intensity of the competition. On account

of new changes, new entrepreneurs enter the market, and on other side changes are necessary in current technology, otherwise it is difficult to survive for the business unit in current period.

(5) **Estimate of purchase power of the customers :** Customer is king of the market. But according to changes in competitive forces, there will be certain effects on the purchase power. Under the circumstances, it will be easy to forecast the capability of the customer to shoulder the financial burden.

(6) **For consequences in sales :** Pre-thinking can be undertaken for what and which changes in sales would be required to be effected and how much increase in sales expenses would be required to be made, in context of changes in competitive forces, and accordingly strategies would be framed.

(7) **For brand difference :** A decision taken in respect of brand difference would be beneficial, in view of competitive forces and accordingly brand strategy can be adopted in changed new position.

(8) **For development of technology :** Management can take proper decision about degree to which new technology would be beneficial. For this, pre-thinking can also be undertaken for problems of technicians and their training. To balance with new condition of the industry, development of technology is necessary.

(9) **Benefit of size of the unit :** The decision about the size of the business unit is important for survival against competitive forces. Large sized units have special advantages alongwith certain limitations. Management can think of this problem in strategic manner.

(10) **Strategy of diversification :** Production diversification would be necessary. To implement the same additional capital would be required. Due to this, there will be change in rate of return on capital investment, matters Management can take strategic decisions on these matters.

4. **Limitations of the analysis of competitive forces :** Analysis of the competitive forces is beneficial at various angles. But to get benefits of it, it is necessary to know its limitations. These limitations can be stated as under.

(1) **Changes in the factors :** Various factors, which affect business viz. supply of materials, number of the competitors, capacity of competitors, fashion of the customers, sales organisation etc. would be usefully considered if there is steadiness in such factors. In fact, factors which affect business, do not remain steady, So strategic benefits are difficult to avail. Therefore, it is necessary to continue evaluation of factors constantly.

(2) **Lack of reliable information :** Proper analysis of the competitive factors can be done only when information received for each factor is reliable. Generally, information related to these factors is received through questionnaire, through reports or from industrial magazine or institutions. Such information should be examined for its completeness and authenticity. Most of the units do not submit complete or true information to keep secrecy of their industry and due to this, analysis done through such information does not remain truly guiding.

(3) **Negative approach :** The approach of the management, while analyzing competitive forces is important. If analysis were done with negative approach, profitable business opportunities also would be felt to be ordinary. If it is felt that it is difficult to enter

the new market because of transportation problem the decision to leave it, is not proper. If new market is profitable, positive thinking can be done to enter in the new market, through transportation services of private resources.

(4) **Natural factors** : Sometimes, analysis of forces becomes useless, due to natural uncertainty. While analyzing forces, management should have made some information of natural factors. But if circumstances of excessive rain or absence of rain arise, earthquake or any natural calamities happen, analysis of other forces would not be useful.

(5) **Trade cycle** : In economy, trade cycles can be seen. If there are unexpected changes in the trade cycle, information obtained through analysis of forces, will be useless. These factors create favorable or adverse effects on the purchase power of the customers. And on account of this, there will be uncertainty in the demand, which makes strategic plans unsuccessful.

(6) **Changes in the government policies** : When there is change in the export-import policy, industrial policy, foreign exchange policy, tax policy etc. of the government, information arrived out of analysis of forces will not be much important. It is also difficult to estimate for government policies in advance, because in certain matters government also keeps secrecy. Moreover, in case of change in the government, there may be changes in the policies, and it makes strategies unsuccessful.

(7) **Legal Restrictions** : Sometimes, adequate advantages of analysis of forces are not available on account of legal restrictions. Restrictions on number of partners in partnership, restrictions on capital in company's form, restrictions of borrowed capital, labour laws restrictions etc. are kept into account and strategic decisions are taken. And therefore, management does not get benefit of environment analysis adequately.

2. **Conclusion** : Management has particular importance, at the angle of the strategy, of the analysis of strategic forces shown by *Mr. Michael Porter*. Management can take proper decisions in respect of their own capabilities and weaknesses, and will survive through adopting a specific strategy against competitive forces. Management may survive in the competition, not only that, it may get maximum return on the investment, by adopting a certain strategy, keeping into account the new changes in environment.



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