Michael Porter’s Five Forces Model

LEARNING OBJECTIVES

After examining this chapter, readers will have the ability to:

- Understand that intense competition and rivalry characterize the healthcare industry.
- Realize that healthcare entities are required to possess a deep understanding of their competitors to best position themselves for marketplace success.
- Recognize that competition is multidimensional, existing on multiple fronts, and that each front must be understood if marketing success is to be achieved.
- Realize that the nature of competition in any industry is based on five forces: existing competitors, potential entrants, substitutes, suppliers, and buyers.
- Appreciate the value of Michael Porter’s Five Forces Model as a tool for understanding and addressing competition in the healthcare marketplace.

INTRODUCTION

The healthcare marketplace is characterized by intense competition and rivalry—elements that will only intensify as healthcare entities of all kinds vie for the opportunity to serve target markets. Those entities that can
successfully navigate the complex healthcare environment will be handsomely rewarded with increased market share and prosperity.

Successful navigation of this environment, of course, requires a deep understanding of marketplace competitors. All too often, however, entities view their competitive environment in an overly narrow fashion that fails to acknowledge the true depth and breadth of competitive forces in the marketplace. Competition is multidimensional, and its vastness must be clearly understood if marketing success is to be achieved. The critical task of accurately identifying the competitive elements in a market is greatly facilitated by Michael Porter’s Five Forces Model.

Illustrated in Figure 28-1, Porter’s Five Forces Model provides useful insights into the multifaceted nature of competition. According to Porter, the nature of competition in any industry is based on five forces: existing competitors, potential entrants, substitutes, suppliers, and buyers.

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FIGURE 28-1 Porter’s Five Forces Model
These forces are unique to each industry—and industry segment—and combine to determine the competitive intensity and ultimate potential of associated markets. These five forces are explained as follows.

**EXISTING COMPETITORS**

Existing competitors are the most obvious competitive force, jockeying for position through new product development, innovative promotional campaigns, and so on. Rivalry among existing competitors is especially intense when competitors are numerous and fairly equivalent in terms of size and power, when exit barriers are high, and when industry growth is slow resulting in struggles for market share. These characteristics are frequently observed in the healthcare marketplace, illustrating the intense rivalry within the industry.

**POTENTIAL ENTRANTS**

Entities that might potentially enter the market represent significant threats to existing competitors. New entrants bring new capacity and resources to the market along with desires for market share. The magnitude of the threat posed by new entrants is largely based on the particular barriers to entry that exist. Typical examples of entry barriers include capital requirements, proprietary product differences, government policy, and the market dominance and brand identity of existing competitors. Significant entry barriers yield significant protection from the threat of new entrants, while few barriers increase the competitive nature of the market. Certificates of need possessed by hospitals and patent protection possessed by pharmaceutical firms are examples of barriers that offer substantial protection in the healthcare marketplace.

**SUBSTITUTES**

Substitutes are products that differ from particular offerings but largely, and sometimes completely, fill equivalent wants and needs. As a result, substitute offerings can greatly impact the performance of healthcare entities and even threaten their very existence. Laser vision correction could be viewed...
as a substitute for eyeglasses and contact lenses. The services of a chiropractor could be viewed as a substitute for the services of an orthopedic surgeon. The seriousness of the threat of substitutes is predominantly based on their performance and price characteristics. Substitutes that offer equal or better performance pose significant threats, especially when price advantages exist.

**SUPPLIERS**

Suppliers provide the components necessary for healthcare organizations to offer goods and services to their customers. Surgery scalpels, pharmaceuticals, hospital beds, and diagnostic imaging equipment represent just a few of the many products that healthcare entities purchase from suppliers. Without these "raw materials," healthcare entities could not function. This dependence on suppliers poses a significant threat to healthcare entities.

Suppliers can raise their prices, lower the quality of the components that they provide, or simply go out of business—all situations that can yield potentially devastating effects. Suppliers are particularly powerful if they are few in number, if few substitutes exist, and if entities are not key customers.

**BUYERS**

Porter's term *buyers* is equivalent to the term *customers*, which is better suited for the healthcare marketplace. Quite obviously, customers possess significant bargaining power over healthcare entities because their patronage ultimately determines institutional survival, growth, and prosperity. The array of customers in the healthcare marketplace is quite varied, including residents in nursing home beds, patients in hospital beds, patrons at local pharmacies, recipients of home health services, and even health insurance companies and other third-party payer entities that pay for medical services on behalf of clients. Without customers, operations cease. For this reason, marketers must ensure that all marketing efforts are customer focused. Importantly, marketers must strive to accurately assess the wants and needs of customers and serve them in a manner that will meet and exceed their expectations.
OPERATIONAL MATTERS

Porter’s Five Forces Model is highly useful in that it clearly illustrates the multidimensional nature of marketplace competition. Its use, however, can greatly be extended through the assembly and completion of a Five Forces Worksheet. Marketers simply (1) identify the product offering to be evaluated, (2) construct the Five Forces Worksheet, as illustrated in Figure 28-2, (3) identify existing competitors, potential entrants, substitutes, suppliers, and buyers, and (4) place the identified current and potential competitors on the diagram accordingly. When completed, the Five Forces Worksheet clearly identifies all five competitive forces that entities currently face or could potentially face, as illustrated in Figure 28-3. Completion of this simple, yet highly effective, device yields considerable insights into the current...

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**FIGURE 28-2** A Five Forces Worksheet
CHAPTER 28 MICHAEL PORTER'S FIVE FORCES MODEL

POTENTIAL ENTRANTS
- National chain considering market
- Local hospital considering opening retail pharmacy
- Unknown retail start-ups
- Unknown Internet/mail-order start-ups

SUPPLIERS
- Durable medical equipment firms (2)
- Pharmaceutical manufacturers (2)
- Pharmaceutical wholesalers (3)
- General wholesalers (4)
- Computer systems firms (2)
- Office equipment suppliers (4)

INDUSTRY COMPETITORS
- Retail pharmacies — chain (5)
- Retail pharmacies — independent (2)
- Retail pharmacies — hospital owned/operated (1)
- Internet/mail-order pharmacies (10+)

BUYERS
- City and county residents/visitors
- Local hospitals (2)
- Local nursing homes (3)
- Area medical clinics (7)
- Public third-party payers (2)
- Private third-party payers (7)

SUBSTITUTES
- Herbal remedies
- Folk remedies
- Samples from physician office visits
- Abstaining from treatment (i.e., letting "time" heal headaches, colds, etc.)

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FIGURE 28-3 A Retail Pharmacy’s Five Forces Worksheet

and future competitive marketplace and hence serves as an essential marketing planning tool.

SUMMARY

By clearly illustrating the true depth and breadth of the competitive environment, Porter’s Five Forces Model serves as an indispensable resource for marketers. With this information, healthcare marketers can establish strategic and tactical priorities and position their organizations to capitalize on opportunities and avoid or eliminate threats. Ideally, healthcare marketers will address each of the five forces. By properly addressing the complete competitive environment, healthcare marketers are better prepared to meet and exceed market share and related performance objectives.
EXERCISES

1. Define and comprehensively discuss Michael Porter's Five Forces Model, providing insights regarding its uses, features, methods of interpretation, and value, accompanied by an appropriate illustration. Be sure to include in your discussion an overview of the instrument's importance as a strategic marketing device in the healthcare industry.

2. Select a healthcare entity of your choice for placement in your local market and assign the hypothetical establishment an appropriate brand name. Consult a variety of information sources (e.g., telephone directories, the Internet, industry databases) in an effort to identify entities occupying associated categories of competition listed in Michael Porter's Five Forces Model, preparing an appropriate illustration accordingly. Based on your Five Forces Model, what have you learned about the depth and breadth of competition in the marketplace?

REFERENCE