Strategies in Response to Porter's Competitive Forces in Electronic Commerce

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Abstract

E-Commerce or Electronic Commerce refers to use of the Internet to conduct business transactions. The amount of trade conducted electronically has grown extraordinarily since the spread of the Internet. E-Commerce is fundamentally changing the economy and the way business is conducted. E-Commerce forces companies to adopt new strategies to expand the markets in which they compete, to attract and retain customers by tailoring products and services to their needs, and to restructure their business processes to deliver products and services more efficiently and effectively. As businesses shift their focus from building a customer base to increasing revenue growth and profitability, companies should re-evaluate their current business strategies, if any, and develop new strategies that provide a clear path to success. This paper focuses on McCarthy's four Marketing Mix model and Porter's five competitive forces model for understanding strategies adopted by Internet companies that respond to the five competitive forces and thereby achieve a competitive advantage over others.

Key Words: E-Commerce, E-Business, Marketing Mix, Competitive Forces.

Introduction

The emergence of E-commerce is creating fundamental changes to the way business is conducted. The E-Commerce Industry has come a long way since its early days. The market has matured and new players have entered the market space. E -commerce includes not only buying and selling goods over Internet, but also various business processes within individual organizations that support the goal. Electronic Commerce refers to a wide range of online business activities for products and services. It also pertains to any form of business transaction in which the parties interact electronically rather than by physical exchanges or direct physical contact. To deal with, the competition is the most important essence of today's business. The organization's growth and profitability primarily depends upon how effectively organization deals with the competitor's strategies, products, cost and profit level etc. McCarthy's (1960) four marketing mix model and Porter's (1980, 1985) five competitive forces model helps to identify strategies for facing five competitive forces in thereby achieve a competitive advantage and provide significant new insights into the development and implementation of e-business strategies that contribute to increased profit.

Research Objectives

To understand the strategies that can be derived from the four marketing mix responding to the five competitive forces and thereby brings a competitive advantage to E-Commerce Industry.

Methodology

Secondary sources including books, research papers and journals are used for the purpose of study.

Background

McCarthy's Four Marketing Mix Model

The marketing mix (also known as the 4 Ps) is a foundation model in marketing. The marketing mix has been defined as the set of marketing tools that the firm uses to pursue its marketing objectives in order to sustain in the marketing for long run. It refers to four broad levels of marketing decision, namely: product, price, promotion, and place. Edmund Jerome McCarthy was an American marketing professor and author. He proposed the concept of the 4 Ps marketing mix in 1960. According to McCarthy (1960) and Perreault and McCarthy (1999), a firm develops its marketing strategies by first identifying the target market for its products or services. It then develops a marketing mix—a particular combination of product, price, promotion, and place (i.e., distribution and delivery functions in the supply chain) designed to enhance sales to the target market. A unique mix of these elements in a given industry allows firms to compete more effectively, thus ensuring profitability and sustainability. For example, by coordinating various product offerings and associated price discriminations with sales promotions and effective logistics, a firm can increase its sales and profit. Since the Internet has a significant impact on the makeup of this marketing mix, Internet companies should develop strategies that take the unique nature of online marketing into account.The marketing 4Ps comprises of following (Van Waterschoot, W., & Van den Bulte, C 1992).

Product – The first of the Four Ps of marketing is product.A product is an item that is built or produced to satisfy the needs of a certain group of people. It is important for marketers to reinvent their products to stimulate more demand once it reaches the sales decline phase.

Price –Price of the product is basically the amount that a customer pays for to enjoy it. Price is a very important component of the marketing mix as it determines firm's profit and survival.

Place -Place decisions outline where the product is sold and how it is delivered to the market .The goal of business executives is to get their products in front of the consumers who are most likely to buy them.

Promotion- Promotion includes advertising, public relations and promotional strategy. This tie into the other three Ps of the marketing mix as promoting a product shows consumers why they need it and why they should be willing to pay a certain price for it.

Porter's Five Competitive Forces Model

Michael Porter provided a framework that models an industry as being influenced by five forces. According to Porter (1980, 1985) and Porter and Millar (1985), a firm develops its business strategies in order to obtain competitive advantage in terms of increased profit over its competitors. It does this by responding to five primary forces: (1) the threat of new entrants, (2) rivalry among existing firms within an industry, (3) the threat of substitute products/services, (4) the bargaining power of suppliers, and (5) the bargaining power of buyers. A company assesses these five competitive forces , then tries to develop the market at those points where the forces are weak (Porter 1979). For example, if the company is a low-cost producer, it may choose powerful buyers and sell them only products not vulnerable from substitutes. The company positions itself so as to be least vulnerable to competitive forces while exploiting its unique advantage (cost leadership). A company can also achieve competitive advantage by altering the competitive forces. The five competitive forces model provides a solid base for developing business strategies that generate strategic opportunities. Since the Internet dramatically affects these competitive forces, E- Commerce companies should take these forces into account when formulating their strategies. Porter (2001) remphasized the importance of analyzing the five competitive forces in developing strategies for competitive advantage.Following are the Porter's five forces of competition analysis (Karagiannopoulos et.al. 2005):

I. Bargaining Power of Suppliers

The term 'suppliers' comprises all sources for inputs that are needed in order to provide goods or services. Supplier bargaining power is likely to be high when:

The market is dominated by a few large suppliers rather than a fragmented source of supply.

There are no substitutes for the particular input.

The supplier's customers are fragmented, so their bargaining power is low.

II. Bargaining Power of Customers

The bargaining power of customers determines how much customers can impose pressure on margins and volumes.Customers bargaining power is likely to be high when:

They buy large in volume, there is a concentration of buyers.

The product is undifferentiated and can be replaced by substitutes.

Switching to an alternative product is relatively simple and is not related to high costs.

Customers have low margins and are price-sensitive.

The customer knows about the production costs of the product.

III. Threat of New Entrants

The competition in any industry is higher, the easier it is for other companies to enter into this industry. In such a situation, new entrants could change major determinants of the market environment (e.g. market shares, prices, customer loyalty) at any time. There is always a latent pressure for reaction and adjustment for existing players in this industry. The threat of new entries will depend on the extent to which there are barriers to entry. These are typically:

Economies of scale (minimum size requirements for profitable operations).

High initial investments and fixed costs.

Cost advantages of existing players due to experience curve effects of operation with fully depreciated assets.

Brand loyalty of customers.

Scarcity of important resources, e.g. qualified expert staff.

IV. Threat of Substitutes

A threat from substitutes exists if there are alternative products with lower prices of better performance parameters for the same purpose. They could potentially attract a significant proportion of market volume and hence reduce the potential sales volume for existing players. This category also relates to complementary products. Similarly to the threat of new entrants, the treat of substitutes is determined by factors like

Brand loyalty of customers

Close customer relationships

Switching costs for customers

The relative price for performance of substitutes

Current trends.

V. Competitive Rivalry between Existing Players

This force describes the intensity of competition between existing players in an industry. High competitive pressure results in pressure on prices, margins, and hence, on profitability for every single company in the industry. Competition between existing players is likely to be high when:

There are many players of about the same size.

Players have similar strategies.

There is not much differentiation between players and their products; hence, there is much price competition.

Impact of the Internet on Marketing Mix and Competitive Forces

The Internet can dramatically lower entry barriers for new competitors. Companies can enter into E-commerce easily because they do not need sales forces and huge capital investments as they do in offline markets. As the number of people with Internet access increases, the competition for online business in many industries will also increase.

The Internet also brings many more companies into competition with one another by expanding geographic markets (Porter 2001). The Internet changes the basis of competition by radically altering product/service offerings and the cost structure of firms (e.g., cost reductions in production, distribution, and transaction). The Internet also changes the balance of power in relationships with buyers and suppliers by increasing or decreasing the switching costs of these buyers and suppliers. By reducing customers' search costs, the Internet makes price comparison easy for customers, and thus increases price competition (Bakos 1998). The price competition resulting from lowered customer search costs increases rivalry among existing competitors reduces switching costs of customers, and thereby shifts bargaining power to customers.

The Internet creates new substitution threats by enabling new approaches to meeting customer needs and performing business functions (Porter 2001). The Internet also facilitates an electronic integration of the supply chain activities, achieving efficient distribution and delivery. It also facilitates partnerships or strategic alliances by networking partners or allies.

E-Business Strategies for Competitive Advantage Responding to Five Competitive Forces

This section considers the impact of the Internet on marketing mix and competitive forces, and suggests strategies for achieving a competitive advantage.

Product Strategy

On the Internet, consumers can easily collect information about products or services without travelling to stores to inspect products and compare prices. In the offline market researching about the product can be extremely expensive and time consuming. As a result, consumers rely on suppliers and retailers to aid them in the search, and the suppliers and retailers take advantage of this situation by charging higher prices (Allen and Fjermestad 2000). Consumers end up paying more and often not getting the product they really wanted. However, in E-Commerce Market, a complete search of product offerings is possible at virtually no cost. Because consumers can easily compare prices and find close substitutes, companies are forced to lower prices. Companies cannot achieve competitive advantage simply by exploiting consumers as in physical market. An alternative is for companies to make consumers' product comparison more difficult by differentiating their products from others. Possible competitive product related strategies are:

Product bundling: Product bundling promotes the benefits of the whole package, thus keeping buyers from comparing individual items.

Innovation or the Introduction of Niche products:A niche product can be defined as product that is made and marketed for use in a small and specialized but profitable market that counteracts the threat of product substitutes, new entrants into the market, and competition among existing firms. By using the direct access to consumers enabled by the Internet, companies can collect information, identify target consumers, and better introduce products or services to meet consumers' needs. Companies can also collect information on new products desired by small segments of the market. By creating products that meet the needs of consumers in the niche markets which focus on specific product, companies can command higher prices (Sinha 2000).

Customer-centric strategy: Another strategy associated with niche products or innovation is customer-centric strategy. Compared to a product-centric strategy, which pushes products to consumers, customer-centric strategy pulls information from consumers to improve and customize products(Viehland 2000).

Expansion into aRelated Product Line: An expansion into related product lines can also be a good strategy. According to Porter (1987), the expansion into related product lines can exploit transfer of skills or sharing of activities such as promotion and distribution, which will lead to competitive advantage. Sharing can lower costs by achieving economies of scale and effectively utilizing company resources such as market information, managerial or technical expertise, and knowledge. Like traditional companies, Internet companies can also expand their product line into areas related to their existing product lines.

Price Strategy

The Internet enables consumers to compare prices, products, and services across suppliers. For example, by logging on to price-comparison sites like Pricescan.com and shopping agents like Bottomdollar.com, consumers can readily compare the prices and features of more than 10,000 products available on the Web (Sinha 2000). This leads to increased price competition and lowers the prices of products or services. According to Bakos (1998), lower search costs for price and product offerings in Internet marketplaces promote price competition among sellers. TheInternet thus significantly affects competition, and intensive price competition can eliminate sellers' profits. To overcome these threats, companies have to employ appropriate pricing strategies for selling products over the Internet which are mentioned below:

•**Price Discrimination Strategy**: Price discrimination is a microeconomic pricing strategy where identical or largely similar goods or services are transacted at different prices by the same provider in different markets. Sinha (2000) suggests two strategies for price discrimination: price lining and smart pricing. Price lining refers to the practice of offering the same products or services at various price points to meet different customers' needs. Smart pricing refers to the practice of charging various prices from market to market, depending on market conditions and differences in how customers value the product. Bakos and Brynjolfsson (1997) points that bundling can also be thought of as a type of price discrimination as it reduces the heterogeneity of choices facing consumers and thus their willingness to pay for individual items.

•**Cost Leadership strategy**: Cost leadership is a concept developed by Michael Porter and utilized in business strategy. It describes a way to establish the competitive advantage. Basically it means the lowest cost of operation in the industry. Companies can also protect profits by achieving cost leadership in a particular market or industry. If sellers cannot price discriminate, the lowest price sellers can charge as cost of production. As competition intensifies, companies may have to lower their production costs to protect profits.

Promotion Strategy

To manage e-brands effectively and efficiently, companies have to employ promotion strategies different from those used by traditional marketing.

Customer-Centric Promotion Strategy (Customer RelationshipMarketing): The concept of relationship marketing was first coined by Leonard Berry in 1983 which means attracting, maintaining and enhancing customer relationships within organizations. It allows companies to provide customers with information about their products, collect information about their customers, and engage in data mining. They can then customize products to meet customer needs and offer promotions tailored to specific customer groups. This process helps build a base of loyal and profitable customers (Sealey 2000). The Internet encourages companies to employ this marketing based on direct, personalized relationships with customers. As consumers become proficient at using the Internet, they will only buy products that precisely match their needs. Thus, companies must formulate customer-centric promotion strategies that respond to this new customer power.

•**Viral Marketing strategy**: Viral Marketing is a technique that uses a company's best customers to promote the product. Viral Marketing is a strategy that relies on word-of-mouth to carry a marketing message to a rapidly-growing number of people. When people share a message with others and the recipients share with more people, it can cause a chain reaction which leads to an exponential growth of communication. In order to devise a successful viral marketing campaign, an e-commerce company must know their audience, engage viewer emotions and make content easy to share.

Place Strategy

Place strategy plays a fundamental role in the marketing mix of a product or service. The place aspects of the marketing mix are closely related to the distribution and delivery of products or services. The Internet and its associated application software have significantly changed the way company's products or services are delivered by reducing transaction and distribution costs. One way for companies to differentiate their products from rival companies is faster and more efficient delivery of products to their customers. One of the sources of Dell's initial competitive advantage can be attributed to its famous direct selling and build-to-order approach. Just-in-time (JIT) strategy allowed the company to operate with the lowest inventory level in the industry. Dell works on customer driven strategies by collaborating with customers to find ways to make technology work for them (Bakos 1998). Strategy related to faster and more efficient delivery is integration of online and offline businesses (clicks-and-mortar strategy) which is discussed below:

Clicks and Mortar Strategy (Biyalogorsky, E., &Naik, P. 2003)

Click and mortar is a type of business model that includes both online and offline operations, which typically include a website and a physical store. A click-and-mortar company can offer customers the benefits of fast online transactions or traditional face-to-face service. It is an Integration of Online and Offline Businesses.

The Clicks and Mortar model enables companies to build up competitive advantages because of the following aspects:

Lower costs: By integrating virtual and physical channels internal and external efficiencies can be improved by saving labour and delivering costs.

Improved trust: Click-and-mortar firms can achieve a competitive advantage over Web-based stores regarding the trust of customers. Because there is a physical location where customers have a direct contact person and a direct address where they can return products, they perceive less risk.

Differentiation through value-added services: Value-added services can be offered in terms of content integration, information integration as well as logistic integration without necessarily increasing costs.

Content integration refers to pre-purchase services like offering information about the product. Integrated information systems allow customers to locate the nearest store and check inventory. Logistic integration of the channels allows the customer to choose the channel through which he picks up and returns the product.

Geographic and Product Market Extension: The Clicks and Mortar approach enables companies to extend its market reach as well as its product across geographical boundaries.

Conclusion

Every business needs to survive and develop appropriate strategies to implement them. In the field of E-Commerce in developing the current competitive climate requires more appropriate marketing strategies to develop and promote. McCarthy's four marketing mix model and Porter's five forces model and serve as a tool for making decisions for gaining competitive advantage by adopting marketing strategies that are very useful in business. These models are studied to understand the strategies which are likely to bring a competitive advantage to Internet companies. By understanding the impact of the Internet on marketing mix and competitive forces, e-business managers can adopt appropriate strategies for meeting the unique challenges of e-business. The E-commerce industry will be faced with challenges as it matures but there is potential for growth owing to rising internet users and advancement in technology. Companies will need to work harder to provide better service to customer as more companies will be foraying in commerce business in future. So there is need for E-commerce industry to adopt good marketing strategies in reaction to various competition forces which are increasing with increased number of players in E- Commerce industry.

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