

THE MODEL OF THE FIVE COMPETITIVE FORCES ON ROMANIAN RETAIL MARKET

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ABSTRACT: *The paper is about the model of the five competitive forces of Michael Porter. In the first part, I have presented the theoretical aspects of the model and after that, I tried to apply the model on the retail market in Romania. I used data gathered from national and international institutes of market research and also from the information offered by the main retailers on their web sites. The retail market in our country is not very good crystalized, but has had a good evolution in the last years. The competition is intense, the barriers are relatively high, the power of national suppliers is diminished by the integration of Romania in European Union, the power of consumers is moderate and the substitutes appear as discount stores and e-retailing.*

KEY WORDS: *retail; Porter; Romania; competition; market*

JEL CLASSIFICATION: *M19, M39*

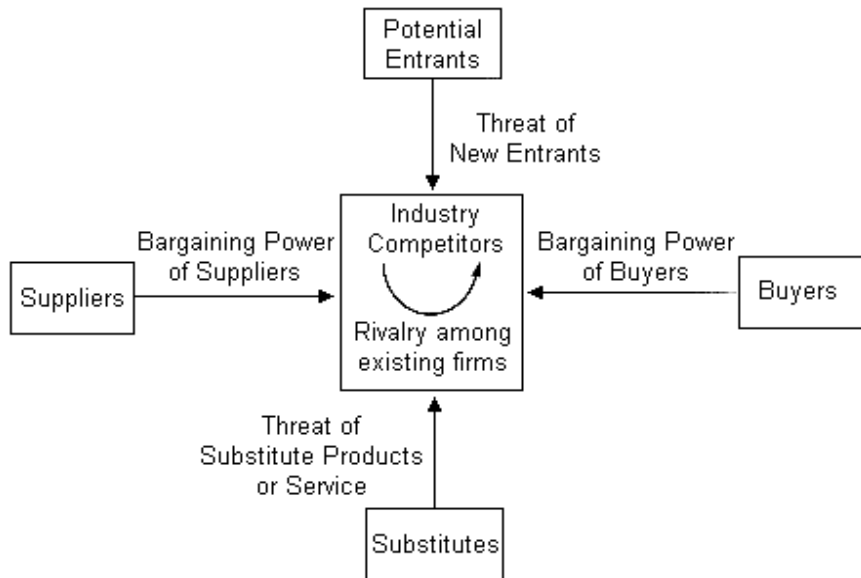
1. THE THEORETICAL BACKGROUND OF THE FIVE COMPETITIVE FORCES MODEL OF MICHAEL PORTER

Michael Porter (1980) considers that rivalry (competition) on the market is result of the five variables or main forces: rivalry level, bargaining power of customers and that of suppliers, the threat of new entrants and of substitute products. These variables are interconnected. They are illustrated in the matrix of the five competitive forces of Porter (figure 1).

Level of rivalry among existing firms characterize the intensity of competition in a particular industry to fill a specific market segment and is determined by factors such as number, diversity of competitors and the relative strength of them, the extent to which industry can be defined as young or mature (growth prospects are limited in a mature industry, leading to increased competition among participants and

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the difficulty in maintaining market share), high fixed costs, low product differentiation, major strategic stakes in industry, higher barriers to exit the sector, etc..



Source: Porter, M., (1980), *Competitive strategy*, The Free Press, New York

Figure 1. Forces determining competition in a sector

To competitive pressure, the company must adopt a strategy aimed at two objectives: increasing competitive pressure that they exert (increasing its size and market share through a strategy of growth) and reduce the competitive pressures that bear (in distinction its products from those of competitors). There are industries in which firms meet their niches and segments of customers, calling the strategy Live and Let Live (live and let others live). But there are branches in which regular practice and the suppression of any move is sanctioned competitive (e.g. electronics). Suppression is by pricing and quality and game theory requires that applications need to find optimal strategies.

Bargaining power of buyers. Buyers affect an industry through their ability to force lower prices, negotiate a better or more services and to determine competitors against each other (Wheelen & Hunger, 2000). For a company, buyers may be the final consumers of products or companies distributing products in stores. Bratianu (2000) believes they may be considered as a force and that, as a threat, if they demand the lowering of sales prices or request a growth company producing quality products and services, leading to increased costs. When buyers are a weak force, the producing company may increase prices and thus can obtain higher profits.

According to Porter (1980), a buyer or group of buyers will be hard if you find one of the situations: buying a lot of buyer's product or service, is able to integrate upstream, causing the good one; suppliers are numerous because the product is standard and undifferentiated, very little switching costs, the acquired product represents a substantial part of the buyer's costs, which creates a desire to seek a lower

price, the buyer has a low income and is thus very sensitive to cost and service differences, the product purchased is immaterial in terms of quality and price, and thus can easily be replaced. A group of buyers is low when producers threaten downstream integration, conversion costs are very high because the products are not standardized or buyers are fragmented and have no particular influence on product or price.

Bargaining power of suppliers. Power suppliers of firms in an industry may be manifested by increasing prices or reducing quality products delivered. Power depends on a number of market characteristics, and relative importance of the recipient business system. Power increases if the resource is important for the recipient company, the number of suppliers is reduced for one reason or another or switching transfer entails significant costs. In terms of Porter (1980), the bargaining power of suppliers is determined by factors such as degree of product differentiation (increase their power to customers), degree of concentration of suppliers, the relative importance of a product for the buyer, the availability (or on the contrary the unavailability) of substitutes, the degree of integration of downstream suppliers. Business strategy is to moderate pressures from customers or suppliers through: concentration to increase bargaining power, diversification of outlets and the company supplies to reduce dependence, vertical integration upstream or downstream.

The threat of new entrants. Newcomers are companies that can compete or start companies already compete in an industry. They bring a desire to win and often have significant resources. New entrants enter the market when the profit margin is attractive and the barriers to entry are low. Porter presented his works seven possible barriers to entry to a sector: economies of scale, product differentiation, the necessary capital, transfer costs, access to distribution channels, absolute cost advantages, due to their position on the curve of experience, access to resources and low cost of designing products, government policy. These types of barriers vary from one business area to another, having for some sectors a considerable influence. *Economies of scale* consist in the reduction of the unit cost of production as a result of judicious allocation of production, which constitutes a real barrier to entry in many industries. *Product differentiation* is based on the qualities of products or services, a strong brand identity or business reputation on quality, reliability and after-sales services (Morden, 2007). *The needed capital.* Intrusion in a sector requires significant investment in technology, production facilities, distribution, after-sales services, which new entrants cannot be achieved only by taking additional risks. *Transfer costs.* Switching costs are costs that will incur new entrants to attract a customer of a company already on the market. *Unequal access to distribution channels.* New entrants on the market have to ensure distribution of the product or its distribution channels often controlled by companies already on the market. *Absolute cost advantages* are the effect of economies of scale and experience curve for companies on the market, which translates significant barriers to new entrants in the field. *Government policy.* Although the main role of government is the protection of competitors on a market, it restricts competition by granting monopolies and certain regulations. Industries that provide utilities are considered natural monopolies because it is more efficient to have one company that provides energy in a locality than to permit the existence of several companies to fight a local

market. The European Commission has worked with member governments to remove a large part of these barriers.

The threat of substitute products or services. Substitutes are those goods that seem different but can satisfy the same need as another product. The competition created by the threat of substitute products coming from outside that industry. When the threat of substitutes is high, an industry profitability suffers. Substitution products and services limited profit potential of an industry by placing a ceiling on prices. The threat from substitutes is determined by factors such as price and availability of substitute products, the sensitivity of the product sales price change compared with their substitutes, switching costs from one product to its placeholder, availability buyer to purchase replacement products. Although the five competitive forces model of Porter is particularly useful in strategic analysis of competitive environment, it is also open to criticism. Thus, the analysis is mainly static, while in reality in the competitive environment is changing. The model assumes that all five forces are close in importance, while critics such as Aaker (1992), Baker (1993) and Harvey-Jones (1991) believes that nothing is beyond the client. Other criticisms concerned that forces from the model are seen as threats, although some organizations adopt successful strategies for cooperation with suppliers and that the model ignores the human resource involved in the strategic approach. Despite this criticism, M. Porter's approach provides a useful starting point in environmental policy analysis and development of corporate strategy. The model was followed by analysis of changes in industry in decline and launch strategic groups analysis of the market.

2. APPLICABILITY OF PORTER'S MODEL ON ROMANIAN RETAIL MARKET

In recent years, retail activity in our country has undergone many changes both in the types of incumbents and the range of products. There is a large difference between the distribution sector in Romania and the developed European countries, Romania retail continuing to evolve much slower rate compared to other countries in Central and Eastern Europe. Retail system in our country has as main features: fragmented nature prevail traditional trade, the emergence of new forms of retail, an early stage of development of electronic commerce.

The threat of new entrants. In the retail sector, barriers to entry are relatively high. No need for a long time or financial resources that cannot be attracted to open a store at a smaller scale. To increase but significant investment is needed and greater economies of scale. It is difficult to understand but that is the one year extension retailers because many operators of commercial establishments open, but just as quickly give and bankruptcy. If consider the major international retailers entering the market in Romania, we appreciate it increasingly difficult for small traders to face the competition that manifests itself in the market. A trend that emerged in the last decade is the continuous decrease of independent retailers. Thus, if barriers to launching a new store is not impossible to overcome, the ability to establish favorable contracts with suppliers, procurement of certain facilities and competitiveness become practically a utopia for small retailers. Vertical structure and centralized procurement of large retail

chains give a competitive advantage over independent retailers. In terms of top international retailers entering the market in 2009, according to a ranking conducted by the consulting company CB Richard Ellis, which was attended by 69 states, Romania ranked as second with new nine retailers on the market and three large commercial centers opened in 2009, the first position being occupied by the United Arab Emirates, which has attracted 21 new openings. Romania has seen the opening of three new mall sites in 2009, added to the existing supply of retail market, says the report “How Global Is the Business of Retail?”

The bargaining power of suppliers. Retailers' growing power in the last decade has weakened the bargaining power of suppliers, as is the globalization and integration of Romania into the EU while, allowing the use of foreign suppliers to ensure and lower prices. The strategy of many retailers was to increased volumes for best-selling products to absorb cost pressures and, more importantly, focused on reducing capital expenditure and reducing inventories. As the consumer goods industry dynamics change, a new set of priorities for retailers is emerging. These changes have affected, inevitably, and business relationships. The top priority list are included aspects such as optimizing and streamlining the product range of products, optimizing structures, procurement, review of capital expenditure, increasing store productivity, reduce inventories. Providers had to deal with multiple requests and that is why their expertise should cover a broad spectrum of skills. They must be prepared to become more than just suppliers of products for retailers, so they should be data providers to help them in the process of retailing activity. Manufacturers who fully understand the business model of each retailer in hand and will be able to adapt the set of priorities imposed by them will have a major competitive advantage in the that class of narrow vision suppliers, which are limited to promotional plans and launching new products (Figure 2).

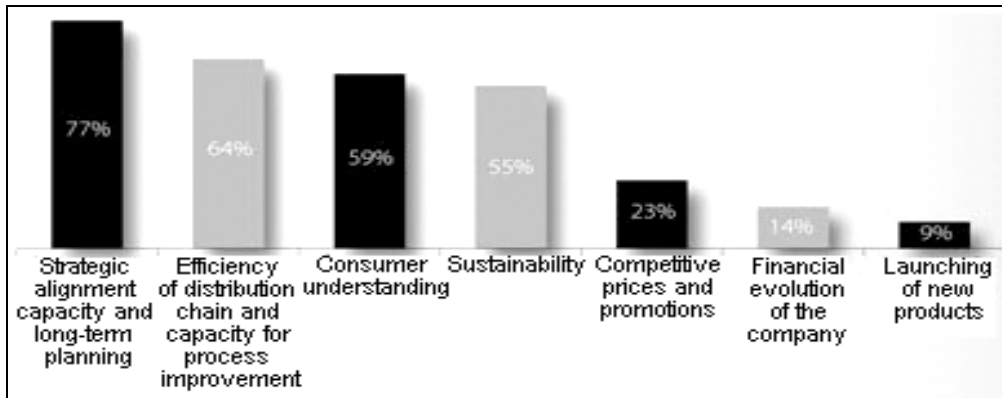


Source: www.magazinulprogresiv.ro

Figure 2. The capability shield proposed by Institute of Grocery Distribution

As shown in figure 3, retailers expect their partners to have and provide information both on current trends and consumer buying behavior and about the future. Another key area that appears on the list of priorities is related to supply chain efficiency, the logistics of each provider, through which one can obtain significant cost

reductions and can leverage stocks. Providers must be prepared to cope with the situation, no far away, when in any business plan, they will take into account issues such as reducing waste and carbon dioxide emissions and providing organic products. As retailers seek new ways to improve business models, there is no doubt that these elements will play a central role in trade between retailers and suppliers.



Source: www.magazinulprogresiv.ro

Figure 3. Key points for retailers in bargaining with suppliers

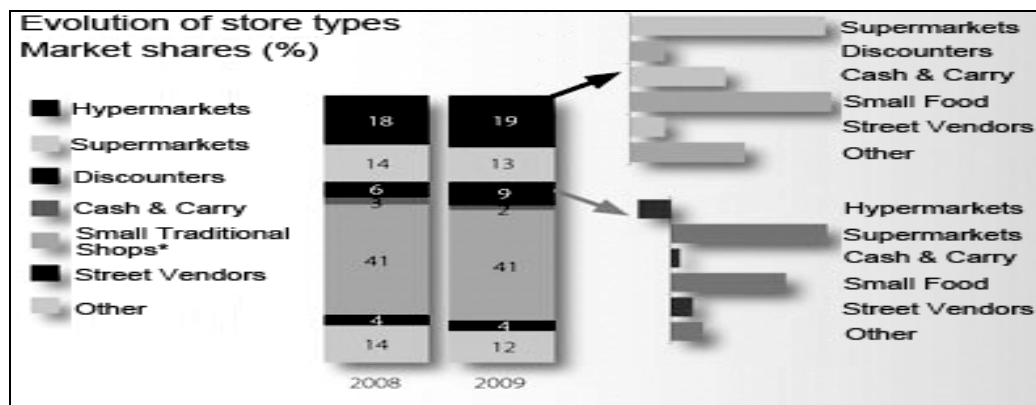
Bargaining power of buyers is moderate because of the size and concentration of major retailers. To reduce power and you retain customers, retailers seek to differentiate products and create strong brands. Individual private customers have a relatively low bargaining power in front of large retail chains, however, their power is greater for small retailers, who are less organized. As a result of economic crisis, low purchasing power and decreasing trend of Romanian consumer confidence in the future, retailers have had to adjust supply to changes in customer behavior, focusing increasingly more on products at affordable prices and promotions.

A comprehensive study on consumer behavior in times of crisis, conducted by the GfK institute in 25 countries, showed that 84% of participants were forced to change their behavior. The main things affected by the crisis were: going out, spending on energy and telephone bills, vacations and travel frequency. Asked in January 2010, within the study GfK Roper Report, to which they gave up the last 12 months, Romanians placed in descending order: clothes and shoes, vacations and travel expenses, inability to further savings and not least the night out. Moreover, in 2009, 47% of the Romanians said that many visitors get home, compared with 40% declaring this two years ago. Regarding how leisure, most Romanians were predominantly oriented in 2009 to less expensive activities such as walking outdoors or sports. Another trend resulting from this is consumer concern for health. The GfK survey highlights in the segment devoted to finance that 39% of the Romanians plan to deal with personal finance and investment in 2009 while in 2008, only 13% declared their concerns for these issues.

Romanian consumers became more interested in sound management of finances from the desire to ensure a safer future for himself and his loved ones. A

notable fact is the early disappearance of casual consumers. If they rarely bought a product category from either spoiling, or from curiosity, now began to abandon it completely. He focuses on products of primary necessity, as living standards and purchasing power declined considerably. George Mucibabici, president of Deloitte Romania, considers that we are witnessing the birth of a new type of consumer who prefer useful and durable products, which renounces impulsive purchases and carefully analyzing purchase decisions, weighing prices, quality and value added to innovative products. The crisis proved to be a learning experience for the consumer and his new habits will continue after the exit from the crisis. For the retail operators and companies producing consumer goods, the challenge will be to adapt to new requirements and to bring the consumer market to the level before the crisis.

Regarding the evolution of the types of stores, the Gfk study highlights changes in market shares of channels distribution in 2009 compared to 2008. Thus, in 2009 hypermarkets increased their market share slightly from 18% (in 2008) to 19%. Supermarkets have registered a slight decrease from 14% in 2008 to 13% in 2009. By contrast, discount stores rose from 6% in 2008 to 9% in 2009, thus increasing market share by 50% (figure 4).



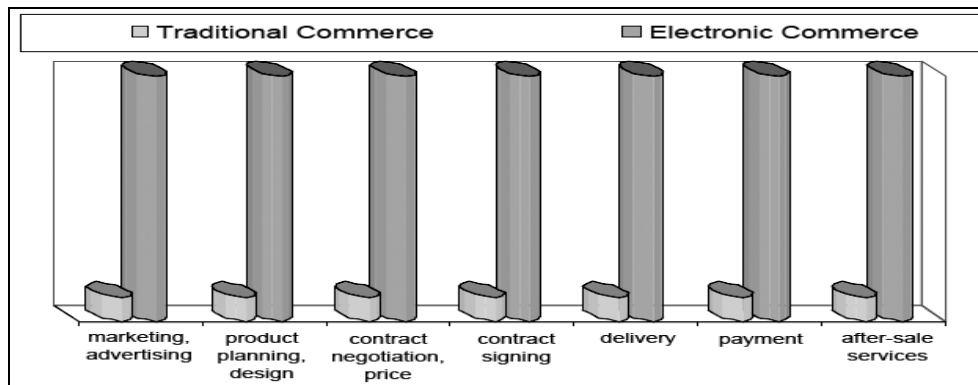
Source: GFK Roper Report 2010

Figure 4. Impact of purchasing behavior in conditions of crisis on market share of retailers

In direct relationship with other types of stores, hypermarkets have gained some customers of supermarkets and traditional stores. In contrast, discounters, even if they won a lot of supermarkets and traditional stores, hypermarkets lost in relation. They have benefited from a richer assortment, promotions, especially affordable prices prevailing in 2009, positioning themselves from this regard in a peer battle with discounters.

The threat of substitute products. There are many threats on the retail market - entering the big discount stores, for example, they usually offer products at much lower prices. This is why major retailers have launched their own brands (TIP for Real, Clever for Billa, No 1 and Tex for Carrefour, Expert Digital and Westwood for Domo, Myria for Altex, ARO for Metro, etc.), thus attracting customers which are

moving towards cheaper products in recession conditions. For retailers, the rising share of income available for expenditure on leisure, travel, etc. may pose a threat of substitution, less present in recent years due to reduced purchasing power, caused by financial and economic crisis. E-retailing (e-commerce business to consumer B2C) is also a threat to retailers from stable trade. With the increasing accessibility of Internet, electronic commerce captured the interests of individual consumers and companies of all sizes and interests. This is a new business model (e-retailing or e-commerce) via the Internet, which radically changed their efficiency, reduced the cost, including transaction ones (State & Costache, 2007). Size of advantages obtained by the use of e-retailing technology in business varies according to the model of the applied e-retail, the quality of management decisions and the degree of specialization of operational staff, issues that we address below in figure 5.



Source: D. Radoi, *The electronic commerce – vector of the new economy*, National Institute for Economic Research, Working Papers Series, no. 9, Bucharest, 2008

Figure 5. Productivity surplus got through the use of e-commerce, in comparison with the classic model

On virtual market, millions of people have access, being the largest potential market. This means increasing market share and sales opportunities, which may result in more demand. The demand gets new values through the role that it has on production and economic branches, the ability to require production of goods and services are in accordance with customers' particular requests. Advantages of e-retailing and the need to reduce costs, in order to adapt to cheaper products targeted by buyers, have led some of the local market retailers to create virtual stores that complement and sometimes replace physical units that are much more expensive. For example, in the case of electronic products and appliances, specialized retailers like Domo, Flamingo and Altex own their online stores, which may represent an important substitute for products sold in stable trade. Customer enjoy much lower prices, free or cheaper shipping, the opportunity to compare more easily and quickly the offerings of competitors and also save time.

Rivalry between the existing firms on Romanian retail market is increased by equal size and power of dominant retailers, who are pushing to increase market share, the trend of extinction of small retailers through acquisitions, mergers or

alliances, and high costs to exit this market. The 15 biggest retailers on the Romanian market in 2009 have achieved cumulative sales of nearly 8 billion Euros, down by about half a billion euro in 2008, but increased their market share from 14% to 17%, according to a study of a Polish market research company PMR. This shows that the decline in consumption last year hit less the top ranking in retail industry and more among small retailers on the market. Among leading groups there are Metro, Rewe, Schwarz and Carrefour that are dominant the large markets of western Europe, particularly France and Germany.

Table 1. The first 15 retailers on the Romanian market

No	Company/ Group	Turnover in 2009 (mil. Euros)	Turnover in 2008 (mil. Euros)	Field	Stores
1	Metro	1900	2120	Food	Metro, Real
2	Rewe	1500*	1524	Food	Selgros, Billa, Penny Market
3	Carrefour	1135	1190	Food	Carrefour, Carrefour Express
4	Schwarz Group	900*	778	Food	Kaufland
5	Louis Delhaize	400*	400	Food	Cora
6	Tengelmann**	369	277	Food	Plus
7	Auchan	350	278	Food	Auchan
8	Praktiker	257	292	DIY	Praktiker
9	Dedeman	250	250	DIY	Dedeman
10	Bricostore	190*	240	DIY	Bricostore
11	Altex	180	344	Electro Retail	Altex
12	Domo	170	207	Electro Retail	Domo
13	Delhaize	150*	132	Food	Mega Image, Red Market
14	Avon	113*	113	Direct sales of cosmetics	Sales agents
15	Ambient	100*	200	DIY and construction materials	Ambient
TOTAL		7900	8400		

Note: *estimation made by Ziarul Financiar, ** the company was taken this year by the Germans from Lidl and Schwarz.

Source: www.zf.ro, 30.03.2010

International operators are expected to continue to strengthen their position in Romanian retail, under circumstances of the global economic crisis. According to PRM consultants, several local retailers have been forced by market conditions to close their businesses, while others have frozen expansion plans, having solvency problems. The study includes both sales of consumer goods and DIY products, machinery and fuel. Retail market in Romania will go down with 2.3% in 2010, the second consecutive year of decreasing, to 190 billion lei (46.9 billion Euros), according to PMR study, which estimated a return of the industry in 2011-2012. Representatives of the research company stated that the retail market in Romania continues to offer good prospects for investors, due to the reduction of costs for labor and real estate prices.

3. CONCLUSIONS

The model of Porter led to the following conclusions about the threat of new entrants, bargaining power of suppliers, bargaining power of customers, the rivalry between existing firms on the retail market in Romania and the threat from substitute products. In the retail sector, barriers to entry are relatively high. No need for much time or financial resources that cannot be attracted to open a shop, but to increase requires substantial investment and economies of scale. Increased power of retailers in the last decade has weakened the bargaining power of suppliers, as is the globalization and integration of Romania into the EU because allows the use of foreign suppliers that ensure lower prices.

Consumer bargaining power is moderate because of the size and concentration of major retailers. In order to reduce their power and gain their loyalty, retailers try to differentiate their products and create strong brands. Following the economic crisis, low purchasing power and downward trend of Romanian consumer confidence in the future, retailers have had to adjust supply to changes in customer behavior, focusing increasingly more on product with low prices and also on promotions.

There are many threats on the retail market - penetration of large discount stores, for example, they usually offering products at prices much lower. This is why major retailers have launched their own brands, thus attracting customers that are turning to cheaper products in conditions of recession. E-retailing is also a threat to stable trade retailers. With the increasing accessibility of Internet, electronic commerce has captured the interest of consumers, individuals and companies of all sizes and interests. Rivalry among existing firms in the retail market in Romania is enhanced by the equal size and power of dominant retailers, who are pressured to increase their market share, the trend of extinction small retailers through acquisitions, mergers or alliances, and high costs to exit this market.

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