

# Revising Porter's Five Forces Model for Application in the Travel and Tourism Industry

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## ABSTRACT

This paper takes a new look at Porter's five competitive forces model. In doing so, this work proposes a new competitive forces model centered on the travel and tourism industry that includes two additional forces, namely information technologies and government regulations, and adds an additional element to the buyers' perspective, namely the power of intermediaries. This model is applied in the case of Greece and, although several limitations, from the findings it is proven as capable of explaining the competitive forces that affect the level of competition in the Greek travel and tourism industry.

**Keywords:** Porter's competitive forces, information technology, intermediaries, government regulation, Greece, travel and tourism.

## INTRODUCTION

Several structural elements within the business environment affect the level of competition in an industry. To these ends, there is continuing interest by academics and practitioners to study the totality of environmental influences or conditioning that are outside an organization's boundary (Smith et al. 1980), and various models have been proposed and discussed (e.g. Henderson 1976; Smith et al. 1980) that examine the external environmental forces that impact on organisations.

However, up to now the most significant and dominant paradigm in the literature of industry analysis is Porter's (1980) competitive forces model. This framework proposes five potential forces of industry competition that have changed the way that managers, consultants and practitioners view the competitive environment (Slater & Olson 2002) and determine the profitability and the degree of attractiveness of a given industry, as has been reported by Blair and Buessler (1998) for the medical group industry and by Thurlby (1998) for the electricity supply industry.

Porter's five competitive forces that constitute strong threats to a company's profitability and when act favorably can establish the long run profitability of a given industry are (Hill & Jones 1995, 70-81; Porter 1980):

1. The rivalry among established companies that is a function of three main factors: industry competitive structure; demand conditions, and, the height of exit barriers in the industry.
2. The threat of new potential entrants that is a function of the height of barriers to entry that depend on three main sources: brand loyalty, absolute cost advantages, and economies of scale.
3. The pressure of substitute products that can limit the price a company can charge for its products and services.
4. The bargaining power of buyers. Buyers are able to force down prices or they may demand higher quality and better services which may increase a company's operating costs.
5. The bargaining power of suppliers. Suppliers are able to force up the price of their products or reduce the quality of products supplied which may decrease a company's overall profitability.

Since 1980 that the model was first introduced, a substantial body of research has been compiled that either supports, revises or complements Porter's basic premises. Among these studies Thyrby (1998) supports that Porter's model is static and ignores time. Likewise, Slater & Olson (2002) believe that although Porter's basic premises are valid, the five forces model is an incomplete representation of the market forces that influence industry and business performance.

The deficiencies identified at Porter's model are evident in the travel and tourism industry where its shape is changing and customers' needs and governments' responses change and evolve in a different way. As Evans, Fox & Johnson (1995) suggest:

*Despite the optimism for growth in tourism, the industry is in a state of rapid change. Change is reflected by a variety of factors including new tourism products, regulatory changes, globalization, use of new technologies, environmentalism, increasing world debt, and economic cycles (p. 37).*

Thus, the five forces model does not adequately address the changes having taken place the last decades in the travel and tourism industry. In addition, the model does not adequately include all actors affecting tourism firms' environment. Based on these deficiencies of the model, the overall goal of this paper has been set to complement, not replace, Porter's five forces model in respect to the travel and tourism industry. It does this in four sections. These sections cover: a discussion of elements not extensively addressed by Porter's original model but having direct influence to the travel and tourism industry; the delivering of a new competitive forces model explicitly for the travel and tourism industry; the application of the model in the case of Greece; and the conclusions and the implications of the study.

## NEW ELEMENTS IN PORTER'S MODEL

As already mentioned there is a necessity to extend the five forces model to reflect developments and peculiarities of the travel and tourism industry. Therefore, this section discusses elements not addressed extensively in Porter's original model but having relevance to the level of competition in the travel and tourism industry.

### *INTERMEDIARIES*

Nowadays, the disparities inherent in mass production and mass consumption have caused intermediaries to enter into the distribution chain between buyers and sellers (Wynne & Berthon 2001, p. 18). Traditionally, distribution in the travel and tourism industry is characterized by intermediaries that are actually buyers for the products and services offered by tourism businesses. Although intermediaries may be considered a part of the bargaining power of buyers force, due to the important role they play in the travel and tourism value chain, they may be considered as a distinctive element within Porter's power of buyers force. In particular, their power is evident from the fact that in 2000 tour operators had a share of 25 percent in the total international tourism market, meaning that they organized approximately 175 million international trips (Calvek 2000, p. 479). As Wynne & Berthon (2001) state:

*The international tourism industry is characterized by large numbers of small suppliers who are globally scattered. In Third World destinations this is compounded by the secluded locations of many of the attractions, limited domestic markets and weak infrastructures. Likewise, tourists are numerous, diverse and are geographically separated from the suppliers... In response to these challenges, the industry has developed a complex value chain, utilizing the services of several intermediaries. In its simplest form, the chain members include the destination service provider, the inbound tour operator, the outbound tour operator and the local travel agent (p. 422).*

Intermediaries, in the form of tour operators, organize a large number of trips from generating markets to foreign countries, and, as a result they are the middlemen that undertake the initiative to persuade clients which destinations to visit (Laws 1991, p. 120). Tour operating combines aircraft seats, beds in hotels (or other forms of accommodation), and other services and activities. The bulk purchase of the components of the tourist package allows individual packages to be competitively priced to the consumer on the basis of a high take-up rate of offers made (Cooper et al. 1998, p. 256; Goodall & Bergsma 1990). Thus, tour operators have a dominant position that derives from the fact that they are buying under conditions

of perfect competition but are selling under conditions approaching oligopoly (Klemm & Matin-Quiros 1996, p. 130).

*The competitive advantage of the tour wholesalers lies in their doubly strategic position between all principal suppliers and between suppliers and consumers. Their power derives from the enormous volumes they can command, their pivotal familiarity with diverse market segments, and the capacity to shift tourist flows from one destination to another (Britton 1991, p. 457).*

### **INFORMATION TECHNOLOGIES**

Porter's traditional model did not recognize information technology (IT) as a distinctive competitive force, but IT was only considered as a means of supporting the five forces. This deficiency of Porter's model was reported by Schertler (1984) who attempted to analyze how IT can affect the five competitive forces. Likewise, McFarlan (1984) and Thurlby (1998) considered IT as a way to achieve competitive advantage and refined Porter's model to incorporate an IT dimension. As McFarlan (1984) suggested by adding to the product an IT context, could result in increased power of the organization, reduced cost and add value to the product. All these will create barriers to new entrants or substitute products to enter successfully the market. Therefore, IT has now been recognized as a force in its own right (Thurlby 1998).

In the increasing competitive environment that tourism companies operate, developments in information technology offer new chances to improve communication with consumers and business partners (Kuom & Oertel 1999). Tourism is one of the world's largest industries and has historically been an early adopter of new technology (Wynne & Berthon 2000, p. 421). Without question, IT is drastically altering the competitive environment of the travel and tourism industry and rewrites the rules of how companies conduct business and reach their customers (Connolly & Olsen 2000, p. 74).

Systems of information technology, that comprise of computers, computerized reservation systems, digital telephone networks, videos, videotext, teleconferencing, internet and management information systems (Poon 1989), have changed travel and tourism industry's structure and have created entirely new ways to do business. Since travel and tourism is an information intensive industry (Poon 1993), IT is the single greatest force determining competitive strategies (Connolly & Olsen 2000, p. 73).

Until recently, bookings have been predominately undertaken by telephone, but now bookings can be made electronically. For example, in 1981 approximately 100,000 hotel rooms were booked through Global Distribution Systems (GDS), although this number increased to around 33,000,000, in 1996, and is expected to rise even more in the years to come (Kuom

& Oertel 1999). In the airline industry, GDS account for about 80% of all airline tickets sold (Kuom & Oertel 1999).

IT increases choice and enhances relationships to each of the various sections of the travel and tourism industry (suppliers, tour operators, travel agencies and travelers). Home or business users can check out a broad variety of tourism and travel products and services, and thereby 'bypassing' parts of the established tourism value chain (Kuom & Oertel, 1999). Internet technologies offer a number of advantages to tourism businesses and is fast becoming an important new channel for commerce (Wynne & Berthon 2001, p. 18). The World-Wide Web (WWW) enables customers to access electronically up to the minute information and make price comparisons, independently of place and time. In case that one seller is out of stock or too expensive, there is no need to drive miles to an alternative competitor but just to find another one through Internet.

### **GOVERNMENT REGULATION**

Yarborough & Yarborough (1990) suggest that governments define and enforce property rights and the rules of competition, and, as a result, affect the functioning of most industries and the relationships among market forces. In fact, a political dimension has an immediate impact at firms and each country's business environment. This is more evident in the travel and tourism industry, where government is a vital force initiating tourism expansion at a destination or country and creates the necessary infrastructure required for tourism development. To these ends, although somebody may allege that governments regulation can be included under Porter's new entrants competitive force, various strands of international tourism research demonstrate the need to include government regulation as a separate force driving industry competition, since change in regulation may call for a change in a firm's overall strategy (Rugman & Verbeke 2000, p. 378).

Governments have usually essential or even critical influence over the tourism industry by providing numerous services including infrastructure, transportation, security, overseas marketing, as well as funding of tourism projects (Andriotis 2000; 2002a; Elliot 1987), and, by creating the legal framework within which the tourism industry operates. In doing so, governments have the power to change travel and tourism industry's structure and create entirely new ways to do businesses by placing constraints around the way in which resources are used.

There has been considerable discussion about the nature of changes in governance, and their causes in the travel and tourism industry. In practice, there is likely to be a mix of government intervention in the travel and tourism business environment, since government regulations may be put into place, which either prohibit or encourage tourism. From one point, governments may seek to secure the adoption of measures to discourage tourism development and penalize tourism operators flouting the rules. From another point, government's financial

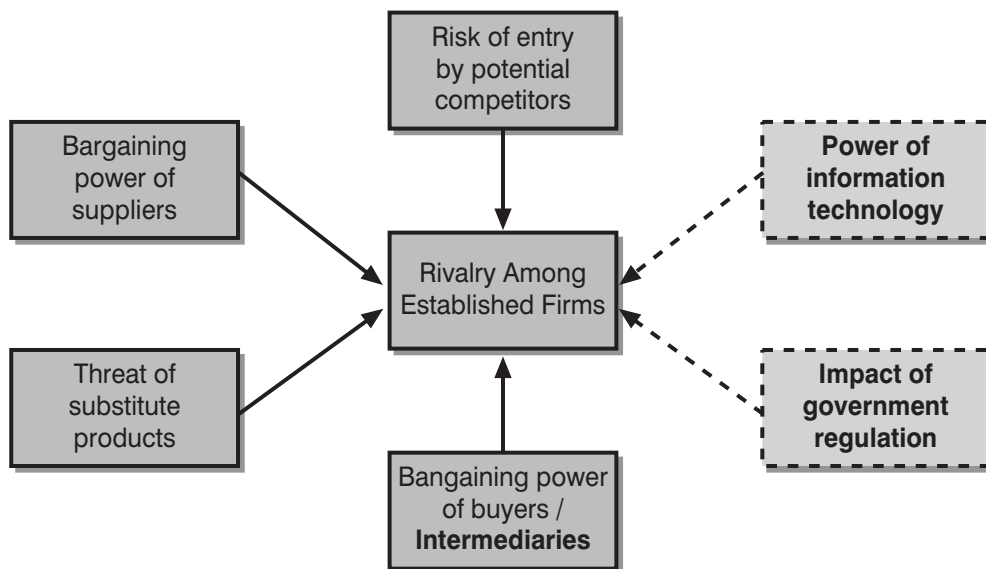
incentives can be used to expand the tourism industry. Likewise, deregulation of aviation can, and has been, used expressly by many governments as an instrument of change to shape tourism anew.

### DELIVERING A NEW COMPETITIVE FORCES MODEL FOR THE TRAVEL AND TOURISM INDUSTRY

Before proposing a revised model of competitive forces, it should be stressed that the major notions of Porter’s forces are as valid today as they used to be 25 years ago. As a result, it is not our intention to challenge the points Porter made so effectively. Instead, this paper concentrates on forces that were not distinctive elements in the original model, as well as on new ways of thinking about the original forces.

In reality, due to changes having taken place in the travel and tourism industry, as well as the distinctive nature of the industry, it is necessary to revise the model in order to make it more relevant. In this respect, Figure 1 represents a revised competitive forces model, which reconfigures Porter’s five original forces by adding two more, namely the power of ITs and the impact of government regulation, and, by proposing an additional element to buyers perspective, namely the bargaining power of intermediaries.

**Figure 1: A revised competitive forces model for the travel and tourism industry**



**Source: Compiled by Porter (1980)**

This model will be tested in the case of the Greek travel and tourism industry. More specifically, to provide a critical analysis of the competitive forces in the case of Greece, this paper adopts a case study approach based on data collected through secondary sources. However, before going into detail in the case of Greece, it should be noted that in the travel and tourism industry there are different types of enterprises, such as: hotels, campings, travel agencies, airlines, shipping companies, etc. that may present differences when using the proposed model. As a result, the proposed model is tested in selected types of tourism enterprises within the Greek travel and tourism industry and, as a result, it is not proven that it can be used in the same efficient and effective manner in all markets of the Greek travel and tourism industry.

**APPLICATION OF THE MODEL IN THE GREEK TRAVEL AND TOURISM INDUSTRY**

Tourism plays an important role in the Greek economy. In 2002, close to 14.2 million tourists visited Greece, creating incomes of approximately €10.3 million (HNT0 2002). Association of Hellenic Tourist Enterprises (2003) estimates that approximately 810 thousand persons are directly involved in tourism activities.

Although the significance of tourism for the Greek economy, Greek tourism businesses face strong competitive pressures. For example, in 1996, a study by ICAP (1997) found that within 30 Greek travel agencies only 21 were profitable. Likewise, Moussios (1999) states that of the 7,500 hotels in Greece, some 6,000 are loss making. As a result, it becomes essential to investigate the forces that may drive Greek travel and tourism industry's competition and the associated negative results.

***BARGAINING POWER OF SUPPLIERS***

There are no Greek owned charter companies transferring tourists from tourism generating countries to Greece. As a result, airlines, as suppliers of transport services, can seriously affect the Greek travel and tourism industry by raising their prices. On the other hand, as far as the supply of labor is concerned migrant workers are prepared to receive low wages (Andriotis & Vaughan 2004; Lazaridis & Wickens 1999). However, migrant workforce is available only for low-level unskilled jobs, although high skilled professionals require higher payments. In the past, employees' strikes in Olympic airways, the national carrier, have forced the company to raise wages.

### ***THREAT OF SUBSTITUTE PRODUCTS***

Greek tourism businesses face severe competition. First, they compete with other tourism companies offering similar products or services within Greece. Second, they compete with other countries, which the tourists may choose to visit. The major competitive countries of Greece include southern European Mediterranean countries such as Spain, Portugal and Cyprus. In addition, the emergence of cheap destinations from north Africa (such as Morocco, Tunisia) and the eastern Mediterranean (Egypt, Turkey, and Syria), are seen as a growing threat, since Greece is not as cheap as it used to be in the past (Andriotis 2000; Buhalis 1998; EIU 1990).

### ***RISK OF ENTRY BY POTENTIAL COMPETITORS***

In Greece, the barriers of entry, in the form of capital required and issue of operational license, are low in some types of tourism businesses, such as travel agencies, small accommodation establishments, tourist shops and car rentals. This means that their number will continue to increase in the future. Likewise, although high capital investments are required for the construction of large hotels, incentives provided by the Greek government (e.g. by the last development law 2601/98) will increase the entry of new competitors. On the other hand, the high amounts required for the establishment of an airline and a shipping company means that the oligopolistic situation will continue in the future.

### ***RIVALRY AMONG ESTABLISHED TOURISM FIRMS***

The rivalry among Greek tourism businesses is keen. In fact, there is a large number of tourism enterprises and this number continues to increase. For example, the supply of hotel beds in the Greek hospitality industry increased from 57,022 in 1961 to 285,860 in 1981 and to 593,990 in 2000. The increasing number of tourism businesses leads to overcapacity at many Greek regions and places greater pressures on many types of Greek tourism businesses.

As far as air transport is concerned, although deregulation after the summer of 1991, has allowed to airlines, other than Olympic airways, to operate domestic flights the competition up to now is not severe. Finally, the passenger shipping is going to enter the era of free competition soon (Alexopoulos & Theotokas 2001).

### **BARGAINING POWER OF BUYERS / INTERMEDIARIES**

In Greece, as in most Mediterranean countries, there are two major categories of clients, the independent tourists who make their own arrangements, and the inclusive tourists coming through tour operators (Andriotis 2003a). As independent tourists cannot guarantee increased sales to entrepreneurs, tour operators play an important role in the Greek tourism industry, mainly for packaging the various elements of the tourism product and distributing it to consumers (Andriotis 2003b; 2003c). As a result, intermediaries constitute a powerful group of buyers in the Greek travel and tourism industry to the extent that Howarth (1994) estimated that, in 1993, 65% of the hotel market in Greece was organized through tour operators. As Howarth (1994) reports:

*It is an undisputable fact that the average Greek tourist entrepreneur is heavily dependent on the tourist package price which is strongly negotiated by the international Tour Operators. It is an "unhealthy" dependence as a result of the weak position of the Greek tourist product in the international market (p.3).*

Because tour operators determine tourists' choice through advertising and promotion and due to the trend toward inclusive tour packages, organized exclusively in origin countries, the problem is getting severe (Andriotis 2000; 2002b). As Dighe (1997) remarks for a long time, major tour operators have treated Greece as a secondary cheap destination that sells always very well but late in the season. Since "the demand for tourism services is highly elastic with respect to price" (Truett & Truett 1987, p. 185), tour operators, in their attempt to maintain high profit margins, put fierce pressure on Greek entrepreneurs to keep prices down (Bird 1995).

### **POWER OF INFORMATION TECHNOLOGY**

Although there is limited research for technology adaptation in the Greek travel and tourism industry, it is believed that because most of the Greek tourism enterprises are small in size<sup>1</sup>, they are not able to benefit from the use of IT. This is evident by a study undertaken by Papanikos (2000) where it was found that only 17% of small and medium-sized hotel establishments use e-mail, compared to 64% of large establishments, and that only 18% of small and medium-sized hotel establishments accept reservations through Internet, compared to 61% of their larger counterparts. On the other hand, a study undertaken by Sakellariadis & Drosakis (2001) for the use of information and communication technologies by travel agencies in Crete and Rhodes found that although these companies use the Internet to promote their tourist products and services, the majority does not use the Internet for reservations because their customers arrive directly from tour operators.

In brief, since the majority of Greek tourism companies have not utilized ITs as a means to distribute directly their products/services and provide their customers with information, they will not be able to benefit from the use of ITs and eliminate or even remove intermediaries' intervention.

### ***IMPACT OF GOVERNMENTAL REGULATION***

In the evolution stage of Greek tourism, the government provided market-led incentives, such as grants interest free subsidies, untaxable allowances, and extra depreciation, directed at increasing bed spaces and the construction of facilities demanded by the tourist market (Andriotis 2001). In addition, during 60's, the first Xenia hotels were established by the Hellenic National Tourism Organisation all around Greece. Later, because of problems having resulted from uncontrolled tourism development, the Greek state through Law 797/86, attempted to control development and declared areas with high concentration of accommodation establishments as 'Areas of Controlled Tourism Development' where only high-class hotels could be constructed. Parts of these areas were declared as 'Saturated Tourist Areas' where no construction of accommodation establishments was allowed (Andriotis 2001).

Also, up to now the Hellenic National Tourism Organization exercises control over prices by specifying regulations for minimum prices to be charged for rooms or apartments, according to accommodation type (Andriotis 2003a). In the case of an establishment wanting to charge higher prices than the minimum, these prices should be declared to the Hellenic National Tourism Organization. However, frequently, hoteliers in their attempt to reduce lost revenue accruing from rooms remaining unsold, frequently reduce prices by offering discounts to tour operators (Buhalis 1995). This policy is in contravention of Law 642/1977, which imposes measures, such as fines, removal of operational license and reduction of category on law-breakers.

Up to 1991, legislation created legal barriers of entry to airlines, other than the national flag carrier Olympic airways, to operate domestic flights (Fragoudaki 2000). Likewise, recently barriers to sea transport have been erected. This liberalization of the Greek domestic air and sea market has had profound effects by ending monopoly in the air transport and oligopoly in the sea transport.

From all the above it is evident that Greek governments have played a significant role in the development of the tourism industry, with some times providing incentives to the private sector, and others adopting restrictions as a way to discourage further expansion.

## CONCLUSION

This paper proposed a revised competitive forces model for application to the travel and tourism industry. The seven forces model proposed three main amendments at Porter's model. First, the model explicitly considered the role of intermediaries as a powerful group of buyers in the travel and tourism industry. Second, the model highlighted government regulation as a reason for changing market conditions for tourism businesses. Finally, the model declared IT as a vital means of tourism companies to improve communication with consumers and business partners.

The main implications of the proposed 'seven forces' approach is that tourism firms in order to achieve sustainable competitive advantage they have to consider the usefulness of forces, other than those proposed by Porter. This was evident in the case of Greece, where the seven forces model was tested and it was found that, although the limitations of the study, mainly the lack of data for the Greek travel and tourism industry, and, the variety of enterprises operating within the Greek travel and tourism industry that may differ in the way that competitive forces impact on each of them, the proposed amendments drive Greek travel and tourism industry competition and guide strategic management change.

Now, let's see some ways that Greece can use the new elements proposed by the revised model for the benefit of its travel and tourism industry.

To eliminate the intermediation of foreign tour operators and receive more benefits from tourism, there is a need to use the power of ITs. For example, to enable the transfer of information between bodies and individuals interested in the direct purchase of accommodation, transportation, excursions, tourist attractions and events on-line, the establishment of a central reservation system is necessary (Andriotis 2003a). This system could be available on computer terminals at the Hellenic National Tourism Organisation offices in Greece and abroad, as well as local offices.

"Without state intervention, tourism development will likely lack the cohesion and direction necessary to sustain itself over the long term" (Brohman 1996: 62). Given the importance of the tourism industry to the viability of Greek economy and the profitability of many tourism and non-tourism enterprises efforts should be made by the government to eliminate the problems faced by the tourism industry. Although, in the past the Greek government has been actively involved in the development of the tourism industry, technocrats have made many mistakes, mainly in forecasting demand. As a result there is an oversupply of rooms in some Greek regions (Andriotis 2001). Therefore, attempts should be taken to control future tourism expansion. Better governance and coherent tourism policy might be the key to address the competitive forces faced by the Greek travel and tourism industry.

To conclude, the forces proposed in the model may change over time, and, as a result, their relative importance may also change. For a tourism business, competitive advantage may result from being able to spot and exploit future forces quicker than its competitors. Therefore, for anyone wishing to use the proposed framework must first check and confirm its degree of accuracy in the time it is being used. Also, there is a need to explore the proposed forces in more detail and to confirm the relevance of the model to the travel and tourism industry of other destinations. Finally, further work is required to confirm whether the proposed model can be applied to other service-orientated industries.

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### ENDNOTE

For example, Papanikos (2000) found that approximately 80% of Greek hotel establishments are small and Andriotis and Vaughan (2004) found that in Crete the average number of employees for travel agencies and car rentals was 3.5, ranging from 1 to 8, and to the tourist shops was two employees, ranging from 1 to 6.