

Threat from Substitues

Consider the next force, the threat from substitutes. A buyer's willingness to pay depends in part on what alternatives are available. Their inclination to switch also depends on the products price performance characteristics.

Consider the average airline customer. For a short whole distance, the air traveler may be willing to travel by road or train if the costs are comparably lower. It's important to note here that substitution may happen in two ways, that is, at the level of form or function.

The first is substitution by a similar product with the lower price performance ratio. For instance, coffee may be substituted by water or soft drinks. The second is, when the same need is met by a different product. Here, the function remains constant while form changes.

For example, the demand for business hotels in your city may be substituted by airlines or video conferencing. As the price value characteristics of these alternatives improve, that is, increased frequency of flights that allow travelers to head back home on the same day or in the case of videoconferencing, lower cost and better bandwidth availability, the demand for hotel rooms decrease.