

**Cannondale Coorporation**  
**External Environment**

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## **Analysis of the External Environment**

Cannondale is a part of the motorcycle, bicycle and parts industry. The official SIC code for this industry is 3751. A few top companies in this industry are Harley Davison, Huffy, Murray, Trek, Kawasaki and Cannondale. This industry is highly influenced by the public's desire for recreational activities, their concern with general fitness and transportation needs.

Throughout the world 1 billion bicycles are in use. The majority of the world's bikes are made and used in Asia. In the United States, bicycle sales total approximately \$5 billion annually (Thompson C-200). Through out the 1980's and early 1990's, the industry saw a steady line of growth. During the mid 1990's, this growth moved to the maturity stage. The industry is now growing at a rate of 2% annually (Thompson C-197).

A learning curve and economies of scale exists for the bicycle industry. The industry has a high fixed cost associated with the equipment used to manufacture bicycles. As a company produces more bicycles, the unit cost of the bicycle drops. Therefore, bicycle manufacturers who produce bikes in high volume are able to charge lower prices for their product. A learning curve exists when a company becomes more proficient at producing a product as the number they produce increases. Bicycle companies become more skilled at crafting bicycles as the number produced increases. It follows that companies within the bicycle industry can charge a low price if they produce in high volume and the number of bicycles produced goes up.

## **Five Forces Model**

The Five Forces Model developed by Michael Porter is one of the most effective ways of measuring the level of competition for a given industry. The model determines the level of competition between rival sellers, new entrants, buyers, substitute products, and suppliers in a given industry. An overall level of attractiveness is given to an industry from this analysis.

Rivalry among sellers measures the level of competition between members of the same industry that sell the same product. For most industries, the level of competition between sellers is the most influential characteristic. The bicycle industry is no different in this regard. In the bicycle industry, there is a moderately high level of competition between sellers. One of the reasons for the high degree of rivalry is that the industry is not seeing the same level of growth that it did in the past. Since growth of the industry has become flat, a bicycle manufacturer can only increase its sales at the expense of one of their competitors. Another factor leading to the degree of competition is the number of sellers in the industry. In the United States, there are over 100 bicycle producers selling bikes to the public. Because of this large number of producers, there is a high degree of competition (Thompson C-200). Last, consumers switching cost is low for the bicycle industry. Buyers have little or no cost to switch from one brand of bicycle to another when they purchase a new bike. The industry, therefore, has a moderately high level of competition between sellers.

The threat of new entrants measures the likelihood that new companies will try to enter an industry. The motorcycle, bicycle and parts industry has moderately low likelihood that new companies will try to enter the industry. New entrants to the bicycle industry can be deterred because of the economies of scale and learning. Also, there is a brand preference among many consumers of this industry. Customers are loyal to a particular brand, for instance Harley Davison motorcycles have a strong customer following. Many consumers will only ride a Harley and will not accept a substitute for a Harley motorcycle. Furthermore, new entrants to the bicycle industry will very likely be met with retaliation from existing firms, since the growth rate has slowed for the industry. Another factor discouraging new companies to the industry is moderate capital investment required to enter. A rather large amount of capital is required to manufacture bicycles on a large scale and receive the benefit of economies of scale. All these factors lead to the conclusion that it is not very likely that new firm will attempt to enter this industry.

Competitive pressure from substitute products is relatively high. Most bicycles are used for exercise and recreational activities. There are many good substitute activities available that can replace bicycling. Users of bicycles could easily find other forms of exercise or recreational activity such as jogging, roller-blading, weight lifting or even golf. New kinds of recreational activities can pose a threat to the bicycle industry. For instance, the growth in the popularity of roller blades comes at the expense of other recreational activities such as bicycling. Subsequently, there is a low switching cost of consumers to substitute products. There are many other recreational activities that can be enjoyed for the same price or less to the consumer. All of these factors show the high degree of competitive pressure from substitute products.

Buyers have moderate bargaining power. Again, buyers have low switching cost to other brands of bicycles or substitute products, which helps to give them some leverage over bicycle manufacturers. If a buyer decides to purchase a new bike, the previous bike owned will have little influence on the cost of a new bicycle. There are a large number of companies who produce bikes so the buyer can be selective when making a purchase. Buyers can decide when they will purchase a bicycle; there is usually no fixed time period in which a consumer must make a purchase. Furthermore, a bicycle is not a necessity. If the current cost of bicycles is too high, the consumer can simply hold off making the purchase or purchase another form of recreational equipment to give them satisfaction. Last, many of today's buyers of bicycles are well informed of the product through various bicycling magazines and Web sites. This gives the buyer the ability to make informed buying decisions. Buyers of bicycles have a moderate level of buying power because of these reasons.

The power of suppliers measures the level of power that suppliers have over sellers in an industry. Suppliers in the bicycle industry have a moderate level power. Most bicycles manufactures purchase supplies for their bikes rather than manufacturing all the parts on their own. A large number of parts are purchased from Asian manufacturers. Firms in the industry could backward integrate to make the supplies for themselves, but it makes economic sense for them to pursue the areas of manufacturing they are best at and let other manufacturers make the other supplies. Suppliers than have some control over price

charged for their products, but if prices rise too high firms that manufacture bikes will backward integrate and produce the products themselves. Suppliers to the bicycle industry have a moderate power.

According to the Five Forces Model the bicycle industry is a relatively unattractive industry. There are many factors from outside the industry that are working against it. The two strongest factors are the threat of substitute products and the rivalry among competing sellers. Efficient and competent firms in the industry should still be able to achieve sufficient profits. As a whole, the industry is unattractive. Weak performers in this industry should search for other industries where they possess the necessary competencies and where there are better opportunities for growth. Firms looking to enter the bicycle, motorcycle and parts industry should seriously consider their decision.

### **Other External Factors**

A few other factors effect the external environment of an industry. These include political and legal factors, general economy, societal factors and technology. The bicycle industry has no strong political or legal factors affecting it. The only factor working against the industry is an environmental regulation that some state parks have put in place limiting the access to bike trails. Next, the general healthiness of the economy influences the industry. The sale of bikes is closely related to the amount of disposable income available to the public. If there is a downturn in the economy, consumers will put off purchasing bicycles. In addition, there are societal factors that are linked to an industry. For the bicycle industry, the public's concern with fitness is the major societal factor at work. Last, technology plays a large role in the bicycle industry. During the 1980's and 1990's much of the growth increase can be attributed to new technologies, such as the use of new light weight materials in the frame of bicycles which greatly increased performance. These are some of the other external factors that have an influence on the bicycle industry.