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BUSINESS STUDIES IN ACTION

HSC COURSE | SEVENTH EDITION



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About this resource

Jacaranda Business Studies in Action HSC Course Seventh Edition has been revised and reimagined to provide students and teachers with the most relevant and comprehensive resource on the market. This engaging and purposeful suite of resources is fully aligned to the HSC Stage 6 Business Studies Syllabus.

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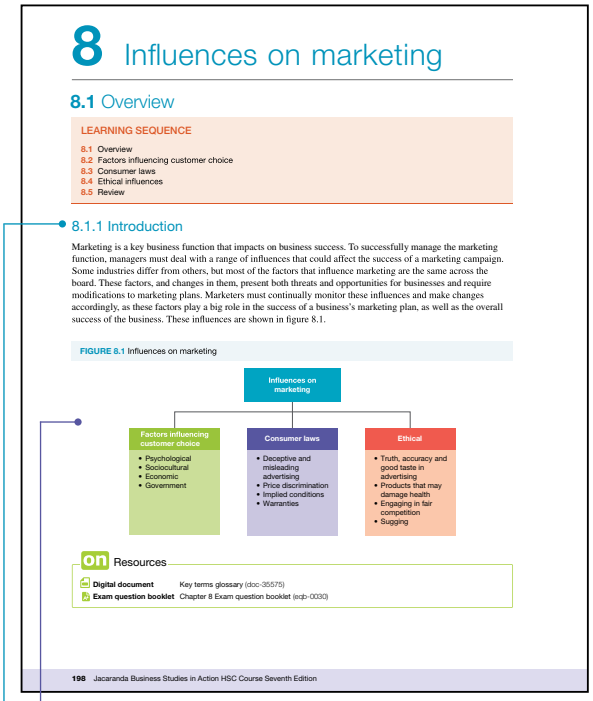
Print

Printed textbook with free digital access code inside

Fully aligned to the HSC Stage 6 Business Studies Syllabus

Have confidence that you are covering the entire HSC Stage 6 Business Studies Syllabus, with:

- key focus area and outcomes stated at the start of each topic
- syllabus links visible at the start of every subtopic
- tailored exercise sets at the end of every subtopic, including HSC exam questions
- relevant and up-to-date case studies, statistics and examples
- comprehensive chapter reviews including a detailed summary and key terms glossary, plus chapter review exercises including exam questions.


8 Influences on marketing

8.1 Overview

LEARNING SEQUENCE

8.1 Overview
8.2 Factors influencing customer choice
8.3 Consumer laws
8.4 Ethical influences
8.5 Review

8.1.1 Introduction

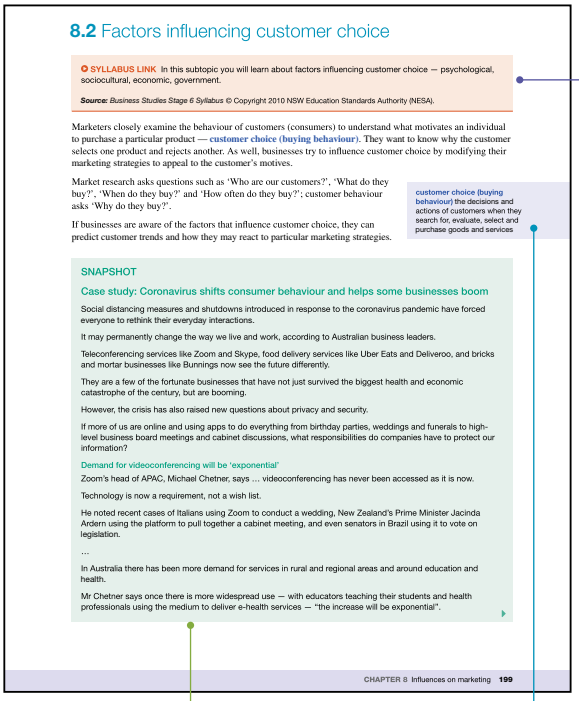
Marketing is a key business function that impacts on business success. To successfully manage the marketing function, managers must deal with a range of influences that could affect the success of a marketing campaign. Some industries differ from others, but most of the factors that influence marketing are the same across the board. These factors, and changes in them, present both threats and opportunities for businesses and require modifications to marketing plans. Marketers must continually monitor these influences and make changes accordingly, as these factors play a big role in the success of a business's marketing plan, as well as the overall success of the business. These influences are shown in figure 8.1.

FIGURE 8.1 Influences on marketing

on Resources

Digital document Key terms glossary (doc-35575)
Exam question booklet Chapter 8 Exam question booklet (ecjb-0030)

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8.2 Factors influencing customer choice

SYLLABUS LINK In this subtopic you will learn about factors influencing customer choice — psychological, sociocultural, economic, government.

Source: Business Studies Stage 6 Syllabus © Copyright 2010 NSW Education Standards Authority (NESA).

Marketers closely examine the behaviour of customers (consumers) to understand what motivates an individual to purchase a particular product — **customer choice (buying behaviour)**. They want to know why the customer selects one product and rejects another. As well, businesses try to influence customer choice by modifying their marketing strategies to appeal to the customer's motives.

Market research asks questions such as 'Who are our customers?', 'What do they buy?', 'When do they buy?' and 'How often do they buy?'; customer behaviour asks 'Why do they buy?'.

If businesses are aware of the factors that influence customer choice, they can predict customer trends and how they may react to particular marketing strategies.

customer choice (buying behaviour) the decisions and actions of customers when they search for, evaluate, select and purchase goods and services

SNAPSHOT

Case study: Coronavirus shifts consumer behaviour and helps some businesses boom

Social distancing measures and shutdowns introduced in response to the coronavirus pandemic have forced everyone to rethink their everyday interactions.

It may permanently change the way we live and work, according to Australian business leaders.

Teleconferencing services like Zoom and Skype, food delivery services like Uber Eats and Deliveroo, and bricks and mortar businesses like Bunnings now see the future differently.

They are a few of the fortunate businesses that have not just survived the biggest health and economic catastrophe of the century, but are booming.

However, the crisis has also raised new questions about privacy and security.

If more of us are online and using apps to do everything from birthday parties, weddings and funerals to high-level business board meetings and cabinet discussions, what responsibilities do companies have to protect our information?

Demand for videoconferencing will be 'exponential'

Zoom's head of APAC, Michael Chetner, says … videoconferencing has never been accessed as it is now.

Technology is now a requirement, not a wish list.

He noted recent cases of Italians using Zoom to conduct a wedding, New Zealand's Prime Minister Jacinda Ardern using the platform to pull together a cabinet meeting, and even senators in Brazil using it to vote on legislation.

…

In Australia there has been more demand for services in rural and regional areas and around education and health.

Mr Chetner says once there is more widespread use — with educators teaching their students and health professionals using the medium to deliver e-health services — "the increase will be exponential".

CHAPTER 8 Influences on marketing 199

Each Chapter begins with an introduction that grabs students' attention, providing a snapshot of what the topic is about.

Diagrams and images break down content, allowing students to understand complex concepts.

Up-to-date and relevant case studies allow students to apply their knowledge to real world examples.

Glossary boxes to develop and support business literacy.

Syllabus links are visible at the beginning of every subtopic.

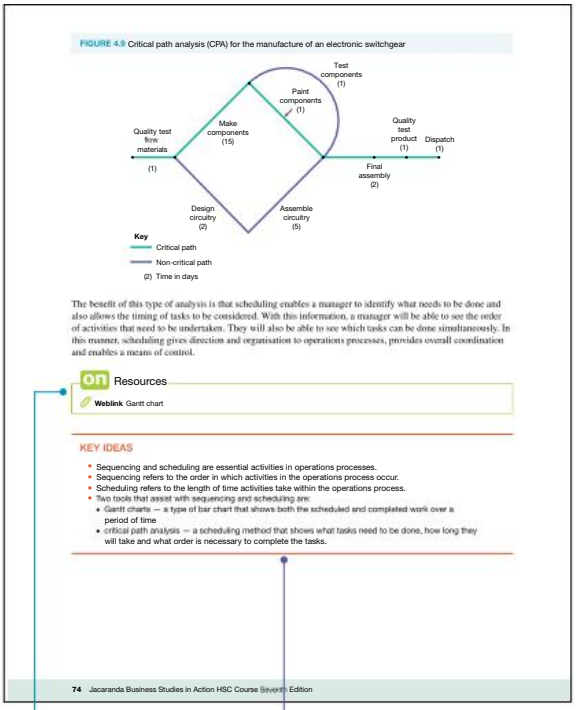


FIGURE 4.9 Critical path analysis (CPA) for the manufacture of an electronic switchgear

Test components (1)
Paint components (1)
Quality test raw materials (1)
Make components (15)
Quality test product (1)
Dispatch (1)
Final assembly (2)
Design circuitry (2)
Assemble circuitry (5)

Key
Critical path
Non-critical path
(2) Time in days

The benefit of this type of analysis is that scheduling enables a manager to identify what needs to be done and also allows the timing of tasks to be considered. With this information, a manager will be able to see the order of activities that need to be undertaken. They will also be able to see which tasks can be done simultaneously. In this manner, scheduling gives direction and organisation to operations processes, provides overall coordination and enables a means of control.

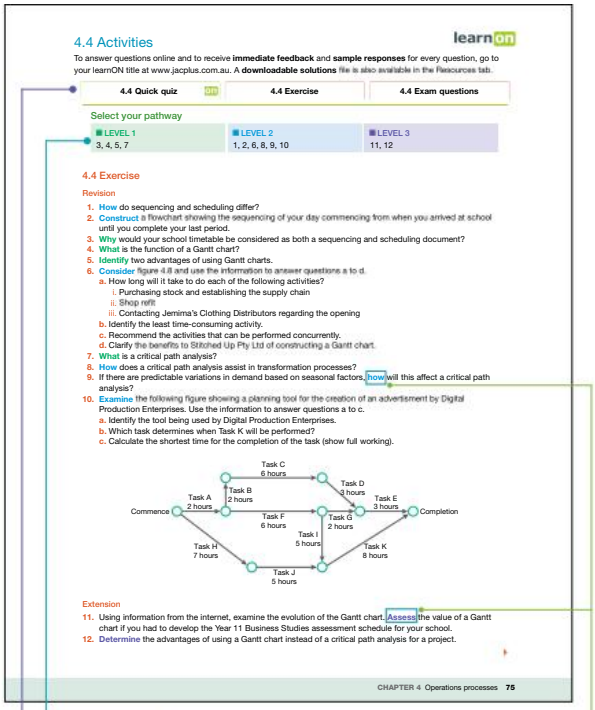
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Weblink Gantt chart

KEY IDEAS

- Sequencing and scheduling are essential activities in operations processes.
- Sequencing refers to the order in which activities in the operations process occur.
- Scheduling refers to the length of time activities take within the operations process.
- Two tools that assist with sequencing and scheduling are:
  - Gantt charts — a type of bar chart that shows both the scheduled and completed work over a period of time
  - critical path analysis — a scheduling method that shows what tasks need to be done, how long they will take and what order is necessary to complete the tasks.

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4.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

4.4 Quick quiz | 4.4 Exercise | 4.4 Exam questions

Select your pathway

LEVEL 1 3, 4, 5, 7 | LEVEL 2 1, 2, 6, 8, 9, 10 | LEVEL 3 11, 12

4.4 Exercise

Revision

1. How do sequencing and scheduling differ?
2. Construct a flowchart showing the sequencing of your day commencing from when you arrived at school until you complete your last period.
3. Why would your school timetable be considered as both a sequencing and scheduling document?
4. What is the function of a Gantt chart?
5. Identify two advantages of using Gantt charts.
6. Consider figure 4.8 and use the information to answer questions a to d.
   a. How long will it take to do each of the following activities?
      i. Purchasing stock and establishing the supply chain
      ii. Shop refit
      iii. Contacting Jemima's Clothing Distributors regarding the opening
   b. Identify the least time-consuming activity.
   c. Recommend the activities that can be performed concurrently.
   d. Clarify the benefits to Stitched Up Pty Ltd of constructing a Gantt chart.
7. What is a critical path analysis?
8. How does a critical path analysis assist in transformation processes?
9. If there are predictable variations in demand based on seasonal factors, how will this affect a critical path analysis?
10. Examine the following figure showing a planning tool for the creation of an advertisment by Digital Production Enterprises. Use the information to answer questions a to c.
    a. Identify the tool being used by Digital Production Enterprises.
    b. Which task determines when Task K will be performed?
    c. Calculate the shortest time for the completion of the task (show full working).

Task C 6 hours
Task A 2 hours
Task B 2 hours
Task D 3 hours
Task E 3 hours
Commence
Task F 6 hours
Task G 2 hours
Completion
Task I 5 hours
Task H 7 hours
Task K 8 hours
Task J 5 hours

Extension

11. Using information from the internet, examine the evolution of the Gantt chart. Assess the value of a Gantt chart if you had to develop the Year 11 Business Studies assessment schedule for your school.
12. Determine the advantages of using a Gantt chart instead of a critical path analysis for a project.

CHAPTER 4 Operations processes 75

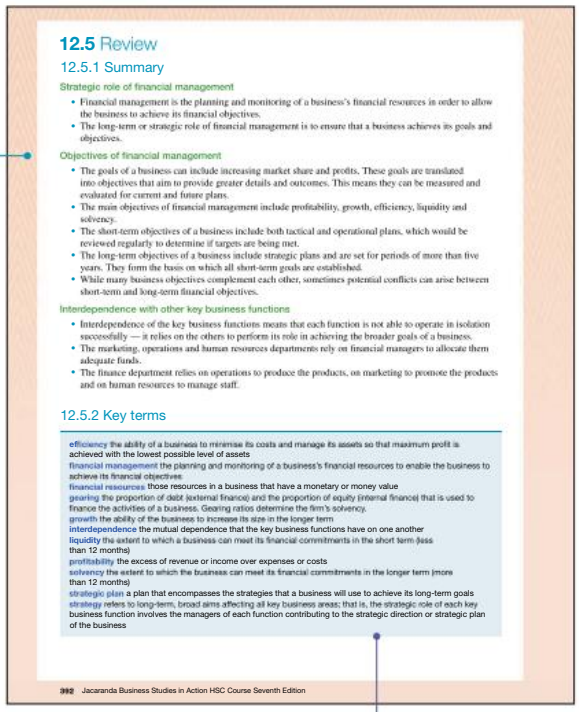
OnResources link to targeted digital resources including video eLessons and weblinks.

A summary of key ideas is provided at the end of each subtopic.

Online and offline question sets contain revision, extension and HSC exam questions.

Learning pathways allow for differentation in every question set.

HSC 'key process verbs' are colour-coded and used in graded questions throughout the text that appeal to all levels of learners.



12.5 Review

12.5.1 Summary

Strategic role of financial management

- Financial management is the planning and monitoring of a business's financial resources in order to allow the business to achieve its financial objectives.
- The long-term or strategic role of financial management is to ensure that a business achieves its goals and objectives.

Objectives of financial management

- The goals of a business can include increasing market share and profits. These goals are translated into objectives that aim to provide greater details and outcomes. This means they can be measured and evaluated for current and future plans.
- The main objectives of financial management include profitability, growth, efficiency, liquidity and solvency.
- The short-term objectives of a business include both tactical and operational plans, which would be reviewed regularly to determine if targets are being met.
- The long-term objectives of a business include strategic plans and are set for periods of more than five years. They form the basis on which all short-term goals are established.
- While many business objectives complement each other, sometimes potential conflicts can arise between short-term and long-term financial objectives.

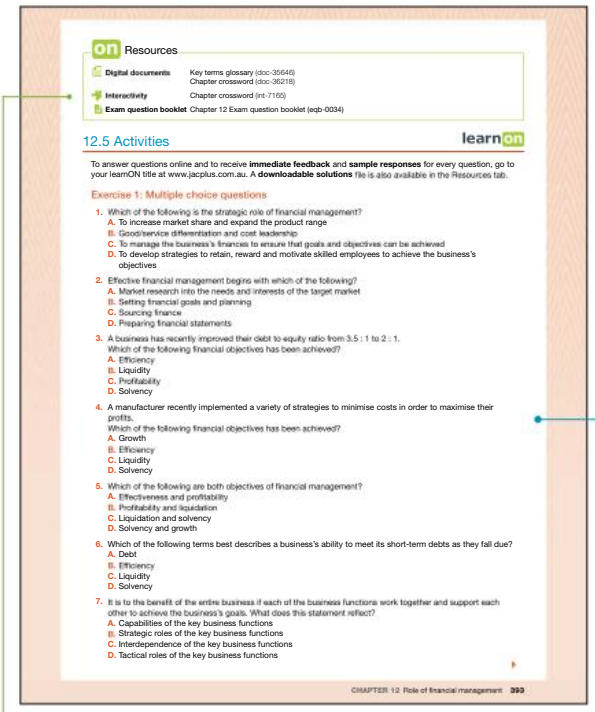
Interdependence with other key business functions

- Interdependence of the key business functions means that each function is not able to operate in isolation successfully — it relies on the others to perform its role in achieving the broader goals of a business.
- The marketing, operations and human resources departments rely on financial managers to allocate them adequate funds.
- The finance department relies on operations to produce the products, on marketing to promote the products and on human resources to manage staff.

12.5.2 Key terms

efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets
financial management the planning and monitoring of a business's financial resources to enable the business to achieve its financial objectives
financial resources those resources in a business that have a monetary or money value
gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.
growth the ability of the business to increase its size in the longer term
interdependence the mutual dependence that the key business functions have on one another
liquidity the extent to which a business can meet its financial commitments in the short term (less than 12 months)
profitability the excess of revenue or income over expenses or costs
solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)
strategic plan a plan that encompasses the strategies that a business will use to achieve its long-term goals
strategy refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

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on Resources

Digital documents: Key terms glossary (doc-35646); Chapter crossword (doc-36218)
Interactivity: Chapter crossword (int-7165)
Exam question booklet: Chapter 12 Exam question booklet (eqb-0034)

12.5 Activities

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Exercise 1: Multiple choice questions

1. Which of the following is the strategic role of financial management?
   A. To increase market share and expand the product range
   B. Good/service differentiation and cost leadership
   C. To manage the business's finances to ensure that goals and objectives can be achieved
   D. To develop strategies to retain, reward and motivate skilled employees to achieve the business's objectives
2. Effective financial management begins with which of the following?
   A. Market research into the needs and interests of the target market
   B. Setting financial goals and planning
   C. Sourcing finance
   D. Preparing financial statements
3. A business has recently improved their debt to equity ratio from 3.5 : 1 to 2 : 1.
   Which of the following financial objectives has been achieved?
   A. Efficiency
   B. Liquidity
   C. Profitability
   D. Solvency
4. A manufacturer recently implemented a variety of strategies to minimise costs in order to maximise their profits.
   Which of the following financial objectives has been achieved?
   A. Growth
   B. Efficiency
   C. Liquidity
   D. Solvency
5. Which of the following are both objectives of financial management?
   A. Effectiveness and profitability
   B. Profitability and liquidation
   C. Liquidation and solvency
   D. Solvency and growth
6. Which of the following terms best describes a business's ability to meet its short-term debts as they fall due?
   A. Debt
   B. Efficiency
   C. Liquidity
   D. Solvency
7. It is to the benefit of the entire business if each of the business functions work together and support each other to achieve the business's goals. What does this statement reflect?
   A. Capabilities of the key business functions
   B. Strategic roles of the key business functions
   C. Interdependence of the key business functions
   D. Tactical roles of the key business functions

CHAPTER 12 Role of financial management 393

A summary of key ideas is provided at the end of each chapter.

Key terms are collated at the end of every chapter for revision.

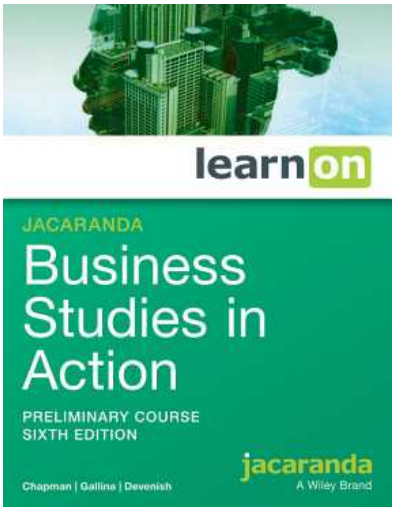
End of chapter resources including a key terms glossary, chapter crossword, chapter test and exam question booklet.

End of chapter activities including multiple choice, short answer and exam practice questions.

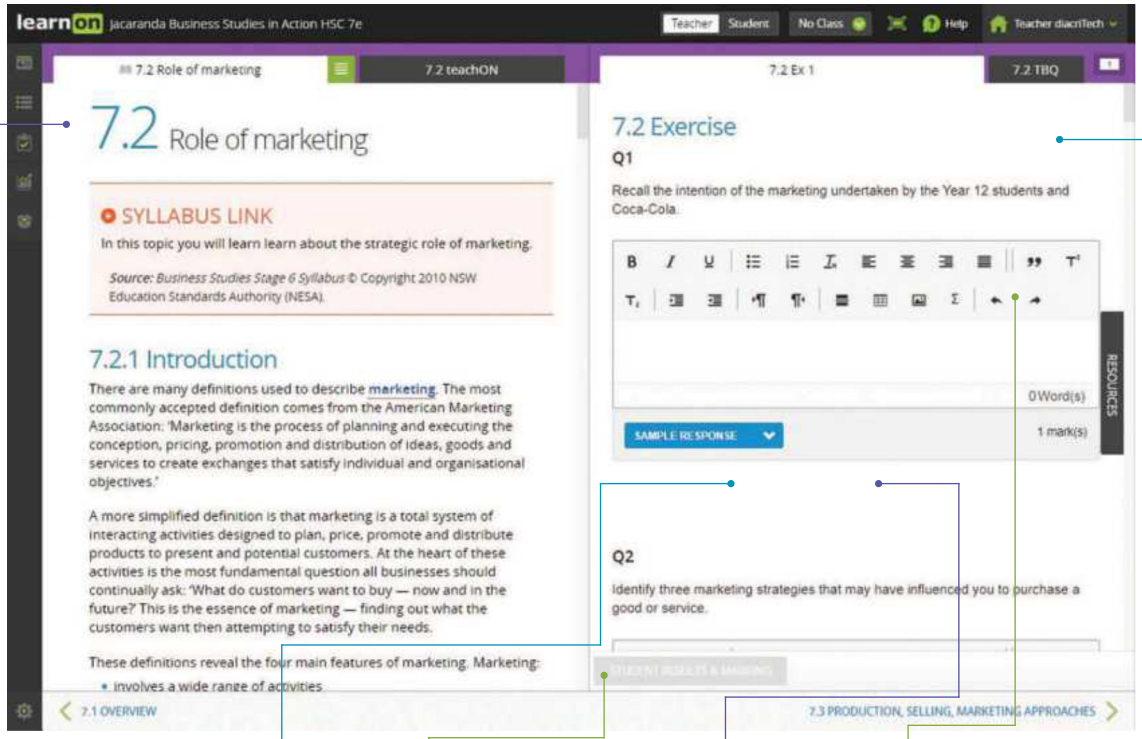
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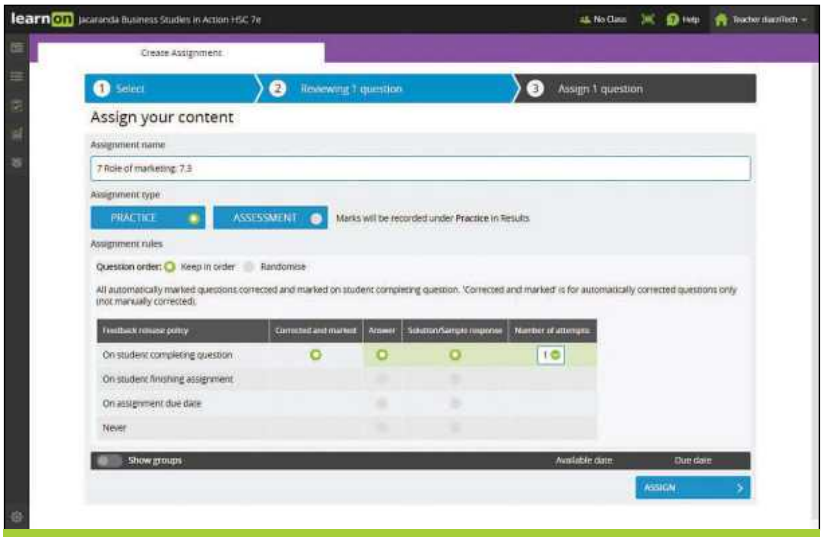
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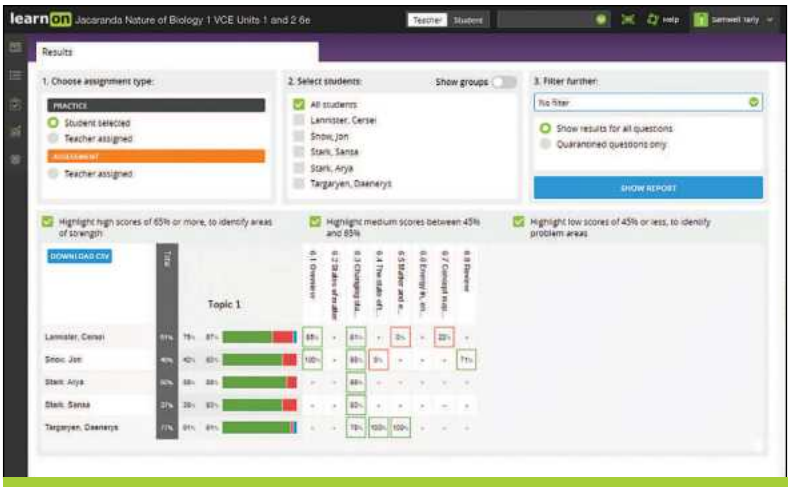
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- quarantined chapter tests with answers and exemplary responses
- an easy-to-navigate marking interface that allows teachers to see student responses, add comments and mark their work
- the ability to create custom tests for your class from the entire question pool — including all subtopic, topic review and past HSC exam questions
- customisable course content, giving teachers more flexibility to create their own course
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TOPIC

1 Operations

FOCUS AREA

The focus of this topic is the strategies for effective operations management in large businesses.

OUTCOMES CHECKLIST

Students should be able to:

- ☐ critically analyse the role of business in Australia and globally
- ☐ evaluate management strategies in response to changes in internal and external influences
- ☐ discuss the social and ethical responsibilities of management
- ☐ analyse business functions and processes in large and global businesses
- ☐ explain management strategies and their impact on businesses
- ☐ evaluate the effectiveness of management in the performance of businesses
- ☐ plan and conduct investigations into contemporary business issues
- ☐ organise and evaluate information for actual and hypothetical business situations
- ☐ communicate business information, issues and concepts in appropriate formats.

CHAPTER SEQUENCE



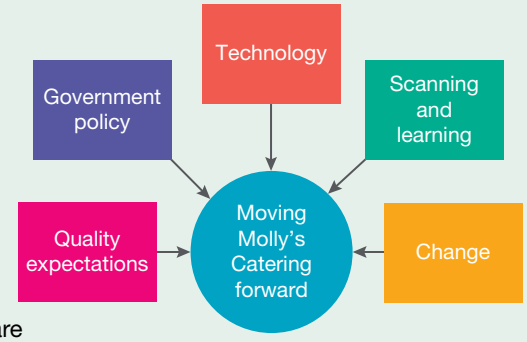
SNAPSHOT

Case study: The hospitality sector and the pandemic — Molly's Catering

The effects of COVID-19 had wreaked havoc on the hospitality industry and Molly's small-medium catering business was faced with some difficult decisions. The early stages of 2020 involved reducing staff hours for some workers and being stood down with no work for others. The government's policy to introduce a wage subsidy had helped some staff but for others with no access it was a grim period with no income. Molly's cash flow had been hit severely.

Molly called a meeting, inviting the managers from operations, marketing, finance and human resources. Molly felt that all managers needed to attend because of their interdependent relationship and that any decisions would impact each functional area. On the whiteboard, Molly identified a number of issues that she had noted about the business operating in the current pandemic-affected economy. These included: revenue was down, changing to delivery/pickup options was not a viable substitute for regular business, the rent had not been paid for a month but the bank had offered deferred repayment, some equipment had become outdated or inadequate, and there was often a lack of work for staff. Managers were asked to suggest strategies that they felt would help the business now and into the future.

The summary of strategies provided was:



1. Quality expectations — continue with appropriate monitoring, control and improvement. Marketing and operations work together to promote this, with the possibility of seeking ISO recognition.
2. Government policy — there is some access to state government financial support in the form of grants, loans, rent reductions/freeze on increases, as well as advice to ensure better work health and safety.
3. Technology — the use of relatively modern equipment is a business strength but new computer hardware and/or software systems could aid logistics and also be used for inventory management of fresh produce. E-commerce could be used to track payments and ordering and even help with the global sourcing of the production of new menus.
4. Scanning and learning — the opportunity to investigate how similar businesses are coping.
5. Change — finance, operations and human resources would work collaboratively to identify the financial costs of purchasing new equipment, redundancy payouts, retraining and the process for re-organising the factory layout if new equipment and social distancing are required. The re-organisation of offices, work from home, sanitisation stations and use of virtual meetings will need to be addressed.

Molly and her staff's proactive response may well ensure that Molly's Catering survives the pandemic.

online only

1 Kathmandu case study: Introduction and operations

This case study provides detailed information on the financial management of outdoor apparel and equipment retailer Kathmandu, including case study content and exercises.

on Resources

Digital documents	Kathmandu case study: Introduction and operations (doc-35654) Answers for case study (doc-35655)
Weblink	Kathmandu

1 Kathmandu case study: Introduction and operations

1.1 Overview

LEARNING SEQUENCE

1.1 Overview
1.2 Role of operations management
1.3 Influences on operations
1.4 Operations processes
1.5 Operations strategies
1.6 Review

1.1.1 Kathmandu history

In 2020, outdoor clothing and equipment company Kathmandu celebrated 33 years of operation. Its first store opened in Melbourne in 1987 but was quickly followed by a New Zealand branch in Christchurch. For the first 10 years, however, the company was satisfied to remain a small, specialist outdoor retailer that for the most part made its own products in New Zealand.

When it first started, adventure clothing and equipment offered limited protection for people interested in exploring nature and its varying weather conditions and landscapes and for those keen to test themselves against the elements. Kathmandu's founders Jan Cameron and John Pawson saw a market opportunity to satisfy the demand of these types of travellers and set about producing fleece and thermal apparel that were lighter and quicker drying than others available and which were far more suited to this growing form of travel. The addition of a third partner Bernard Wicht in 1992 brought expertise honed from his time working with prominent outdoor clothing brands such as Goretex.

Together they worked to ensure Kathmandu was ready to take advantage of a market that was increasingly keen to buy its innovative products. Operations quickly evolved with a clear desire to design sustainable and adaptive products. Keen to encourage repeat sales, Kathmandu also established one of the world's first loyalty programs, the Summit Club, in 1994.

By 2000, Kathmandu had become a vertically integrated retailer that sought to develop its own branded products, conscious of the need for quality materials at low costs that would be sold via its own retail distribution network. Also at this time, the company sought to test the overseas potential of its brand in the United Kingdom, to support its existing Australian and New Zealand stores. On the back of its expansion it was acquired by a private consortium of investors who introduced a new management team that would continue to take the business forward. It also introduced the first of many community initiatives through its association with Red Cross, Outward Bound New Zealand and the Australian Himalayan Foundation. Its work with the Australian Himalayan Foundation, for example, has raised thousands of dollars, delivered LuminAID lanterns to villages that have unreliable power sources and paid for the education of nearly 1000 school students. It is these activities and its community involvement that drive the company to be more than just sustainable and one where it gives more to the community than it takes out.

By 2008 the rise of the internet allowed for the development of its online operations that would support increasing interest in mail order purchases by customers unable to visit its stores.

In 2009 the business was floated on both the Australian Securities Exchange and the New Zealand Stock Exchange and with that a more formal business organisation was created which supported a growth in staff numbers, commitment to developing an efficient and contemporary IT platform and wider distribution network.

The last few years have been quite busy for the business. In March 2018 Kathmandu management bought a United States shoe brand Oboz Footwear with which it had strong synergies such as its ecological sustainability. In 2019 Kathmandu agreed to buy the iconic Australian surf brand Rip Curl.

Kathmandu Holdings Limited (KHL) continues to develop its global outdoor, lifestyle and sports interests and its recent acquisitions have resulted in a 'brand-led global multi-channel' business.

Fast forward to the present and the business's global chain of travel and adventure stores continue to focus on crafting high-quality, sustainable products with the adventure tourist in mind.

There are 116 Kathmandu stores located in Australia and 49 in New Zealand and online presence through four sites in North America, Europe, Australia and New Zealand.

Kathmandu's extensive range of apparel (60%) and equipment (40%) is aimed at both the experienced and first-time traveller.

The efforts made by Kathmandu's management to continue on its path to more sustainable business practice has resulted in an intensive study of its existing strategies by a consultancy group that had worked with other global brands. A favourable review by the group, while endorsing existing behaviour, identified areas for Kathmandu's future development around its environmental footprint, governance and social impact, and strongly indicated that it invests in these areas.

> The consultancy group stated: 'Our vision for Kathmandu is to be a bright, shining voice of human rights coming out of the southern hemisphere — and they can do it at home as well as around the world. They can do it with that Kathmandu spirit of adventure and do it in an active way. There is a real opportunity for Kathmandu to lead in the people space, generating truly positive social impacts.'

And with that the Best in the World five-year plan was formulated and the business appears to be tracking well one year into the plan.

Like many retail stores Kathmandu was affected by the COVID-19 pandemic in 2020. Temporary store closures brought on by the need for social distancing resulted in some customers resorting to online shopping and this form of sales spiking by 200% ($106 million) as people sought many of the business's winter and outdoor-oriented apparel including its well known puffy jackets and active clothing.

Store closures resulted in staff stand downs (at no pay) for the duration in an attempt to protect their health and wellbeing. Once opened, additional safety protocols will be added to all stores in the form of hand sanitiser, face masks, contactless customer service and payment, maximum customer limits and social distancing between staff and customers.

Indications are that the store closures cost the business $125 million in lost sales; however, a capital raising strategy earlier in the year reduced external debt significantly.

Despite all the difficulties brought on by COVID-19, management are still buoyant about the year ahead. The new emphasis on health and wellbeing for themselves and their families will result in people wanting to enjoy the outdoors and become fitter.

on Resources

Sample responses Chapter 1 Exercise questions – sample responses (sar-0171)

Weblink Kathmandu

1.2 Role of operations management

Kathmandu's products are continually adapted so they can meet the rigours of challenging weather conditions, diverse terrain and the demands of its customers.

The main activities of the business are designing, marketing and retailing apparel and equipment for outdoor, travel and adventure through wholly owned subsidiaries in New Zealand, Australia and the United Kingdom. It is both a producer of goods (via its contractors) and a service provider (retail and online stores) — it is a vertically integrated supplier. It is also in the process of consolidating wholesale distributors in the United Kingdom, China and Germany.

The strategic five-year plan, Best for the World, is built around three pillars — people, planet and practice.

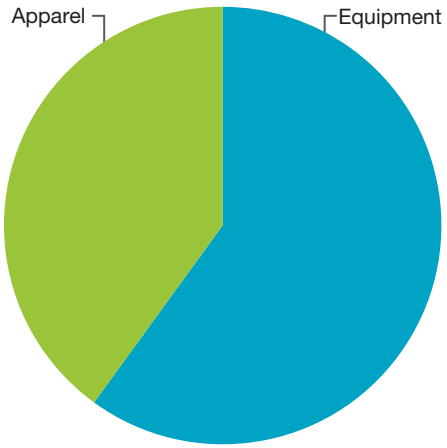
- **Best for people** covers all people in the organisation including supply chain workers, employees, customers and the community. Most notable is the aspirational goal to empower the community to positively change 100 000 lives through education, personal development and wellbeing.
- **Best for the planet** involves a shift to a 'circular economy' that has at its core three principles — designing out waste and pollution, keeping products and materials in use and regenerating natural systems.
- **Best in practice** focuses on governance through meeting the highest standards of positive social and environmental impact. Management will undergo training and development in providing clear performance accountability for all of the business's sustainability and community impact strategies.

Source: Kathmandu Sustainability Report 2020 @ www.kathmanduholdings. www.kathmandu.com.au

Kathmandu demonstrates cost leadership, as management strives to continue improving efficiency through investment in information technology (IT) infrastructure, automation and emphasising more cost-effective social media during promotional periods. Additional cost advantages are achieved through optimising the use of retail labour in respect to its stores.

The range of goods sold in its stores and through its website is extensive and includes outdoor travel clothing and equipment aimed at the experienced and/or the first time traveller.

FIGURE 1.1 The breakdown of Kathmandu's production split



Its apparel includes:

- waterproof, fleece and down jackets
- thermal wear
- shirts and trousers
- merino wool clothing
- footwear and socks.

Its equipment includes:

- assorted packs
- bags
- sleeping bags
- tents
- travel and camping accessories.

Goods are designed in-house and this decision enables Kathmandu to make full use of the experience of its staff to offer contemporary fashion. Management also makes use of customer feedback to create well-made original products.

Quality and performance are central to Kathmandu's apparel and equipment; therefore, resources, including the product team, are devoted to design, technical efficiency, quality and strong relationships with suppliers that ensures a range of apparel and equipment that meets the needs of its extensive customer base. Its products can be broadly differentiated into apparel and equipment.

FIGURE 1.2 Kathmandu's apparel and equipment



1.2.1 Interdependence of operations with other areas of the business

Interdependence across key functional areas is a feature of the business and in the most recent annual report the Chief Executive Officer's (CEO) view of the future was especially optimistic as he mentioned the role of all areas of the company.

The business continues to focus on distinctive, sustainable, quality products and opening new stores. These qualities are also a key feature of the marketing strategies used by the business to grow sales. Marketing recognises the importance of quality and innovative products and how the company maintains its brand authenticity (quality products associated with the Kathmandu brand). Maintaining gross margins and delivering operating efficiency, particularly through effective cost leadership, are essential to the development of Kathmandu apparel and equipment. Human resources involves an ongoing commitment to ensuring that employees develop skills and have opportunities for career development across all areas of the business. This helps ensure they have the capacity to adapt to a changing retail environment and thus move the company forward. The synergy displayed across the key functional areas ensures a competitive business that, according to its CEO, will maintain its focus on continued growth in core markets.

on Resources

Sample responses Chapter 1 Exercise questions – sample responses (sar-0171)

Weblink Kathmandu

1.3 Influences on operations

A range of influences, many external, have an impact on the successful operation of Kathmandu. Its pillars for growth include the desire to take advantage of its strong brand awareness and opportunities for sales growth via global expansion in strategically viable markets. Europe (outdoor lifestyles associated with some countries and diverse climates) and China (market size and increasing affluence) present the best opportunities for growth. Technology remains important as management allocates resources to its online platform to improve usability and functionality. Kathmandu seeks to use an 'omni-channel' approach that allows its customers one range irrespective of where they choose to shop. An effective digital platform also allows for a 'soft expansion' into international markets, as online sales require fewer bricks-and-mortar stores, which is also compatible with cost savings.

Cost-based competition in the form of efficiency in the management of its supply chain operations, ongoing automation and digital platforms are also prominent influences on operations.

Sustainability is a core business goal and centres on management's desire to minimise both its waste and its environmental footprint. Operational efficiency is closely aligned with sustainability. The company's commitment is reflected in:

- award recognition in 'larger business sustainability leadership'
- elimination of harmful chemicals
- recycling of plastic bottles into finished products
- increased use of sustainable cotton
- increased recycling rate.

Kathmandu's management flags its intent in a recent sustainability report, when it states:

> At Kathmandu, sustainability isn't a department, it's a way of doing things.

Its management continues:

> We strongly believe in sustainable product development and doing business ethically. We're focused on minimising environmental impact, and look to contribute to the wider community. We believe we have an opportunity, and responsibility, to help create a better world. Na tatou — nga kaitiaki o te Ao. We need to care for this world together.
>
> *Source:* Kathmandu Holdings Limited Sustainability Report 2019, Kathmandu_SustainabilityReport_2019_LR.pdf.

Its highlights include: being a *Certified B Corp* business that meets the highest verified standards of social and environmental performance, receiving an 'A' in the *Ethical Fashion Report*, ranking second in the *Textile Exchange Report* for the third year, launching its *Five Year Sustainability Plan* and recycling 9.3 million bottles into gear.

Kathmandu also opened its first 100 per cent solar-powered store in Victoria. As a stand-alone store (and not located in a shopping centre) the use of solar power aids in the business's net-zero carbon target by 2025 by eliminating 124 million tonnes of carbon dioxide emissions. On overcast days the solar power will be supported by battery back-up. A live feed of the store's solar activities will be displayed on a monitor in store so customers can view power use against power generation.

Kathmandu seeks to make its biggest statement through corporate social responsibility. This includes protecting workers' rights, better understanding its supply chain and minimising its waste to lower its environmental impact. Management recognises the challenges it faces in this area and identifies three key focus areas in its Community Investment Strategy. The areas are empowering customers, supporting community-based projects

and, in particular, contributing to social change in Nepal (the region that it claims inspires its brand). More specifically this involves:

- partnerships — the development of programs in educational and financial aid, animal and heritage conservation, disaster and poverty relief
- clothing recycling — the ability of customers to donate used clothing through the Red Cross, which is then sold via one of the charity's shops to raise money for local and international humanitarian work.

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1.4 Operations processes

1.4.1 Inputs: transformed resources

Inputs, in the form of transformed resources, include the materials that are required to produce Kathmandu's apparel. For example, fabrics are chosen to minimise environmental impacts and are driven by custom er feedback. The priority of preferred materials at Kathmandu is:

1. responsible down
2. recycled polyester
3. sustainable cotton
4. approved fabrics and trims (minimal chemicals)
5. responsible wool
6. materials that minimise water use
7. preferred man-made cellulosics
8. materials that seek to reduce ocean plastics.

All materials have an impact on the environment so it is a matter of selecting those that minimise the effects. Serious consideration is given to each material's impact on climate change, water use, pollution and resource depletion. For example, the emergence of the business occurred at a time when manufactured fleece was just gaining prominence as an alternative to wool in material technology. It was much faster drying than wool as well as being lighter and warmer — all qualities much sought after by outdoor enthusiasts. In 1994, after years of research, Kathmandu released Ecofleece, a recycled fleece fabric. Concern at the finite nature of fossil fuels used in the manufacture of polyester fabrics and a mounting number of plastic bottles made the decision to switch to Repreve, a brand of recycled polyester, an easy one.

The last five years have also seen the business's transition to sustainable cotton and 99% of all new products have been made exclusively this way since 2019.

The Better Cotton Initiative (BCI) involves engaging with suppliers that use pre-consumer waste from the factory floor and blending the fabric back to a yarn and, in doing so, removing all heavy impacts from the growing and dyeing phases of cotton production.

Kathmandu's customers are broadly categorised into six core groups:

- young and serious (aspirational achievers)
- young and casual (fun seekers)
- middle aged and serious (experienced enthusiasts)
- middle aged and casual (family adventurers)
- older and serious (rediscoverers)
- older and casual (appreciators).

The importance from an operations perspective is to ensure the product team develops products that are both technical and stylish to meet these market segments' needs and that knowledge of the core groups is disseminated in-store so that staff selling techniques are also adapted to the different segments.

1.4.2 Inputs: transforming resources

Transforming resources includes its human resources in the 101 supplier factories globally, including 76 in China, 12 in Vietnam and 3 in Indonesia.

Kathmandu sources its materials from a number of countries including China, Pakistan, Vietnam, Taiwan, South Korea and New Zealand.

Key supplier facts include:

- 99 suppliers (76% in China)
- 8.5 years is the average tenure working with suppliers
- 12 audits (including 2 unannounced). Due to COVID-19 this number was less than usual.
- 62 corrective action suppliers for suppliers
- 5 per cent turnover of suppliers.

1.4.3 Transformation processes

The role of the four Vs — volume (large-scale production), variety (both technical, functional and fashion conscious), variation in demand (although predominantly a winter brand, an emphasis on a summer range is also marketed extensively) and visibility (increased e-commerce and in-store customer experience through more effective visual merchandising in store and product presentation) — is significant to the success of the business.

The increased role of information technology in further developing online sales growth (especially globally) and the use of an experienced, customer-driven in-house design process allows for technical and original products — it is the basis of its competitive advantage and one that Kathmandu anticipates will provide the platform for further success.

1.4.4 Outputs

Retail store teams seek to personify the company's ethos to every customer they serve. The core purpose is to inspire adventure in all and sell products that encourage everyone to get out there and get going. It is the basis for same-store sales growth (increased sales that occurs within the store as opposed to sales across all stores) recorded in the most recent financial report.

The New Zealand Support Office is where products are developed by equipment and apparel designers and merchandisers, as well as being home to members of the other functional areas of finance, operations, marketing and human resources. In Australia there is similar representation of the key functional areas in its Melbourne office, but also employees that focus on store development, online, visual merchandising and IT divisions.

All product warranties are provided in accordance with statutory consumer guarantee requirements in accordance with the Australian Consumer Law.

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1.5 Operations strategies

Kathmandu's range of products reflect their performance objectives of high quality, quick to market and mass customisation at a low cost. Quality and performance are integral to new product design and development. This is the focus of ongoing investment in improved design and technical development, which has broad appeal to its customer base.

1.5.1 Supply chain management

Supply chain management is an ongoing commitment that seeks to establish stronger relationships with contractors. Better selection processes have resulted in 100 per cent of new suppliers being screened using social criteria. This and previous strong selection criteria have resulted in enduring relationships with an average tenure of suppliers of 8.5 years and only 5 per cent turnover.

Kathmandu has a robust factory assessment and monitoring program. Those that supply the business must ensure that workers receive the minimum legal wage. However the company recognises that a majority of the workers in its supply chain earn less than what most would consider fair and is working collaboratively with other global brands and with the Fair Labour Association to ensure an ethical fashion industry.

As a means of self-assessment, it uses the globally recognised HIGG Index — a suite of tools that enables businesses to accurately measure and score a product's sustainability performance and in doing so protect factory worker wellbeing, local communities and the environment.

SNAPSHOT

Case study: Khusi beanie — protecting workers' rights

Nepalese knitters were specifically used to produce the Khusi beanie in an attempt to allow them to gain independence in a region where women are still unable to match the literacy and employment rates of men.

It was important that the project emphasise the importance and significance that the company places on supply chain accountability. The beanies were knitted at home by community-based groups and then sent to a factory for completion and packaging. The factory had never been audited by an overseas company before, so Kathmandu sent auditors in and they did find some issues of non-compliance. A corrective action plan (CAP) was agreed on to ensure that the project maintained integrity and that workers' rights were protected.

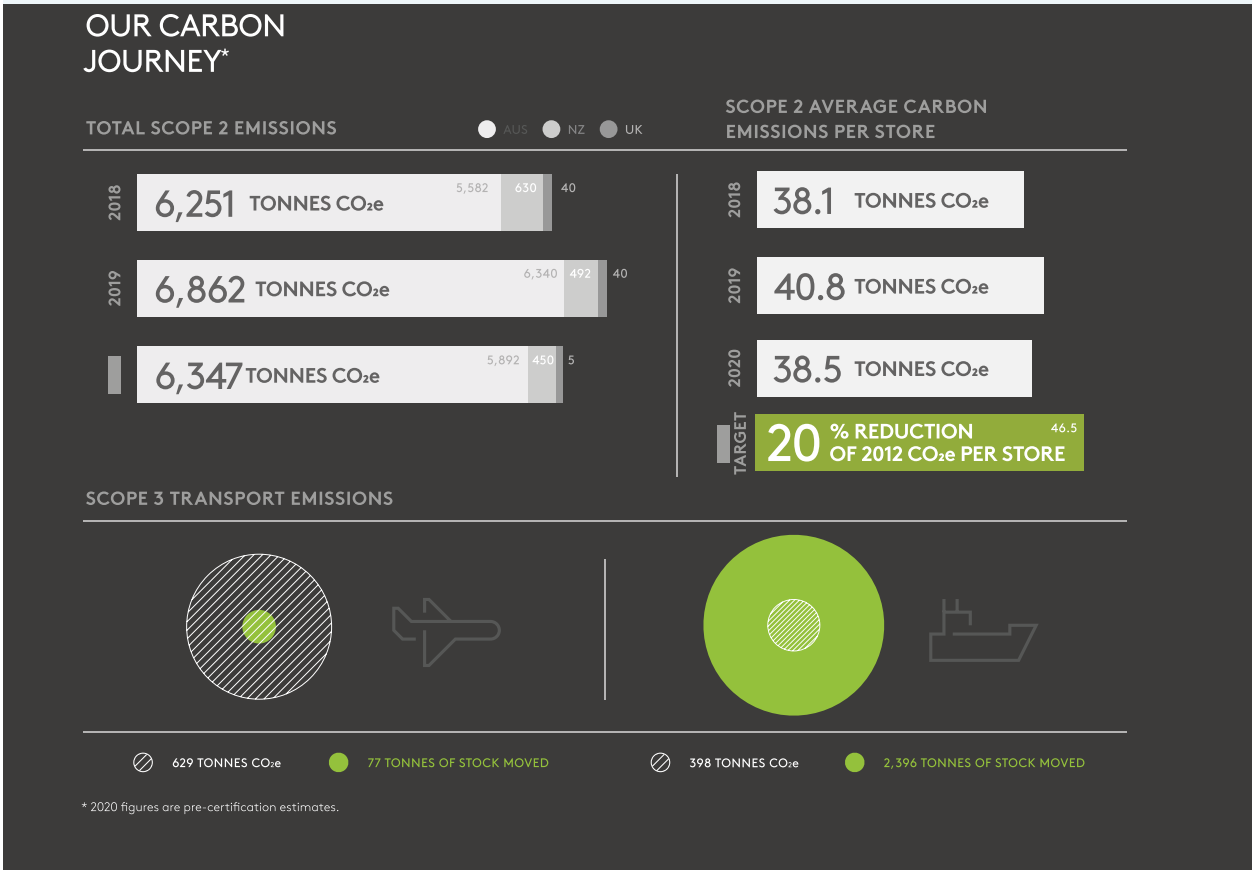
The Khusi beanie workers



1.5.2 Supply chain

Outsourcing is the main focus of Kathmandu's product manufacturing process across the globe with an emphasis in China, where 76 per cent of its products are made. The main advantages of such a process are a low-cost, high-quality product. It does, however, have some disadvantages such as the need for a policy of responsible purchasing that ensures it does not put undue pressure on suppliers to provide goods in unreasonable timeframes and the use of workplace audits to ensure compliance. Recently, Kathmandu teamed up with its outdoor industry competitors and worked with them as supply chain partners to initiate one shared audit for the manufacturing firms used by them all. This collaborative action was aimed not only at reducing costs but also alleviating audit fatigue for the supplier and freeing up more time to address problems.

FIGURE 1.3 The road to carbon zero for Kathmandu



1.5.3 Inventory management

Inventory management is a key metric for the business's management. Recent financial data indicate that stock levels fell by an average of 7.6 per cent per store, and the focus of high turnover remains a priority. This was made possible through investments in planning software that enabled more accurate buying and to reflect store differences. The seasonal nature of stock ensures effective stock holding processes.

1.5.4 Quality management

Quality management, including a commitment to continuous improvement, is central to Kathmandu's growth strategies, especially in the Australia and New Zealand markets. This will take the form of elevating brand awareness through design and innovation especially in respect to adventure travel. In addition, the business's desire for improved quality can be seen through growing social media and digital channels, better customer service such as a range of products available both in-store and online, new stores and improved customer service.

More recently its focus has been on designing for quality. Initial questions with regard to functionality and supporting marketing claims provide opportunities to then consider wider questions in regard to the quality of manufacturing processes.

The Supplier Quality Excellence program is designed to identify quality control problems before the item reaches the customer. By reducing the number of unacceptable products that arrive in the company's warehouses, there will be fewer returns due to poor workmanship.

The program is an award-based system for suppliers and includes a factory audit that helps drive ongoing improvement via product inspections and assessing return rates. Initial results indicate improvement and first-time pass rates of 38 per cent.

1.5.5 Global factors: global sourcing

The need for an effective and responsible supply chain management process is expected across all businesses, but especially those involved in global sourcing. Kathmandu seeks to protect the human rights and improved working conditions for its contract workers. This involves greater transparency and working in partnership with suppliers. To this end, the Outdoor Industry Association (OIA) Sustainability Working Group is a collaborative group of more than 300 outdoor brands and suppliers who work cooperatively to identify and employ more effective business practices.

Kathmandu segments its supply chain according to the problems it observes and its willingness to work in harmony with factory owners. Therefore, if there is a supplier that is unprepared to acknowledge it has workplace issues and is reluctant to work with Kathmandu to facilitate change, then Kathmandu is likely to terminate its business arrangement. Favoured suppliers are those that act with integrity, honesty and openness and it is these factories that work with Kathmandu to build strong employee relationships.

Kathmandu also has a responsible purchasing policy that recognises the importance of not putting undue pressure on factories through product development delays that may result in less time to produce apparel and equipment and in turn increase overtime and subcontracting. It also engages in best buying practice via ethical sourcing. Disappointed that decades of factory audits have failed to improve the lives of workers in global supply chains, the business has in the last four years embarked upon the process of accreditation with the Fair Labour Association (FLA).

Workers are encouraged to email Kathmandu with any concerns they may have (especially important in China where trade unionism is not supported) but at time of writing there was yet to be anyone using the facility, so the business started to engage the social media site WeChat as a means of engaging with contracted workers in China.

Kathmandu's commitment to a compliant and ethical global supply chain resulted in the decision to appoint two full-time workers dedicated to improved working conditions. In 40 recent audits, 10 were found to be non-compliant with its code of conduct.

1.5.6 Other global factors

Economies of scale are achieved in accordance with the need to remain competitive in the retail apparel space. Sourcing high-quality, mass produced goods from low-cost suppliers in a global business environment assists with achieving this.

Scanning and learning and research and development are important and while continuing to invest heavily in its own product development resources, Kathmandu has established partnerships with industry associations. These partnerships assist it with measuring and improving its progress in relation to sustainable and ethical practices in the production of its apparel and equipment.

FIGURE 1.4 Kathmandu's return rates are reducing year on year.



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1.6 Review

1.6 Activities

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1.6 Exercise

1. **Outline** the first 10 years of Kathmandu's development.
2. **What** gap in the market was identified by the Kathmandu founders?
3. **Explain** how Kathmandu could be described as a vertically integrated company.
4. **List** some of the community partnerships established by the company.
5. **How** did listing as a public company change the business's focus?
6. **Why** is Kathmandu more than just a travel equipment and apparel store?
7. **How** have the recent acquisitions changed Kathmandu's product lines?
8. **Identify** the main activities of Kathmandu.
9. **Outline** the features of operations management apparent in this case study.
10. **Why** are values important in the operations process?
11. **Assess** the role of operations and the other key business functions.
12. **List** the types of apparel and equipment produced.
13. **What** are the influences affecting the operations function?
14. **Summarise** the operations process.
15. What are three operations strategies that could be considered particularly important? Select one and **explain** how it assists Kathmandu to sustain its competitive advantage.
16. **Examine** how globalisation has impacted operations strategies.
17. **Analyse** the role of Kathmandu's partner groups in assisting it to face the challenges of operating as a global company.

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Weblink Kathmandu

2 Role of operations management

2.1 Overview

LEARNING SEQUENCE

2.1 Overview
2.2 Strategic role of operations management
2.3 Goods and services in different industries
2.4 Interdependence with other key business functions
2.5 Review

2.1.1 Introduction

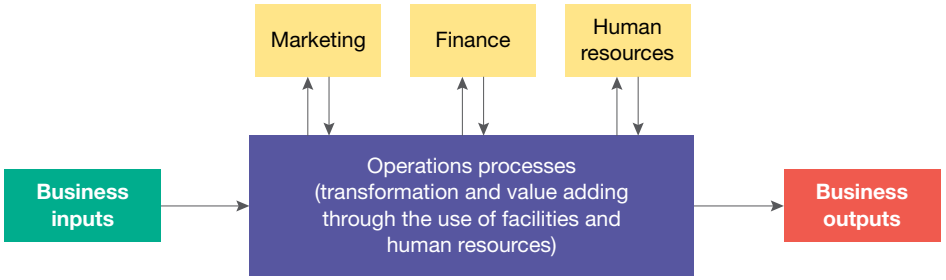
Many businesses are involved in processes that involve some form of transformation. **Operations** refers to the business processes that are engaged in transformation or, more generally, 'production'. It is a term that applies both to the manufacturing and services sector. In manufacturing, operations refers to the processes of turning inputs such as raw materials into outputs of finished or partly finished goods, with the use of labour and equipment; for example, a vehicle manufacturer turning steel into cars. In the services sector, operations is the process of actually converting inputs such as labour and equipment to deliver the final service; for example, the washing, cutting and styling of hair by a hairdresser.

The strategic role of operations management involves allocating resources so that all aspects of the business meet the customer's needs. In addition, operations management will also consider the importance of cost leadership and of differentiating the business's goods and/or services.

All production decisions will require that operations management engages with the other key functional areas of marketing, finance and human resources to deliver a low cost, high quality good or service to market that will generate sales that meet business goals.

operations the business processes that involve transformation or, more generally, 'production'

FIGURE 2.1 The relationship between operations and other key business functions



on Resources

Digital document Key terms glossary (doc-35656)
Exam question booklet Chapter 2 Exam question booklet (eqb-0024)

2.2 Strategic role of operations management

SYLLABUS LINK In this subtopic you will learn about the strategic role of operations management including the significance of cost leadership and good/service differentiation.

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Operations management is an essential key business function that overlaps with the other business functions such as marketing, finance and human resource management (HRM). Each of these essential business functions has a **strategic** component. Strategic means 'affecting all key business operations'; that is, the strategic role of the operations management involves operations managers contributing to the strategic direction or strategic plan of the business. This is shown in the case study of Virgin Australia.

strategic refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

SNAPSHOT

Case study: Virgin Australia — strategic directions



Commencing operations in Australia in 2000, Virgin Airlines is the second largest domestic carrier after Qantas. Virgin Airlines primarily operates domestic flights between the Australian capital cities. Following a takeover of Skywest Airlines in early 2013 and the purchase of 60 per cent of Tiger Australia in mid-2013, Virgin Australia also has a strong presence in both domestic regional markets and in South-East Asia. The company also flies internationally through the South Pacific and to the USA, the Middle East and Europe.

Decisions made in the operations function have a direct impact on the other key business functions. For example, the decision to acquire Tiger Australia had significant financial implications. The scale of Virgin Australia's operations is increasing and as the business acquires other airline brands, the operations function becomes more complex. Virgin Australia has therefore used technology to reduce duplication and to create operational efficiencies that save $200 million annually.

The increase in scale also means an increase in customer numbers. Evidence of this was seen in the recent growth in Velocity membership loyalty rates of 15 per cent in 2013. Apart from the operations decisions affecting the financial results and the marketing objectives, the growth in scale of operations has led to effects on the human resources function. Employment numbers had grown and the types of skills required changed as the business invested in state of the art technology to effectively manage the global operations.

COVID-19 has however disrupted Virgin Australia's strategic direction and its desire to expand domestic and global operations further. Travel has been severely affected and as a consequence the business has made some (temporary) changes to ensure that it remains competitive and delivers on its core promises to its stakeholders.

The Virgin Australia Group entered voluntary administration in April 2020 in an attempt to recapitalise the business.

This successful process involved new owners Bain Capital forging ahead as the preferred owner and a restatement of its commitment to consolidate the success of the last 20 years.

New chief executive Jayne Hrdlicka will work with the new owners to develop a new strategic direction for the business.

Cost restructure to the business is required and began with a simplification of operations through a reduction by one-third of its 9000 staff as well as reducing the airline's fleet of aircraft by one-half, cancelling orders for new planes, relocating and reducing its office space and focusing on domestic routes for the foreseeable future. The decision to 'discontinue' the Tiger Australia brand temporarily will still give it the low cost carrier option in the future.

The new owners are looking at a far leaner operation but the restructure would provide sufficient financial resources should there be further external shocks to the aviation industry.

A gradual return to flying within the domestic, then the Pacific, region offers some hope for the business but the return to international routes is a long way off. Management believes it can return to its place as a major force in aviation through six key strategic areas:

1. Realising cost efficiencies
2. Focusing on customer value
3. Harnessing its culture
4. Ongoing investment in digital and data technologies
5. Financial security through a strong balance sheet and investment capital for transformation and growth
6. Jobs and future growth

Ms Hrdlicka sees an opportunity to become a mid-market airline rather than the full service approach it offered previously. The 'new' Virgin Australia will require that customers pay for food, and business class will target luxury holiday travellers.

What makes a role strategic is not so much the length of time, but rather the level with which it integrates and affects all key business areas.

Generally, the overarching goal of business is to maximise profits. In most businesses, this is done by focusing on two very important aspects of profit:

- revenue or income
- costs or expenses.

Revenue or income should be maximised so as to bring in the greatest possible volume of money. Conversely, costs need to be minimised in order to reduce the overall level of expenses incurred.

Financial and marketing aspects of business tend to specifically target the revenue side of the business. Costs, however, are not only left to the operations and human resource function. This is because all aspects of the business incur cost, even though all aspects are not generating revenue directly. This type of analysis of revenue and cost looks at the business as a series of **profit centres** and **cost centres**.

profit centres those aspects of a business that directly derive revenue and profits

cost centres particular areas, departments or sections of a business to which costs can be directly attributed

Profit centres are those aspects of the business that directly generate income. Cost centres are those that do not directly generate income but do incur costs. The operations function can be considered as a cost centre in a business. A strategic aspect of operations management is therefore the management of costs.

2.2.1 Cost leadership

There are several different sources of operational costs in business. There are input costs, transformation costs and the costs of getting goods to market. There are also costs associated with inventory and quality management. Some of the different types of cost are identified in table 2.1.

TABLE 2.1 An overview of the types of costs within the operations function

Costs that are a feature of the operations function				
Input costs	**Labour costs**	**Processing costs**	**Inventory costs**	**Quality management costs**
• Facilities • Land • Resources • Interest on investment • Leases on machinery • Installation and testing • Energy	• Full-time and part-time employees • Casual employees • Subcontractors • Overtime • Recruitment and training • Redundancy • Rostering	• Machinery maintenance • Electricity • Scheduling • Product design • Template and tooling • Prototyping	• Back order • Logistics and distribution • Storage • Inventory management • Insurance • Deterioration • Shrinkage and theft • Damaged goods	• Prevention of loss through quality planning and training • Sampling and inspection of goods and processes • Error and remediation through warranty claims, sales returns and complaints • Machining errors, injury and machine downtime

It is apparent in the table that there are numerous sources of costs that are incurred in the operations process. Therefore, an important aspect of strategic operations management is cost leadership. **Cost leadership** involves aiming to have the lowest costs or to be the most price-competitive business in the market. A key aspect to cost leadership is that although trading with the lowest cost, the overall business should still be profitable. This means that operations managers must find ways to minimise costs.

cost leadership involves aiming to have the lowest costs or to be the most price-competitive in the market

SNAPSHOT

Case study: Walmart — cost leadership

Walmart has two different slogans: 'Every Day Low Prices' and 'Save money. Live better'. These slogans indicate Walmart's approach to cost that has made it a global example of successful cost leadership. Walmart will not engage in sales discounting, preferring to have the lowest prices daily and not needing to lower selling prices through discounting.



Walmart founder, Sam Walton, articulated the company vision as follows:

If we work together we'll lower the cost of living for everyone . . . we'll give the world an opportunity to see what it's like to save and have a better life.

In order to achieve the lowest prices possible Walmart has undertaken some significant decisions in the management of its supply chain and sourcing. Three aspects to Walmart sourcing and supply chain management are significant:

1. Walmart has over 2800 suppliers. When it approaches, or is approached by, a supplier the business aims to negotiate large volumes of supply. In this way the supplier can obtain a guaranteed minimum return and the company can save money because of economies of scale generated. The guarantee of supply means the business can ensure that stock levels are maintained.
2. Walmart management have realised that if inventory is not continually moving then the cost is increasing. This means that the movement of stock from the supplier to the actual stores is constant up to the point of sale. In order to manage this process, Walmart reduces its reliance on warehouses. Warehouses add cost and keep stock stationary. While some warehouses are necessary, they are strategically located to enable short lead times between the storage facility and retail outlets. The company has a sophisticated system of cross-docking (see the following BizFact) that requires the use of leading edge technologies and the capacity to track the movement of all sourced items at all times.
3. The lack of warehouses had meant that Walmart could not keep up with Amazon, a direct competitor in the online retailing space. Walmart has recently set up warehouses in order to manage its growing e-commerce presence.

BizFACT

Cross-docking ensures that most inventory is never stored in a warehouse, but is brought to a point where it can be directly transferred for shipment to retail outlets.

The balance between cost and quality in operations strategy

There is a direct relationship between cost and quality. As the standard of materials, labour and other inputs rises, and the precision and speed of facilities and equipment rises, the prices of products made by the business will increase. Conversely, if the costs of inputs is very low then it is likely that the final prices will reflect the lower quality of inputs and processes. Operations managers and those who lead the other business functions will need to decide what level of quality is sought and hence what level of costs to incur. In this way they will need to decide what balance to create between costs and the desired quality.

SNAPSHOT

Case study: Samsung — cost leadership in innovative manufacture

Samsung is well known for its production of smartphones. As the biggest competitor to Apple in the phone market, Samsung has led the way in terms of cost reductions. Seeing an opportunity to reduce costs of labour, capital costs, taxation and environmental costs, the company decided to relocate production from Korea and China to Vietnam, a regional neighbour, in 2016. The Vietnamese government assisted through allowing ten years of tax concessions. Samsung spent $2 billion on the relocation and continues to be committed to the country. The efficiencies achieved have been so significant that almost half of all devices are now produced there. Samsung has recently begun construction of a $220 million research and development centre in a bid to explore further cost advantages.



2.2.2 Good/service differentiation

A second key strategy applied by operations managers is that of product differentiation. Products may be classified as either goods or services. The characteristics that distinguish goods and services are shown in table 2.2. Generally, services only come into being as the result of a need for that service; it does not exist prior to the need. Contrast this situation with that of goods. Typically goods already exist even before a person seeks them.

TABLE 2.2 Distinguishing between goods and services

Characteristics	Features of goods	Features of services
Tangibility and perishability	Goods are tangible. That is, they have a physical dimension in that they can be seen, moved, touched and stored. Some goods are perishable in that they may spoil if not used (e.g. fresh fruit).	Services are intangible. They only exist while they are being performed, although the effects may endure for long after the completion of the service.
Customisation	Goods tend to be standardised, though they can sometimes be customised.	Services are generally customised, though they may be standardised to a high degree.
Ownership	Goods can be owned and transferred between people through the sale of ownership.	Services cannot be owned.
Time between production and consumption	The length of time between the production of goods and their consumption can be considerable.	The production of services and the consumption of services are simultaneous.
Determination of value	Value can be independently ascertained through costing all inputs and adding a margin. Inputs can easily be determined: cost of labour, materials and transformation plus a margin for profit.	Value is highly subjective and depends what the market is prepared to bear. However, value will increase with the service provider giving high levels of skill, longer time, high levels of education and experience, and high levels of ability and expertise.

Sometimes goods and services are so closely aligned that it can be hard to distinguish them. Consider the following. You go to a fast-food provider and buy two pizzas. The pizzas are goods that are perishable and should be eaten while fresh. However, the goods cannot be separated from the service that comes with it: the way in which the customer is treated by the person taking the order, the customisation of the goods to meet the customer's specific requirements, the layout of the store and the skill of the chef preparing the ingredients.

Standardisation involves producing goods or services that are homogeneous or identical. Typically, this involves mass producing items in high volume, with no variety and at a low cost per unit. Standardisation is directly related to cost savings achieved through economies of scale. Services can also be standardised to ensure a consistency of quality or uniformity. For example many fast-food franchises seek to deliver menu items in the same, reliable and often familiar manner, no matter where the business is located. It is often seen as the basis for their competitive advantage.

standardisation refers to the making of products that are homogeneous or identical

product differentiation distinguishing products (goods or services) in some way from those of competitors

Apart from cost leadership, operations managers can opt for a strategy of competing in markets based on product differentiation. **Product differentiation** refers to distinguishing goods or services in some way from those offered by competitors.

Differentiation of goods

Goods can be differentiated in a number of different ways. At a basic level, colour variation can constitute a simple differentiation of goods. Other sources of differentiation in goods include:

- *varying the actual features of the good*. Generally goods will be offered in a basic form, with more sophisticated options also available, which will often carry a higher price. For example, breakfast cereal such as oats can be sold in a basic, often cheap, form or it can be sold with additional ingredients, such as dried fruit and nuts, at a higher price. In reference to electronic goods, many are made with remarkable variation as a means of differentiating the market. For example, Sony produces a range of televisions 8K, 4K, HD or OLED with a number of screen sizes. All options start with a low price point that increases with additional features.
- *varying product quality*. This can be achieved by making a low-quality model that is affordable and then increasing the quality (which will be reflected in a higher price). Sometimes the higher quality alternative may be sold under an alternative trade name so that the market perceives both goods as being produced by different manufacturers. For example, some of the major supermarkets offer private label brands. These grocery items such as peanut butter may have been manufactured by a contractor that makes its own brand and the high volume, low cost alternative. Usually the more expensive option is distinguishable from its cheaper counterpart by some type of innovation that accounts for the higher price.
- *varying any augmented features.* This refers to additional benefits associated with particular goods. Typically, augmented features are seen in electronic goods and motor vehicles. For example, a car manufacturer may allow consumers to buy a vehicle with the capacity to fit a spoiler, windscreen wipers on headlights, a built-in GPS and self-parking (autopilot) systems. These are not standard features but rather additional features that can significantly vary a product.

From an operations perspective, a strategic approach assesses the different options and determines which ones can be undertaken with a cost leadership focus.

Differentiation of services

Services can be differentiated in a number of ways including:

- *varying the amount of time spent on a service.* Time is a factor that differentiates between service-providers. Amazon prime offers same day delivery on its goods to some metropolitan city areas.
- *varying the level of expertise brought to a service*. If a person has a higher level of expertise then, as a service-provider, they can provide a more specialised service. Professionals such as medical specialists and barristers can bring different levels of expertise, as reflected in their qualifications and experience, to the services that they offer prospective clients.
- *developing self-service options.* Customers are increasingly looking for flexibility in when and where they access the services provided by businesses; for example, the option of using financial services while on public transport on a Sunday night instead of relying on more traditional banking hours.
- *flexibility.* Choosing when and where to be picked up and the type of car is attractive to many users of ride-share services.
- *no fuss.* Many online retailers offer a 'no questions asked' return option for unwanted purchases, including free postage.
- *varying the quality of materials or technology used in the delivery of the service.* The use of computer-based technologies such as accounting software, CAD and CAM programs, medical technologies and ICTs can significant affect the quality of service provided and is a notable source of differentiation in the services sector. Accounting software MYOB is seen as an industry leader in computer systems for business because of its benefits in speed, cost savings, compiling taxation information, accessibilty to records and greater accuracy.

Again, from the operations management perspective, a strategic approach to service delivery will require managers to assess how much emphasis to place on which aspects of the services mix to best meet customer needs while reflecting cost leadership principles.

Cross branding

For both goods and services, differentiation can be created from cross branding or strategic alliances. This approach adds value to products (goods and services) by offering consumers added benefits from a cross-branding arrangement. Examples include the Woolworths–Caltex alliance and the Coles–Shell alliance. Here products are differentiated, but the differentiation is not from the product itself but rather from an external factor that the business has brought into the mix.

FIGURE 2.2 The IT section of a multinational bank requires a highly specialised and differentiated service. Any security systems in place need to be flexible, adapt to the range of IT issues and threats (from identity theft, spam and industrial espionage) to routine processing matters and inquiries. Quality of systems, high level expertise, speed and security are necessary features of the IT security platform.



KEY IDEAS

- Operations management is an essential key business function that overlaps with the other business functions such as marketing, finance and human resources management (HRM).
- There are several different sources of operations costs in business. There are input costs, processing or transformation costs and the costs of getting products to markets.
- Cost leadership involves aiming to have the lowest costs or to be the most price-competitive in the market.
- Good/service differentiation means distinguishing goods or services in some way from competitors.
- Standardisation involves producing homogeneous goods and services and is usually a high-volume, low-cost approach.
- Sources of differentiation in goods include:
  - varying the actual features, quality and/or augmented features
- Sources of differentiation in services include:
  - varying the amount of time spent on a service
  - the level of expertise offered
  - self-service options
  - flexibility
  - no fuss
  - quality of materials or technology used in the delivery of the service.
- For both goods and services, differentiation can be created from cross branding or strategic alliances.

2.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

2.2 Quick quiz on	2.2 Exercise	2.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 7, 9, 11, 16, 17, 21	5, 6, 8, 10, 12, 13, 15, 18	3, 4, 14, 19, 20

2.2 Exercise

Revision

Read the 'Virgin Australia — strategic directions' case study and answer questions 1 to 4.

1. **Outline** the evolution of Virgin Australia.
2. **Explain** how recent operations decisions have affected other aspects of the business.
3. **Analyse** the difficulties that Virgin Australia faces in resuming its operations in the foreseeable future.
4. **Evaluate** the six key strategic areas that management has identified as being integral to the business's long-term viability.
5. **Demonstrate** how an operations decision can affect each key business function.
6. **Distinguish** between a profit centre and a cost centre.
7. **List** the five main sources of operational costs in business.
8. **How** do businesses realise cost leadership? Provide two examples to support your claims.

Read the 'Walmart — cost leadership' case study and answer questions 9 to 11.

9. **Explain** how Walmart uses cost leadership in its operations management.
10. **How** has Walmart reduced supply-side costs?
11. **Outline** the role of cross-docking in reducing Walmart's inventory management costs.

Read the 'Samsung — cost leadership in innovative manufacture' case study and answer questions 12 to 14.

12. **Why** did Samsung choose to relocate to Vietnam?
13. **How** did Samsung's relocation demonstrate the concept of cost leadership?
14. **Evaluate** Samsung's decision to relocate its production.
15. **Classify** the following as either goods or a service, justifying your choice:
    - the work performed by an IT specialist
    - a stove
    - a bottle of water
    - a T-shirt
    - a ticket to an Ed Sheeran concert.
    - an accountant's advice
    - an airline ticket
    - a handbag
    - time spent learning mathematics with a tutor
16. **Define** the term 'good/service differentiation'.
17. **Distinguish** between the concepts of goods and services.
18. **Compare** how differentiation varies between goods and services.

Extension

19. **Analyse** the difference between standardisation and customisation of goods and services and how they benefit a business.
20. **Evaluate** how cost leadership can provide customers with choice. using brands of goods and services to support your response.

21. Businesses compete on cost and on differentiation (delivering quality products for the same price as competitors or delivering products faster than competitors). **Match** the following business activities with the intended outcome.

Business activity	Outcome
'Tailor' products to customers . . .	to compete on cost
Eliminate waste . . .	to compete on quality
Use automated production equipment . . .	to compete on speed of delivery
Strictly comply with design specifications . . .	to compete on cost
Respond quickly to changes in demand . . .	to compete on quality

2.2 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q11

A sole-trader cleaning business purchases generic products to lower costs and be price competitive. This is an example of which strategy?

A. Cost leadership
B. Economies of scale
C. Inventory management
D. Goods and service differentiation

Question 2 (2 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q21a

A recently established bank has branches in Australian capital cities and online customers across Australia. The management of this bank wants to focus on improving operations processes.

Outline the role of operations management in this business.

Question 3 (4 marks)

Ashwals is a large manufacturer of electronic components. The senior managers are deciding which strategic role of operations will suit Ashwals. Compare TWO options for the management team.

Question 4 (1 mark)

Management at Bridge Constructions Pty Ltd has decided to focus their operations on design and innovation. Which of the following best describes this strategic role of operations management?

A. Cost leadership
B. Differentiation
C. Outsourcing
D. Supply chain management

Question 5 (1 mark)

Which of the following actions are concerned with operations?

A. Selling and value adding
B. Efficiency and conversion
C. Acquisition and value adding
D. Conversion and value adding

More exam questions are available in your learnON title.

2.3 Goods and services in different industries

SYLLABUS LINK In this subtopic you will learn about variety of goods and services across different industries and learn to describe the features of operations management for business in a tertiary industry.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The operations function within any business is shaped by the range and types of goods and services that are produced. Management of operations will differ for producing goods and producing services.

2.3.1 Goods in different industries

Operations decisions will vary for goods depending on whether they are **standardised goods** or **customised goods**. Standardised goods are those that are mass produced, usually on an assembly line, meet quality expectations and are consistent in design. Customised goods are those that are varied according to the needs of customers and are produced with a market rather than production focus. The layout of operational processes will vary depending on whether goods produced are differentiated. The choice of the process selection is strategic as it requires a high degree of cross-functional interaction and coordination. This means all four key business functions need to work together to achieve the operations outcome.

FIGURE 2.3 Perishable goods such a vegetables are often inexpensive and have a short shelf life that requires them to be consumed quickly. Operations processes will need to consider these qualities to ensure freshness.



Goods may also be broadly classified as either perishable or non-perishable. The grocery sector is dominated by perishable goods (foods), whereas household and business goods are generally non-perishable. This means that operational processes will vary between the sectors that produce perishable goods and those that produce non-perishable goods.

standardised goods those that are mass produced, usually on an assembly line. Standardised goods are uniform in quality and meet a predetermined level of quality. These are generally produced with a production focus.

customised goods those that are varied according to the needs of customers. These goods are produced with a market focus rather than a production focus.

Perishable goods and operations processes

Operations processes will need to integrate the following factors:

- high standards of quality, safety and cleanliness at all stages of production
- very short lead (production) time and distribution that is efficient
- suitable, robust packaging and storage processes throughout production and distribution.

BizFACT

The customisation of goods can be seen in the production of music and the shift away from CDs to the use of streaming music services such as Amazon music, Apple Music, Tidal and Spotify. Customers subscribe to these services for a monthly fee and can listen to current and back catalogue music on demand across a variety of genres. This is different to the purchase of a CD where customers may not want some of the songs included. Music streaming services allow customers to create their own playlists. The subscription-based nature of the service and the ability to tailor music choices is proving popular and lucrative for providers.

Non-perishable goods and operations processes

The non-perishable and thus durable nature of some goods ensures that issues of quality and inventory management arise in the operations function. Operations processes will need to integrate the following factors:

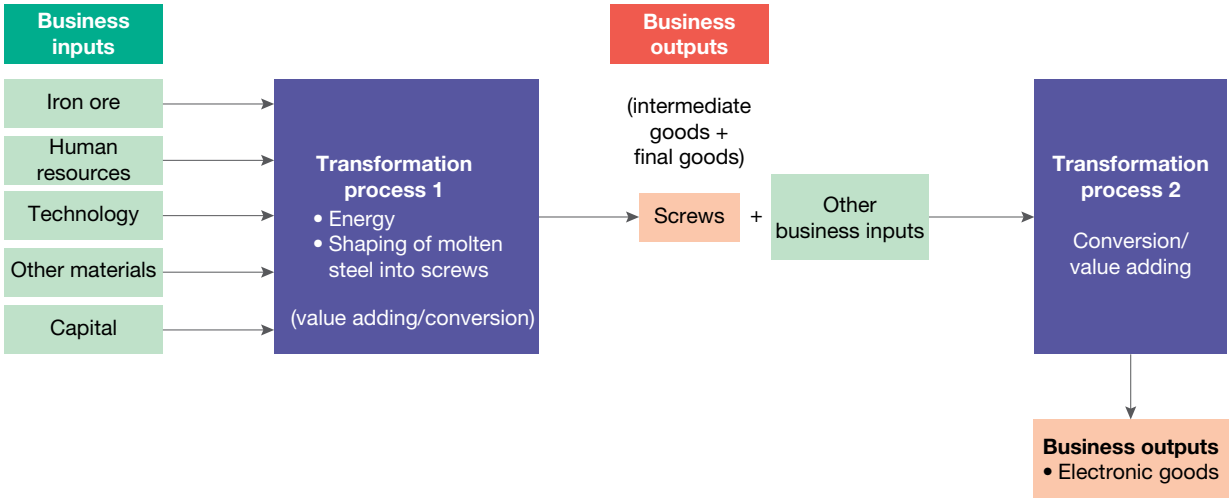
- manage all aspects of quality in the process, from sourcing through to production and distribution
- implement effective inventory management strategies and be highly responsive to market demand in order to minimise waste.

Non-perishable goods can be found in different industries. In the manufacturing sector there are motor vehicles, electrical appliances and audio-visual products, computer-based technologies, clothing, footwear, household goods such as furniture and bedding, kitchen items and tools. Although the variety of goods produced across different industries is huge, many of the operations processes are similar regardless of industry.

Intermediate goods

A feature of some production processes is that goods may be processed more than once because they become inputs that require further processing. Figure 2.4 illustrates the process where a manufacturer produces (adds value) to iron ore in the process of making steel screws. Although the production process ends there for that business, these screws will be used by an electronics manufacturer as an input for the production of its finished goods, adding value to them.

FIGURE 2.4 Intermediate and final goods processing



2.3.2 Services in different industries

As with goods, services can be both standardised and customised. The fast-food industry, as referred to earlier, is an example of an industry that aims to standardise its service. Other services such as those provided by accountants, dentists, doctors and lawyers are generally more customised, in accordance with customer expectations. There are some exceptions such as a general practitioner (GP) who may provide a more standardised service and then refer the patient on to a specialist and hence customised service.

SNAPSHOT

Case study: REA Group — features of operations management for a business in a tertiary industry

How do you keep up with a market changing at the speed of light? The Chief Inventor of an Australian digital company explains how they are using lean to safeguard their future.

REA Group is a digital advertising company specialising in property and the lifestyles that go with it, headquartered in Melbourne, Australia (we are also present in six other countries). We help people buy and rent houses, and find commercial properties for business through our websites and apps, but also get finance and learn about renovation and the market. How we got to become a $9 billion company doing that is quite interesting, and that's the story I'd like to tell in this article.

We have spent the past two decades building a global business, but the truth is that in real estate the only thing that matters is whether you are a great business in your neighbourhood. The challenge for us is to essentially act as if we had 2500 realestate.com.au websites and apps uniquely tailored to each suburb in Australia, and more again for our Asian customers. Sometimes those apps are not for people fortunate enough to be choosing a new home for their family to live in — we also work with homeless people and contributed to the development of an app called Ask Izzy to connect Australia's homeless to resources for them.

Our 20-person Consumer Research Lab — which constantly works on perfecting our offerings based on the key customer expectations of time, transparency and trust — hosts or visits five people every day. That's up to 1000 people a year, which generates a lot of data that we can then use to segment the ecosystem, and understand how to cater to each of its parts (whether it's landlords, renters, investors, renovators or estate agents). We pay these folks to come in, relying on an external agency that recruits individuals from a specific demographic or geographical area, like Perth's Central Business District or a suburb of Adelaide. We interview them, but most importantly observe them as they use our technology.

For example, we might ask them to wear a pair of Tobii glasses that records how they interact with our website or our app (it is fascinating to see how quickly they can scroll through the results and pick up a newly-listed property they haven't seen yet) or we might decide to track their movements and behaviours as they go on a virtual reality walk through an apartment.

We never stop experimenting with technology and we strive to invent something new every day.

A market in transition

Our commitment to research and experimentation is made in response to the dramatic changes our sector is undergoing. The internet has completely transformed the search for real estate, and we are moving closer and closer to a point where rather than search we will be required to facilitate matching properties and information to prospective buyers or renters. For this reason, there is a lot of fear that the role of traditional intermediaries (estate agents) could soon be a thing of the past, and that technology will take their place.

We believe that there is still an important role for people as intermediaries (at least, for good ones), but it is obvious that things have changed a lot in the past few years. A combination of an agent plus technology is becoming the norm to be competitive, and in the future, that tech will also involve more AI. We need to become better channels for people interested in property. Our tools and data sets need to be improved, and some of our value streams will necessarily change.

As ever, the internet has provided both great challenges and great opportunity, and REA Group has largely been able to ride that wave through continuous innovation. In many ways, we have revolutionised the market, but we are now being disrupted by global competitors that were not traditionally property-focused — Google, Facebook, Airbnb, Amazon and WeChat. We are facing the typical innovator's dilemma: can we get our mind around this disruption and create a new, more valuable offering? That's what we are focused on as a company.

Artificial Intelligence will make it possible to complete the transition to matching properties to people: prospective buyers or renters will find the right property in their inbox or home screen notifications when they wake up in the morning, perhaps together with an article on renovating kitchens — perhaps their most pressing need — and

the name and number of a person they can talk to about a mortgage extension for the renovation. Technology in general has really brought a lot of change to our industry: imagine how much time you could save by using virtual reality to view an apartment!

Our journey of transformation

Four years ago, we decided to change the structure of the organisation to become much more customer focused in everything we do, starting from an Agile 'factory' — an ideas factory rather than a manufacturing one, delivering apps and software, not cars. The biggest consequence of the reorganisation was a switch to multidisciplinary teams.

We believe that collaborative learning can achieve incredible things. That's why we pair up programmers and, like at Spotify, we assign our people to small, multifunctional teams — large tribes of 150 people are focused on a customer segment like residential real estate; squads of 10 build products, and guilds that allow a 'craft' or 'trade' such as security engineering to stay in touch and share knowledge across the business silos.

The first lean experiment outside our software development teams was for the team most curious about agile methods, with the toughest waste problem — the lawyers from our Legal team. At the time, with strong demand for their services, we had a huge bottleneck when the process reached them: not only did every deal have to go through them, but our product structure was so complex that each contract was customised. As a team, they regularly worked 70-hour weeks.

After participating in many product stand-up meetings, they decided to try and visualise their own work. They got confirmation that it was a pretty horrific value stream, with what felt like a million steps, and lots of wait time, but for the first time they were able to see the problems. We came to the realisation that the value stream is not complete until the first dollar is paid into a contract, and decided to come up with a system of prioritisation of jobs. A miracle occurred: duplication was reduced, and the bottlenecks started to disappear.

In that instance, we also learned how detrimental interruptions can be (we measured it takes 20 minutes to get back to your regular pace of working after a distraction) and introduced a system by which teams now have a flag that signals the one 'interruptable' person in the group.

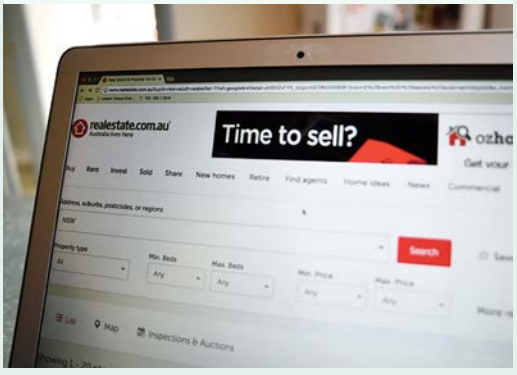
After all this, the lawyers became great ambassadors for a new way of working. As we flipped the company structure to being multidisciplinary, they were deployed as internal consultants supporting every line of business, attending many stand-ups and seeing more and more people asking for their help. They also began to automate legal processes and create self-service tools — humans and technology working in harmony.

People are naturally curious at REA Group, and before too long, our People and Culture team picked it up (they sat next to Legal). Then Finance learned about it, just as they were trying to figure out how to get a new finance system off the ground and needed a quick way to summarise it on a board for their stakeholders and team.

Change reached different parts of the organisation fuelled by curiosity, which is a trait we actively look for in the people we recruit — together with resilience and the ability to think critically. The habits that define us as a company are something you can't avoid learning if you work here: we don't have a manual of the 'REA Way' (much like Toyota didn't have a TPS manual) but encourage sharing at all levels and that's how we create a common culture and set of behaviours. Culture and behaviours are led from the top by our CEO Tracey Fellows, along with creating a sense of challenge and a clear 'why' for our people to engage with. We are changing the way people experience property around the world.

Source: Nigel Dalton, Planet Lean.

REA Group is public listed company that operates Australia's leading residential, commercial and share property websites including realestate.com.au. The business has digital real estate sites and investments in Australia, Asia and North America.



SNAPSHOT

Case study: Snap Laundromat — features of operations management for a business in a tertiary industry

Technology is not used only by businesses that manufacture goods. Businesses that produce services also use technology to improve productivity. Snap Laundromat in Brisbane has introduced an innovative new technology to its washing machines and dryers that enables customers to pay for and operate the laundry services with their smartphones. The founder of Snap Laundromat, Ian McFarlane, created a small network controller about the size of a cake of soap to go inside each machine.

The customer can either swipe a QR code on the machine or visit a website to create an account. Once the account has a balance, the customer can select a dryer or washing machine of their choice. Mr McFarlane said that customers, particularly young people and travellers, have been very quick to take up the new technology. He has started a new business, Eziwash, to make the controllers available to other laundromats. The use of this technology application means that customers can quickly and easily pay for their laundry service, particularly if they do not have cash, and could encourage more people to use the laundromat. Eventually the technology will provide the ability to download customer data and to reward customers for their loyalty.

Use of technology applications can make the customer experience simpler, quicker and more worthwhile.



BizFACT

A business may be large enough to operate each of the key function areas. Alternatively, a business may choose to perform only one or two of the functions in which it is most competent, and hire the services of other businesses to perform the other functional areas. This is seen in the example of Colin's Cafe, a medium-sized shopping centre coffee shop. Managers of this business decided to focus on and specialise in coffee retailing and coffee making. The business hires other businesses to do the accounts, to assist with finding skilled employees and to undertake marketing. The use of external providers in this way is known as outsourcing.

KEY IDEAS

- Goods and services are produced differently.
- Goods may be standardised (mass produced or an assembly line) or customised (varied according to the needs of customers).
- Goods may be perishable or non-perishable.
- The character of the goods will shape the nature of the operations processes.
- Intermediate goods have gone through one set of operational processes then become inputs into further processing.
- Services vary according to whether they are highly specialised or more customised.
- Services can be standardised and in so doing a cost leadership strategy is being applied.

2.3 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

2.3 Quick quiz on | **2.3 Exercise** | **2.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 4, 5, 6, 7, 9	1, 2, 8, 10	11, 12

2.3 Exercise

Revision

1. **Distinguish** between the terms 'standardised' and 'customised'.
2. **How** may goods be customised?
3. **Identify** three goods that are perishable and three goods that are non-perishable.
4. **Describe** how operations processes will be shaped by the need to produce goods that are perishable.
5. **Outline** the role of intermediate goods in the production of other goods and the provision of services.
6. **State** how services can be both standardised and customised.

Read the 'REA Group' and 'Snap Laundromat' case studies and answer questions 7 to 9.

7. **Describe** the characteristics of both businesses.
8. **Explain** how each business uses technology as a means of differentiating its business from the competition.
9. **Outline** the role of interdependence in the businesses.

Extension

10. **Compare** and **contrast** the operations of a manufacturer and a service business.
11. With reference to an example, **assess** whether services can ever really be totally standardised.
12. **Evaluate** the effect of cost leadership on service provision and state whether it reduces the service level provided.

2.3 Exam questions

Question 1 (4 marks)

Distinguish between goods and services and how operations management will differ in the production of each.

Question 2 (4 marks)

Outline two methods used to differentiate between goods and services.

Question 3 (2 marks)

Why is it sometimes difficult to distinguish between goods and services?

Question 4 (3 marks)

What is standardisation? Explain why standardisation is used by businesses.

Question 5 (5 marks)

Analyse the sources of differentiation in goods produced by business.

More exam questions are available in your learnON title.

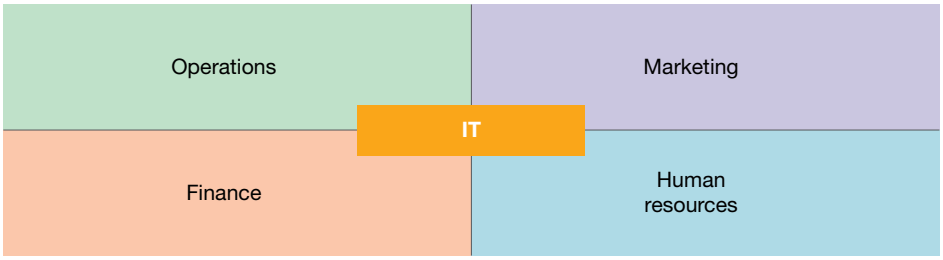
2.4 Interdependence with other key business functions

SYLLABUS LINK In this subtopic you will learn about interdependence with other key business functions. You will learn to assess the relationship between operations and key business functions in two actual businesses.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

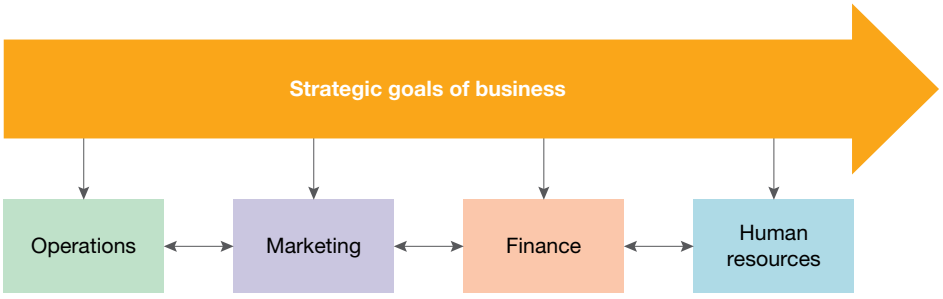
Figure 2.5 identifies the range of key business functions for a business. Although a business can separate the key business functions into departments that perform their distinct roles, the functions are interdependent — each relies on the others to perform effectively.

FIGURE 2.5 The range of typical business functions



Interdependence refers to the mutual dependence that the key business functions have on one another. This means that the various business functions work best when they work together. A soccer team might have highly specialised players, for instance a brilliant left wing, a superb fullback and a dynamic goalkeeper. However, despite their individual brilliance, a side will usually win when all players contribute to the game, each working with the others in the team, passing, communicating and playing for the same victory. In the same way, each section of the business may perform its specialised function extremely competently, but if together they do not work as a 'team' and aim for the same business goals, the business is not likely to achieve its objectives. Interdependence occurs when each key business function area is committed to the same business goals as the other key areas and they each work in a coordinated and collaborative way to achieve these goals as shown in figure 2.6.

FIGURE 2.6 Interdependence and cross-coordination of business functions to achieve strategic goals



2.4.1 Tasks within the key business functions

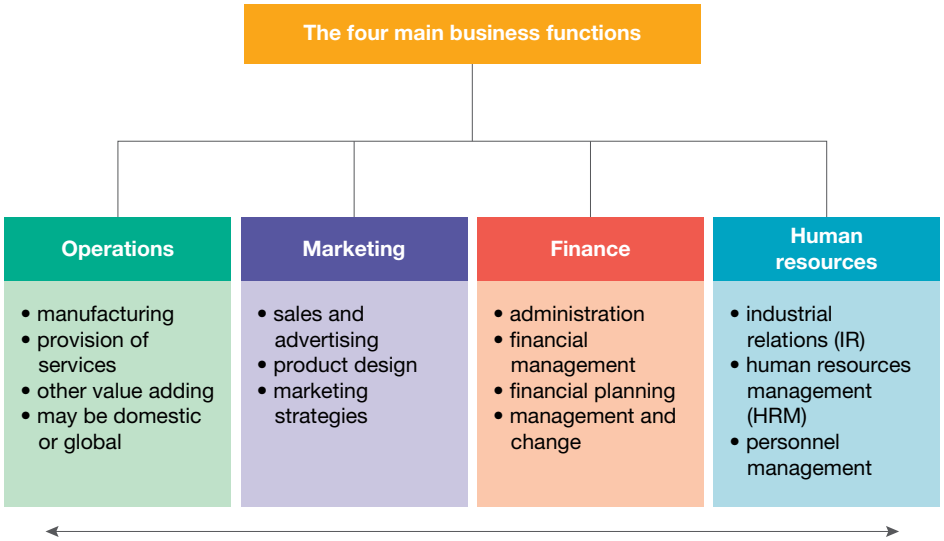
In most businesses, closely related tasks are grouped together. Sales and marketing are grouped, finance and administration are grouped, and operations and research and development (R&D) are grouped. Consequently, the range of functions is generally reduced to four main functions as shown in figure 2.7.

interdependence the mutual dependence that the key business functions have on one another

BizFACT

Information technologies or 'IT' is sometimes a discrete department within a business. However, the activities of the IT section affect each key area of business as technology is pervasive through a business enterprise. Operations uses computer-based technology in planning and processing, scheduling, inventory management, quality management and all other aspects and activities. Marketing uses IT software to assess market trends, design products, design communications, create visual stimulus and so forth. Finance uses technology to record transactions and summarise trading into reports that can then be assessed. Finance also uses mathematical modelling to predict and evaluate.

FIGURE 2.7 These key functions are interdependent.



These key functions are interdependent (i.e. they all overlap) and each relies on the other. In many business, they are separate functions. This is particularly true of large businesses. The word 'synergy' is often applied in order to describe the benefits of interdependence. Synergy means 'the whole is greater than the sum of all the individual parts'.

Operations

Operations, as we have already discussed, refers to the business processes that involve transformation or, more generally, 'production'. It is a term that applies both to the manufacturing and services sector. In manufacturing, operations refers more specifically to the processes involved in turning raw materials and resources into outputs of finished goods or products.

Marketing

Marketing is about meeting the needs and wants of consumers through provision of products (both goods and services) at prices that the market is prepared to pay. Marketing is a highly specialised field of business that looks at all aspects of buying and selling, including the psychological processes that people go through when thinking about purchases. From the analysis of why people buy, to pricing, product development, promotion and distribution, marketers attempt to maximise the earning capacity of their businesses through sales.

Marketing and operations are interdependent and where marketing is concerned about the design of products, and their subsequent sale, to meet the needs of consumers, the operations function involves the acquisition or sourcing of products for resale or the sourcing of inputs for production. Thus, the requirement of product design (a marketing requirement) directly affects the operations function.

Finance

The finance function is concerned with recording and summarising financial transactions into a series of reports that can be easily interpreted. Reports such as income statements (also called revenue or profit and loss statements), which determine the amount of money the business has earned after its expenses have been paid, are very useful to managers and other stakeholders. Other key reports include balance sheets and budgets. These reports provide crucial information to decision makers both within and outside of the business.

A key marketing objective is profitability. **Profitability** requires that a business maximise sales (revenue) and minimise costs (expenses). The operations function is that aspect of business that involves production, and if costs can be minimised then profit margins can be increased. Similarly, if operations processes focus on quality then the resulting products can be sold at higher prices and generate increased revenue.

profitability the excess of revenue or income over expenses or costs

Human resources

The human resources function incorporates all aspects of employment resourcing and includes acquiring, developing, maintaining, motivating and separating staff. Effective human resource management is vital because people are now recognised as the single most important resource for a business. Operational change results in the use of new technologies that are enabling faster processing speeds and changing the way that work is done. This has a direct effect on the human resources within a business. As the nature of work changes, so too do the skills and qualities sought in employees.

FIGURE 2.8 Successful businesses recognise that they rely on the quality of their employees to achieve their goals of profit maximisation, growth and increased market share. People are the business's most valuable resource, so it is important to take care to recruit and maintain the best people.



2.4.2 The relationship between operations and the other key business functions

SNAPSHOT

Case study: Wild Horses Café and Aldi — the relationship between operations and the other key business functions in two actual businesses



At the Wild Horses Café the owner, Jenni, knows that most sales of coffee are made in the morning and early afternoon. Her busiest days are Friday to Sunday and her café is closed on Mondays. Jenni ensures that she pays suppliers for her weekly order each Tuesday so that stock is delivered by Thursday morning. This requires Jenni to ensure she has cash on hand to pay for supplies when she orders. Jenni manages five part-time and casual staff and rosters more staff for work on the weekends and in the weekday mornings when she is busiest. She knows that the volume of orders directly affects income and requires appropriate staffing. Recently, in response to changing coffee tastes, Jenni expanded the range of coffee beans and flavours that she orders. This required leasing a larger coffee machine and purchasing an additional grinder. As a result of this expansion in product offerings, Jenni's café has experienced a surge in sales and she is currently hiring another barista and two new waitstaff.

Aldi

Aldi has been in the Australian market since 2001 and in almost 20 years has grown to become the third largest grocery supplier in Australia, having taken market share from Coles and Woolworths. Aldi operations was carefully planned as the managers knew that strategic growth would take about ten years. The long-term growth strategy meant that Aldi had to invest significant amounts of finance and capital into setting up supply lines and building warehouses to assist supplying the stores with both the perishable and durable goods it sells.

Aldi has attracted loyal customers through its 'special buys' promotions. These promotions involve selling household items at below cost twice a week. Aldi needs to source this stock and have it ready for sale at each of its more than 500 stores nationwide. The operations function has to work closely with marketing and finance in sourcing what customers desire at a price they deem attractive. Aldi continues to grow rapidly despite having only 1600 product lines for sale. Coles and Woolworths are losing market share to Aldi even though each of these grocery brands has tens of thousands of consumer goods for sale in-store. The interdependence of key business functions, understood by smart managers (sourced by human resources) continues to build Aldi's brand in Australia.

KEY IDEAS

- The range of typical business functions is operations, marketing, finance and human resources.
- Interdependence refers to the mutual dependence that each of the key functions have on one another. This means that the various business functions work best when they work together.
- In most businesses, closely related tasks are grouped together — for example, sales and marketing, finance and administration, and operations and research and development.
- Operations refers to the business processes that involve transformation or, more generally, 'production'.
- Marketing is about meeting the needs and wants of consumers through provision of products (both goods and services) at prices that the market is prepared to pay.
- Reports such as income statements, which determine the amount of money the business has earned after its expenses have been paid, are very useful to managers and other stakeholders.
- The function of human resources is to deal with the people the business employs and the issues arising from their employment.

2.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

2.4 Quick quiz on | **2.4 Exercise** | **2.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 5	2, 6	7, 8, 9, 10, 11, 12

2.4 Exercise

Revision

1. **What** is meant by the term 'interdependence'?
2. **Explain** how interdependence occurs between the key business functions.
3. **State** the benefits of interdependence.
4. **Summarise** the role of the (a) marketing, (b) finance, (c) human resources functions in a business.

Read the 'Wild Horses Café and Aldi' case study and answer questions 5 to 9.

5. **List** the four key business functions.
6. **How** does Jenni manage the interdependence of key business functions at Wild Horses Café?
7. **Assess** the relationship between operations and the other key business functions at Wild Horses Café.
8. **What** role has strategy played in the growth of Aldi in Australia?
9. **Assess** the relationship between operations and the other key business functions at Aldi in Australia.

Extension

10. **Evaluate** the role of business strategy and its importance to the coordination of the key business functions. In your answer discuss the concept of synergy.
11. **Assess** the role of IT across the range of business activities.
12. With reference to businesses that you are familiar with, **analyse** the nature of interdependence across the key business functions.

2.4 Exam questions

Question 1 (4 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q22d

Explain the interdependence of finance and operations in a business. Support your answer with relevant examples.

Question 2 (2 marks)

Outline the interdependence of finance and operations.

Question 3 (1 mark)

One department of a large business has identified an opportunity to position its product range as having a quality above the competition. The operations team will now design an innovative product. This is an example of operations and interdependence with which other key function?

A. Finance
B. Marketing
C. Human resources
D. Research and development

Question 4 (6 marks)

Steep Software Solutions is a large business. Team leaders of operations, marketing and human resources meet to discuss how each key function is interdependent. Explain the interdependence between operations and the other key functions.

More exam questions are available in your learnON title.

2.5 Review

2.5.1 Summary

Strategic role of operations management

- Operations management is an essential key business function that overlaps with the other business functions such as marketing, finance and human resources management (HRM).
- There are several different sources of operations costs in business. There are input costs, processing or transformation costs and the costs of getting products to markets.
- Cost leadership involves aiming to have the lowest costs or to be the most price-competitive in the market.
- Good/service differentiation means distinguishing goods or services in some way from their competitors.
- Standardisation involves producing homogeneous goods and services and is usually a high-volume, low-cost approach.
- Sources of differentiation in goods include:
  - varying the actual features, quality and/or augmented features
- Sources of differentiation in services include:
  - varying the amount of time spent on a service
  - the level of expertise offered
  - self-service options
  - flexibility
  - no fuss
  - quality of materials or technology used in the delivery of the service.
- For both goods and services, differentiation can be created from cross branding or strategic alliances.

Goods and services in different industries

- Goods and services are produced differently.
- Goods may be standardised (mass produced or an assembly line) or customised (varied according to the needs of customers).
- Goods may be perishable or non-perishable.
- The character of the goods will shape the nature of the operations processes.
- Intermediate goods have gone through one set of operational processes then become inputs into further processing.
- Services vary according to whether they are highly specialised or more customised.
- Services can be standardised and in so doing a cost leadership strategy is being applied.

Interdependence with other key business functions

- The range of typical business functions is operations, marketing, finance and human resources.
- Interdependence refers to the mutual dependence that each of the key functions have on one another. This means that the various business functions work best when they work together.
- In most businesses, closely related tasks are grouped together — for example, sales and marketing, finance and administration, and operations and research and development.
- Operations refers to the business processes that involve transformation or, more generally, ‘production’.
- Marketing is about meeting the needs and wants of consumers through provision of products (both goods and services) at prices that the market is prepared to pay.
- Reports such as income statements, which determine the amount of money the business has earned after its expenses have been paid, are very useful to managers and other stakeholders.
- The function of human resources is to deal with the people the business employs and the issues arising from their employment.

2.5.2 Key terms

cost centres particular areas, departments or sections of a business to which costs can be directly attributed
cost leadership involves aiming to have the lowest costs or to be the most price-competitive in the market
customised goods those that are varied according to the needs of customers. These goods are produced with a market focus rather than a production focus.
interdependence the mutual dependence that the key business functions have on one another
operations the business processes that involve transformation or, more generally, 'production'
product differentiation distinguishing products (goods or services) in some way from those of competitors
profit centres those aspects of a business that directly derive revenue and profits
profitability the excess of revenue or income over expenses or costs
standardisation refers to the making of products that are homogeneous or identical
standardised goods those that are mass produced, usually on an assembly line. Standardised goods are uniform in quality and meet a predetermined level of quality. These are generally produced with a production focus.
strategic refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

Resources

Digital documents	Key terms glossary (doc-35656) Chapter crossword (doc-36210)
Interactivity	Chapter crossword (int-7149)
Exam question booklet	Chapter 2 Exam question booklet (eqb-0024)

2.5 Activities

learnON

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Exercise 1: Multiple choice questions

1. Which of the following terms best describes operations in business?
   - **A.** Transformation and creation of value
   - **B.** Production and distribution
   - **C.** Transformation and marketing
   - **D.** Manufacturing and services

2. Which of the following is *not* a business output?
   - **A.** Labour
   - **B.** Goods
   - **C.** Services
   - **D.** Waste

3. Which of the following is *not* a customer focus?
   - **A.** Focus on affordability
   - **B.** Responding to changes in consumer needs
   - **C.** Lean production
   - **D.** Excess inventory

4. One challenge for management is balancing the need to minimise production costs with which of the following?
   - **A.** Increasing market share
   - **B.** Maximising profitability
   - **C.** Achieving ecologically sustainable practices
   - **D.** Overproduction

5. Minimising waste is an outcome of which of the following?
   - **A.** The Fair Trade movement
   - **B.** Business innovation
   - **C.** Consumer advocacy for ecologically sustainable production
   - **D.** Business drive to maximise profits

6. Operations management is a strategic business function because of which of the following?
   - **A.** It affects all key business areas.
   - **B.** It takes a long time to implement.
   - **C.** It is critical to maximising revenue.
   - **D.** It is critical to reducing cost.

7. Which of the following is correct in terms of standardised goods?
   - **A.** Varied according to the needs of customers
   - **B.** Produced with a market focus
   - **C.** Respond to the needs of customers
   - **D.** A and B

8. Operational processes for non-perishable goods are which of the following?
   - **A.** Often vary greatly between industries.
   - **B.** Require planning to avoid overproduction.
   - **C.** Require very short lead times.
   - **D.** Must incorporate robust packaging and storage.

9. Finance includes which of the following?
   - **A.** Expenses and promotion
   - **B.** Buying and selling
   - **C.** Maintenance and separation of staff
   - **D.** Balance sheets and recording of financial transactions

10. Human resources does include which of the following?
    - **A.** Analysis of buying behaviour
    - **B.** Acquiring and developing staff
    - **C.** Reports to stakeholders
    - **D.** Promotion and distribution

Exercise 2: Exam practice questions

Question 1 (8 marks)

1. **What** is strategic operation management? **(2 marks)**
2. Refer to a business you have studied and **evaluate** the role of strategic management in its operations. **(6 marks)**

Question 2 (4 marks)

Explain the role of cost leadership and good/service differentiation in strategic operations management.

Question 3 (8 marks)

1. **Identify** TWO costs within the operations function. **(2 marks)**
2. **Analyse** the role of cost leadership in operations management. **(6 marks)**

Question 4 (4 marks)

Distinguish between goods and services and how operations management will differ in the production of each.

Question 5 (6 marks)

Assess the relationship between operations and the other key business functions for two businesses.

Question 6 (4 marks)

Discuss the balance between cost and quality in operations strategy.

Resources

Teacher-led video Chapter 2 Exam practice solutions (tlvd-2931)

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3 Influences on operations management

3.1 Overview

LEARNING SEQUENCE

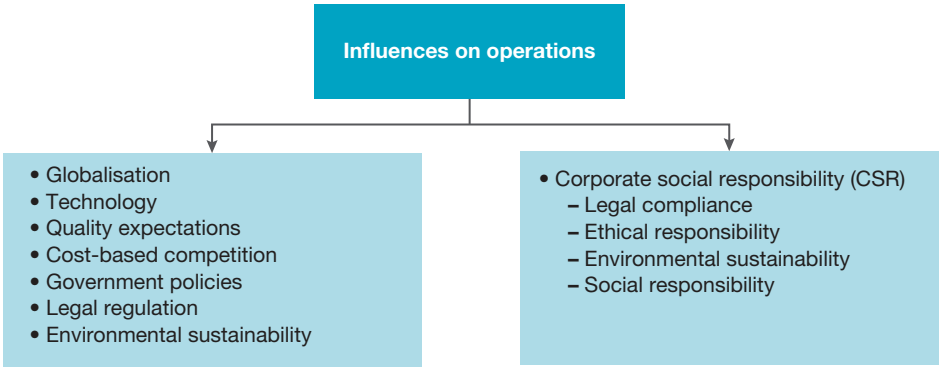
3.1 Overview
3.3 Globalisation and technology
3.4 Quality expectations and cost-based competition
3.5 Government policies and legal regulation
3.6 Environmental sustainability and corporate social responsibility
3.7 Review

3.1.1 Introduction

Operations provides an important contribution to business success and is therefore a significant business function. It follows that the role of operations management extends to ensuring that the business sustains any success, whether it be engaged in the extraction of raw materials (primary industry), production of goods in the case of secondary or manufacturing industry, and/or providing services (tertiary industry).

When managing the role of operations, the business's decision makers across all levels of management will be negotiating any challenges that the internal and external business environment might present. These influences will be dynamic and the scope for change will be ever present and front of mind for many managers. There is a range of influences that impact the operations function and these are identified in figure 3.1.

FIGURE 3.1 Influences on operations



on Resources

Digital document Key terms glossary (doc-35658)
Exam question booklet Chapter 3 Exam question booklet (eqb-0025)

3.2 Globalisation and technology

SYLLABUS LINK In this subtopic you will learn about how globalisation and technology influence operations.

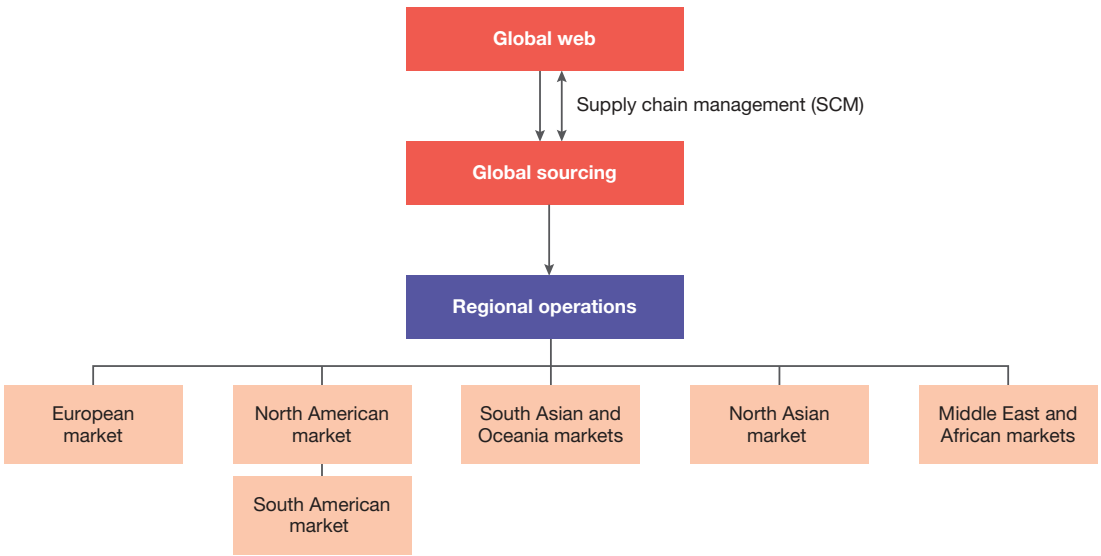
Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

3.2.1 Globalisation

Globalisation refers to the removal of barriers of trade between nations. Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and/or machinery), labour, intellectual capital and ideas, financial resources and technology. From a business perspective, globalisation provides a source of market opportunities both from other nations and to other nations Globalisation can also act as a threat to business as businesses that effectively apply cost leadership principles can undercut the market and dominate.

Globalisation is a significant influence on the operations function. Large businesses are increasingly orienting their practices towards the global market, with a view to meeting the needs of global consumers. Global consumers seek global brands and tend to seek standardised products. This significantly affects the operations function, which is then structured around a series of global production facilities. Figure 3.2 indicates how operations can be organised around the needs of a global market.

FIGURE 3.2 The organisation of operations to meet the needs of a global market based on the global web: a network of production sites located around the world



The following processes are all features of global businesses that seek to target global markets: product design, which must meet the needs of global consumers, the choice of location for manufacturing facilities, the management of quality, and logistics and inventory management processes.

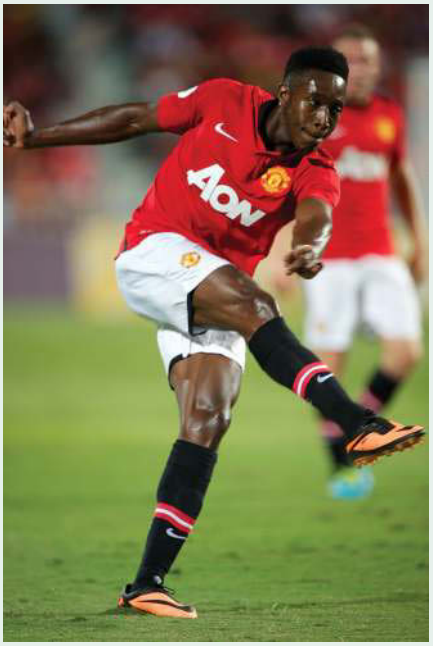
The use of manufacturing plants for the production of goods means that a business can achieve economies of scale advantages. This is evident with businesses like Apple, which has its electronic goods designed in the United States of America, but manufactured in China and then sold globally.

globalisation refers to the removal of barriers of trade between nations. Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and/or machinery), labour, intellectual capital and ideas, financial resources and technology.

The production of services on a global scale within sectors such as finance, travel and tourism, software development and telecommunications also has significant implications for operations processes. AON is an insurer that has effectively created a global insurance brand from the sale of high-quality business insurance products and other business solutions. It seeks to provide a standardised suite of insurance options for customers globally.

SNAPSHOT

Case study: AON — global insurer



AON is a niche provider of insurance, human resources solutions and also of outsourcing for businesses. As a global business it operates in 120 countries and employs over 50 000 workers. AON is mainly a broker for business insurance so it is not well-known in the Australian market, despite exceeding its goals for growth consistently since it entered the domestic market. AON's global brand has been enhanced hugely with its sponsorship of the Manchester United Football Club. According to AON media the company has 'been named repeatedly as the world's best broker, best insurance intermediary, reinsurance intermediary, captives manager and best employee benefits consulting firm by multiple industry sources'.

While AON operates in 120 different markets, it can standardise a large proportion of its product and then make slight variations that meet the specific needs of diverse local markets. In this way many of the 'back-end' business processes can be standardised. This makes AON a strong business partner for global businesses operating in multiple jurisdictions. The consistency of protocols, high internal standards and focus on quality make AON operations reliable and predictable. In this way AON is growing from strength to strength.

SNAPSHOT

Case study: Zara — globalisation and its impact on operations



The popular brand Zara is owned by a company called Industria de Diseño Textil (Intidex). It was founded in 1974, opened its first store in 1975 and initially expanded into Europe and the United States before expanding into Latin America (1992) and Asia (2005). Zara has 2249 stores operating in 96 markets. In 2019 it had $20 billion in sales.

The company is a part of what is called the 'fast fashion' industry. The fast fashion industry is divided into two types of business: those that manufacture their own clothes and those that source and brand clothes produced by other businesses. Zara's competitors H&M and GAP are companies that buy clothes from other manufacturers. Zara, however, grew through its development of localised production in Spain, Morocco, Portugal and Turkey. Though more recently, Zara has started to allow some offshore production, more than 65 per cent of all of its clothes are made in Europe or Morocco. Zara's founder Amancio Ortega believes that production proximity and quick logistics are two contributors to its global success.

All Zara stock, regardless of where it is made, must pass through the Spanish production and distribution plant. This main production and distribution facility employs over 6000 staff and uses very well-designed logistics and distribution lines. Clothes from here are distributed globally within 48 hours, meaning that there is no need for any local warehousing in the 96 markets where it sells its apparel and accessories.

Some of the source nations for fabrics include: Vietnam, Bangladesh, Morocco, China and Thailand. The company has about 1985 suppliers and 8155 factories and manages them through a highly centralised control of production. Sourcing globally reduces costs, as does keeping stock moving quickly rather than storing it in a warehouse.

Even though, more recently, Zara has started to outsource some production, it does not tend to mass produce and hence does not realise the economies of scale some other businesses might. Instead, it keeps production volumes low and moves them quickly to the market. It has also changed the production cycle by designing over 1000 new garments per month, rather than seasonally. The garments made from these designs are responsive to market trends as the business has over 200 designers that interact with consumers globally. New products are launched into Zara's global stores every two months.

Zara uses its global proximity to its markets and well-designed logistics to ensure that customers feel valued. Surveys indicate that on average Zara customers visit stores 17 times per year. This is a far higher number of store visits than those made by loyal customers to competing businesses.

3.2.2 Technology

Technology plays a significant role in the application of the operations function of business. **Technology** is the design, construction and/or application of innovative devices, methods and machinery upon operations processes. People are generally familiar with a wide range of technologies, both personal and household. Smartphones, laptop and desktop computers, gaming consoles and security devices are examples of widely available forms of technology. Such technologies enable people to communicate more easily and facilitate improved business processes. In this way, technology can be seen to be both a range of devices and also having a role in the support of enabling *processes* and applications.

Technology can be applied to, and integrated with, the range of processes that characterise the operations function in business. At an administrative level, examples of technology such as those identified in table 3.1 assist with organisation, planning, decision making and control of operations processes. At a processing level, technology is used in manufacturing, logistics and distribution, quality management, inventory management, supply chain management and sourcing, as outlined in the case study on Zazzle.

TABLE 3.1 An overview of some of the technology used in operations processes

Technology used in the administration of operations	Technology used in the range of operations processes
• Planning technologies: materials requirement planning (MRP), Gantt charts, critical path analysis (CPA) and other scheduling and sequencing tools • Office technologies such as computers (desktop and laptop), scanners, telephone systems and mobile phones • Software such as wordprocessing, graphics packages, spreadsheet, graphing, multimedia and desktop publishing programs	• Large machinery in manufacturing plants such as those typical of assembly line production • Robotics in highly sophisticated production processes requiring great precision • Computer-aided design (CAD), computer-aided manufacture (CAM) and computer-integrated manufacturing (CIM) technologies • Rapid manufacturing (RM) and tooling technologies

technology the design, construction and/or application of innovative devices, methods and machinery in operations processes

SNAPSHOT

Case study: Zazzle — using technology to boost operations



Zazzle is a business that helps consumers make customised products. The web-based company launched in 2005 and has a private company legal structure. Its Head Office is in California, United States, with a newly established European base in Ireland.

Customers order their customised products online; Zazzle manufactures to order and so hires people based on their capacity for design. Annually the company hires thousands of people across three different manufacturing plants.

Zazzle seeks to make on-demand products within 24 hours from the receipt of an order. It manufactures and creates custom designs in each of the following product areas: invitations and cards, homewares, clothing, accessories, home and living, office, baby and kids, art, weddings and gifts. Under each of these broad product categories there are subcategories, examples of which are shown here for the clothing and accessories product lines.

Clothing includes t-shirts, underwear, shoes, tank tops, hoodies, activewear, jackets, dresses, maternity wear, sweatshirts, jerseys, leggings and polos.

Accessories includes bags, watches, keychains, jewellery, hats, buttons, wallets, sunglasses, compact mirrors, scarves, athletic headbands, luggage tags, ties, tie bars, lapel pins, cufflinks, button covers, belt buckles, luggage handle wraps, hair ties, money clips, nail art, passport holders, temporary tattoos and belts.

All of the design options are pre-set. For example, if a person wants a custom-designed frisbee, they can choose between five colour options and can upload their own image and text to go onto the frisbee. Alternatively, a customer may opt for an individually designed item that can be purchased after browsing.

For this niche business, the model relies on insightful business partnerships and innovative design strategies that utilise technology from ordering to despatch, and through product design and customisation. Other important aspects of technology use relate to the use of a shopping cart, adaptive databases that match a customer's previous purchasing choices with suggested options and secure payment systems. Distribution involved further investment in technology.

Zazzle has a number of licences with companies and trademarked brands such as Disney, Harry Potter, Sesame Street and Looney Tunes.

Customisation requires the use of innovative technology and a flexible and creative labour force. The company has spent millions of dollars on enabling technologies to help customers design almost every imaginable consumer good, from custom-made chocolate to customised jewellery.

KEY IDEAS

- Globalisation is a reference to the removal of barriers of trade between nations.
- Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and machinery), labour, intellectual capital and ideas, financial resources and technology.
- Globalisation has significantly affected the operations function of large and global businesses.
- Globalisation affects consumers who seek global brands and this, in turn, shapes the operations function.
- Technology plays a very important role in operations — from administration, through to all operations processes.

3.2 Activities

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3.2 Quick quiz on	3.2 Exercise	3.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 6, 8, 12, 13, 14, 16, 17, 19	4, 5, 7, 9, 10, 15, 18	11, 20

3.2 Exercise

Revision

1. **What** is meant by the term 'globalisation'?
2. **State** two features of globalisation.
3. **Recall** two opportunities that globalisation represents to the operations function in business.
4. **How** does globalisation affect the operations function of a business?
5. **How** does globalisation act as both an opportunity and a threat to businesses?

Read the 'AON — global insurer' case study and answer questions 6 to 8.

6. **What** does AON do?
7. **Explain** how standardisation can improve overall quality standards.
8. **Outline** features that make AON's operations reliable.

Read the 'Zara — globalisation and its impact on operations' case study and answer questions 9 to 11.

9. **How** does globalisation assist with Zara's production decisions?
10. **Why** has Zara decided to manufacture its garments in close proximity to its markets?
11. **Determine** how well-designed logistics helps Zara to minimise costs.
12. **Define** the term 'technology'.
13. **List** four forms of technology found in a typical household.
14. **What** is one advantage of using communications technology?
15. **How** does technology affect the operations function of a business?

Read the 'Zazzle — using technology to boost operations' case study and answer questions 16 to 19.

16. **When** was Zazzle established?
17. **List** two examples of customised goods Zazzle offers to the market.
18. **Describe** the importance of customisation to the market.
19. **What** impact does licensing from trademarked brands have on Zazzle?

Extension

20. Wendy's Windows must decide whether to establish a factory to make a component or contract the manufacturing to an independent supplier. **Discuss** the advantages and disadvantages of each option. **Select** which of the two options is more efficient and **justify** your choice.

3.2 Exam questions

Question 1 (2 marks)

The operations of a business include any activity that converts, adds value or is a work in progress. Describe TWO influences on the operations of a business.

Question 2 (1 mark)

Source: HSC 2006 Business Studies Exam, Section II, Q23a

Aussie Machinery and Farm Supplies (AMFS) was nominated for the 2005 Australian Exporter of the Year Award. AMFS has a reputation for superior environmentally responsible products and quality customer service, which it has used to market its products internationally. Its global network comprises manufacturing facilities in over 50 countries and it employs 1600 workers. The AMFS research and development team has designed a petrol-saving device that will ensure continued growth of the business.

Identify ONE feature of globalisation.

Question 3 (2 marks)

Outline how technology influences operations.

More exam questions are available in your learnON title.

3.3 Quality expectations and cost-based competition

SYLLABUS LINK In this subtopic you will learn about how quality expectations and cost-based competition influences operations.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

3.3.1 Quality expectations

One of the more important goals of the operations function of business is the expectation of quality. **Quality** refers to how well designed, well made and functional goods are, and the overall degree of competence with which services are organised and delivered.

quality a specific reference to how well designed, well made and functional goods are, and the degree of competence with which services are organised and delivered

Quality and expectations cannot be separated. People have an inherent belief in what the quality standards should be for products and their personal level of satisfaction with their purchase decision will indicate whether quality expectations have been met.

SNAPSHOT

Case study: Tiffany & Co. — quality expectations



Global high-quality jeweller Tiffany & Co. has been operating since 1837. The company's reputation is based on its very high quality standards. The company is also known for the high quality of diamonds it sources and for its conservatively contemporary designs.

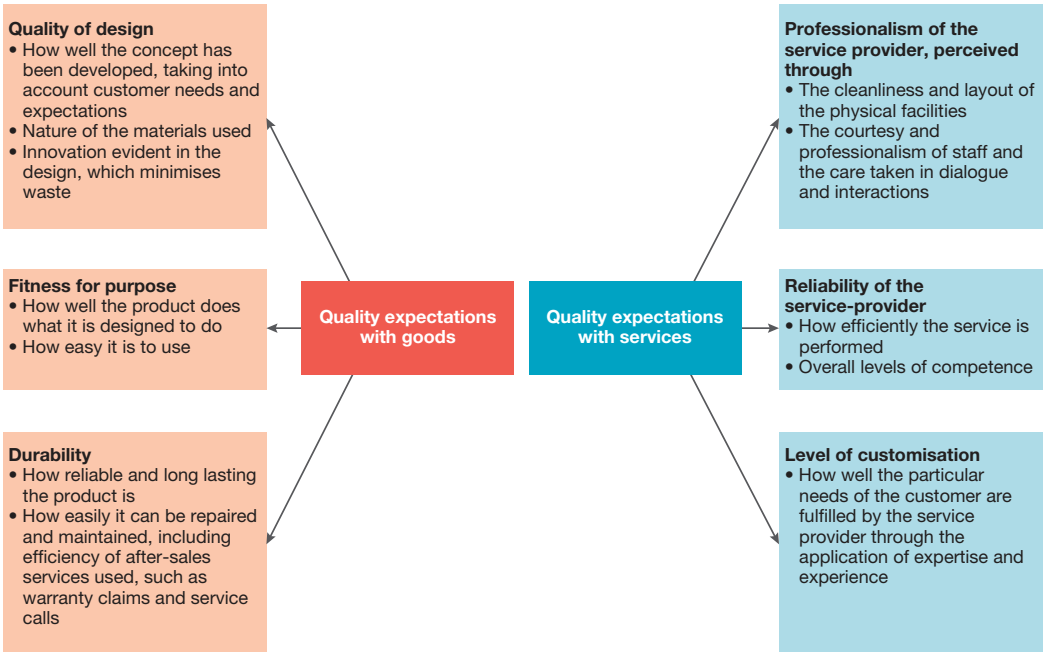
The reputation of Tiffany & Co. has been enhanced through films and popular songs; for example, in the opening scene of the famous 1961 movie *Breakfast at Tiffany's* and other movies such as *Sweet Home Alabama* and *Sleepless in Seattle*. The quality of Tiffany & Co. products is such that if a product fails in terms of expected quality, the company will replace, repair or refund at no cost every time.

Quality products arise when a business has quality processes. Tiffany & Co. has sourcing partnerships (for example, with De Beers diamonds, the world's highest quality diamond merchant) and internal processes that emphasise quality.

High quality has been the cornerstone of the reputation built up by Tiffany and Co., which has in turn generated an expectation by its customers that these standards will always be met.

Within the operations function, quality informs all operations processes. The expectations that people have of businesses determine the way that products are designed, created and delivered to customers. Clearly, this implies that operations processes must follow particular standards or prescribed minimum levels of excellence. Quality expectations in operations may be summarised into several key features that customers often identify — be they goods or services — and these are identified in figure 3.3.

FIGURE 3.3 Distinguishing between quality expectations in goods and quality expectations in services



3.3.2 Cost-based competition

Another significant influence on the operations function arises from the actions of competitors and the way they price their products. In highly competitive markets, cost-based competition can shape the operations function in competing businesses. **Cost-based competition** is derived from determining breakeven point (the level at which the firm's total revenue is exactly equal to its total costs) and then applying strategies to create cost advantages over competitors. Cost-based competition recognises that opportunities for price increase are limited; therefore, reducing costs is a way to maximise profits.

cost-based competition derived from determining breakeven point (the level at which the firm's total revenue is exactly equal to its total costs) and applying strategies to create cost advantages over competitors

fixed costs costs that are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business.

variable costs costs that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy.

Cost-based competition and operations

Cost-based competition is a feature of operations decisions when businesses decide upon a cost leadership approach to the operations function. That is, they focus on reducing costs to a minimum while maintaining profit margins.

In applying a cost leadership approach to business operations (see the following case study), costs may be divided into those that are fixed and those that are variable. **Fixed costs** are not dependent on the level of operating activity in a business. This means that whether the business increases, decreases or maintains production output, these costs remain unchanged. Examples of such costs are building leases and insurance costs. By contrast, **variable costs** are those that change in direct relationship to the levels of output. Such costs include labour and energy costs.

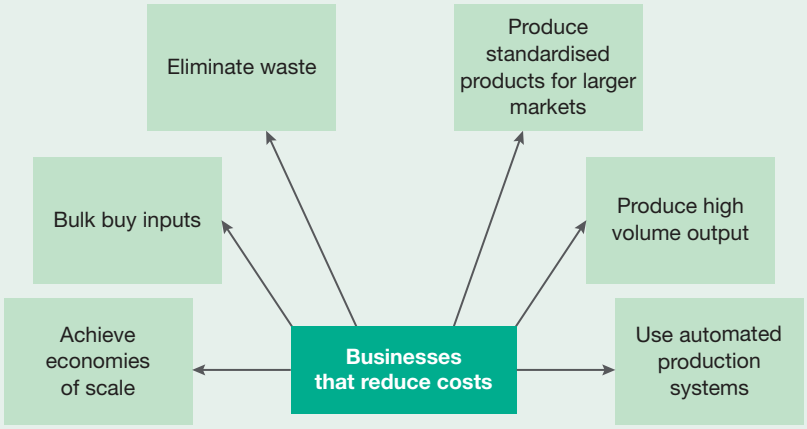
SNAPSHOT

Case study: Kmart, Target and Big W — cost-based competition

Cost-based competition can be seen by customers in the pricing applied by Kmart, Target and Big W — the three main department stores in Australia. When prices for the consumer are low, then the supply chain and procurement strategies applied within the operations functions are efficient.

Each of the three businesses draws inventory from low-cost nations overseas such as China, India and Vietnam. The large volume of turnover generated by each of the businesses enables economies of scale in the supply chain.

Reducing costs can be done a number of ways as shown in the diagram below.



Operations managers in businesses that compete on cost prioritise their decision making based on reducing costs and improving productivity by:

- ensuring stable production processes with limited interruption
- ensuring all resources are used to their optimum advantage
- constantly looking for opportunities to streamline production processes
- updating facilities and equipment with new, more efficient technology
- providing training and development to improve the skills and capabilities of employees.

KEY IDEAS

- Management of quality expectations in both the manufacture of products and the delivery of services is a goal of operations management.
- Quality expectations differ between goods and services.
- Whether quality expectations relate to goods or services, in both cases they lead to consumers having a perception about the standard of products, and accordingly consumers will be prepared to pay a higher price for higher quality.
- Another factor affecting and shaping operations is cost-based competition. Here a business can apply cost leadership to reduce both fixed and variable costs.

3.3 Activities

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3.3 Quick quiz on	3.3 Exercise	3.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
4, 7, 8, 10	1, 2, 3, 5, 6, 9	11, 12, 13

3.3 Exercise

Revision

1. **Explain** how a person's expectations can affect how they view quality.

Read the 'Tiffany & Co. — quality expectations' case study and answer questions 2 and 3.

2. **Account** for the basis of Tiffany & Co.'s reputation.
3. **How** does Tiffany & Co. meet customers' quality expectations?
4. **What** is the relationship between quality and price?
5. Review the list of quality expectations in figure 3.3, for both goods and services also shown below:
   - Quality of design
   - Fitness for purpose
   - Durability
   - Professionalism of the service provider
   - Reliability of the service provider
   - Level of customisation

   a. **Reorder** this list of quality expectations, for both goods and services, from least to most important.
   b. **Justify** the order you chose.
6. **How** does cost leadership affect price?
7. **Clarify** how cost-based competition affects the operations function of business.

Read the 'K-mart, Target and Big W — cost-based competition' case study and answer questions 8 to 10.

8. **State** two strategies that can be applied by businesses to reduce supply side costs.
9. **Explain** how economies of scale can lower costs.
10. **Identify** four means by which operations managers can improve business productivity.

Extension

11. **Analyse** the meaning of quality with reference to a motor vehicle brand. Do this by tabulating the cost and features of different types of motor vehicles (some low priced and some high priced).
12. Compile a list of five major fuel outlets. **Evaluate** the effect of cost-based competition on fuel retailers (refer to brands).
13. a. Distinguish between fixed and variable costs.
    b. Explain which costs vary as scale of production increases.
    c. **Assess** the circumstances under which fixed costs can vary. (*Hint:* Think of a situation in which a business grows rapidly and needs additional facilities and machinery).

3.3 Exam questions

Question 1 (1 mark)

A group of business people have decided not to stay at a hotel because it does not have broadband connection or meals available 24 hours. Which influence on operations is the hotel *not* satisfying?

A. Technology
B. Globalisation
C. Quality expectations
D. Corporate responsibility

Question 2 (1 mark)

In an attempt to improve its competitiveness, a business has decided to locate its operations in a South-East Asian country. Which of the following is the most likely influence on this decision?

A. Cost-based
B. Government
C. Legal regulations
D. Environmental sustainability

Question 3 (3 marks)

What is cost-based competition? Explain why a cost leadership approach to business operations is used by businesses.

Question 4 (2 marks)

Explain why quality and expectations cannot be separated.

More exam questions are available in your learnON title.

3.4 Government policies and legal regulation

SYLLABUS LINK In this subtopic you will learn about how government policies and legal regulation influence operations, how to identify their breadth and how each can affect operations management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

3.4.1 Government policies

All businesses operate in a political–legal environment. Political decisions affect the business rules and regulations, which, in turn, directly affect the management of various key business functions. Government policies change from time to time, most notably due to a change in government or a change in social expectations, and are, therefore, a notable source of change and a significant influence on business operations.

There is a breadth of government policies that affect operations management. These range from taxation rates, required materials handling practices, work health and safety (WHS) standards, industry training requirements, policies relating to public health, environment, trade and industry, as well as employment relations. Since policies can inform law-making, and lead to business opportunities, operations managers need to be fully aware of decisions and what they mean for business management.

FIGURE 3.4 Government policies such as the instant asset write-off policy help businesses claim tax deductions on the purchase of assets such as technological equipment.



3.4.2 Legal regulation

The range of laws with which a business must comply are collectively termed ‘compliance’. The regulations that shape business practices and procedures must be followed at the risk of penalty, hence the term compliance. The expenses associated with meeting the requirements of legal regulations are termed **compliance costs**.

compliance costs the expenses associated with meeting the requirements of legal regulations, i.e. abiding by all laws

Laws make clear the standards of society, and businesses are expected to comply with the standards of behaviour imposed by the legal regulations.

All aspects of business must abide by the laws of business. Operations has particular laws that influence how practices and processes are conducted. Of significance to the operations functions in a business is the role of labour in the transformation process. The relevant laws relating to the management of labour (human resources) include:

- work health and safety (WHS) — in the use of machinery and in interacting with the business environment. Safe and healthy working conditions require that employees be given appropriate safety training, use of protective equipment, and work with machines that abide by noise, pollution and safety standards
- training and development — in the use and application of technology and in the appropriate methods required to work effectively
- fair work and anti-discrimination laws — requiring that employees be treated with dignity and respect.

FIGURE 3.5 Providing a healthy and safe workplace environment is an important part of an operations manager's responsibilities.



Other areas of regulation with respect to the operations process relate to the environment and public health. These laws address issues such as:

- environmental protection — minimising pollution, eliminating and safely disposing of any toxic residues
- rules related to public health — including any fair trading rules which influence product safety standards and fitness for purpose of products. The range of laws affecting business operations is shown in figure 3.6.

BizFACT

National work health and safety laws took effect in January 2012 with the passing of the *Work Health and Safety (WHS) Act 2011 (Cwlth).*

FIGURE 3.6 The range of laws affecting and shaping business operations in Australia

Racial Discrimination Act 1975 (Cwlth)
Sex Discrimination Act 1984 (Cwlth)
Workers Compensation Act 1987 (NSW)
Disability Discrimination Act 1992 (Cwlth)
Age Discrimination Act 2004 (Cwlth)
Anti-Discrimination Act 1977 (NSW)
Work Health and Safety (WHS) Act 2011 (Cwlth)
Environment Protection and Biodiversity Conservation Act (1999) (Cwlth)
Superannuation Guarantee Act 1992 (Cwlth)
Taxation Act 1953 (Cwlth)
Corporations Act 2001 (Cwlth)
Fair Work Act 2009 (Cwlth)

Resources

Weblink Fair Work Ombudsman

KEY IDEAS

- Government policy is a source of change for business.
- Government policies affect operations decisions.
- Policies from government are reflected in laws and regulations.
- Managers who do not comply with government regulations in respect to human resources, the environment and public health risk fines and, in some cases, jail.
- While some government policies restrict business practices, other policies encourage business and provide opportunities.

3.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

3.4 Quick quiz | **3.4 Exercise** | **3.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 5, 6	4, 7, 9, 10	8

3.4 Exercise

Revision

1. **What** are government policies?
2. **Define** the term 'legislation' and provide two examples.
3. **Clarify** how legislation affects the operations function of a business.
4. **Why** are the laws with which a business must comply collectively termed 'compliance'?
5. **Recall** the relationship between legal regulation and compliance costs.
6. **Identify** three laws that relate to business operations.

Extension

7. **Determine** how the law can affect and shape operations management. Refer to information from the **Fair Work Ombudsman** website to assist in answering this question.
8. Select one of the laws listed in figure 3.6. **Evaluate** how the selected law would affect the cost and complexity of business.
9. **Examine** the notion of legal compliance. Explain how compliance adds cost to business but also regulates the conduct of business, with reference to examples.
10. **Investigate** the government policy on small business instant asset write-offs. Answer the following questions.
    a. What does the government classify as a 'small business' for the purpose of the policy?
    b. **How** does the instant assets write-off work?
    c. **Why** do business people like the instant asset write-off policy?
    d. Should the government expand the instant asset write-off policy to include large businesses? **Justify** your response.

3.4 Exam questions

Question 1 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q13

An overseas company has made a pirate version of Sascha's computer game.
What type of global influence on Sascha's business is this?

A. Cultural
B. Financial
C. Legal
D. Political

Question 2 (1 mark)

Source: HSC 2009 Business Studies Exam, Section I, Q4

Which of the following is a legal responsibility that supermarkets have towards their customers?

A. To deliver quality service
B. To advertise weekly specials
C. To offer a money-back guarantee
D. To provide a safe shopping environment

Question 3 (1 mark)

Source: HSC 2005 Business Studies Exam, Section I, Q6

Which of the following is an example of an external influence that may cause a company to change its strategic direction?

A. The outsourcing of marketing
B. The decision to establish web-based ordering
C. The introduction of new management processes
D. The legislation of new environmental health policies

Question 4 (1 mark)

An interest rate increase has led to increased loan repayment costs. As a result, the operations team must find ways to cut their costs to help pay the increase in the loan repayment. Which influence is most responsible for this interest rate increase?

A. Cost-based
B. Government
C. Legal regulations
D. Environmental sustainability

Question 5 (1 mark)

A business has decided to change its packaging so that it can be recycled. This will add cost to operations. This change is a result of which influence on operations?

A. Cost-based
B. Government
C. Legal regulations
D. Environmental sustainability

More exam questions are available in your learnON title.

3.5 Environmental sustainability and corporate social responsibility

SYLLABUS LINK In this subtopic you will learn about how environmental sustainability and corporate social responsibility influence operations, including the difference between legal compliance and ethical responsibility, and environmental sustainability and social responsibility. You will learn to explain why CSR is a key concern in operations management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

3.5.1 Environmental sustainability

environmental sustainability (ecological sustainability) to shape business operations around practices that consume resources today without compromising access to those resources for future generations

precautionary principle requires that, where environmental impacts are uncertain, a business undertakes actions that are most likely to cause the least environmental impact

Awareness of the negative effects of business operations on the environment has led to a call for businesses to adopt environmentally sustainable practices. **Environmental sustainability** (ecological sustainability) means that business operations should be shaped around practices that consume resources today without compromising access to those resources for future generations. There are three main aspects to environmental sustainability (ecological sustainability). These are the sustainable use of renewable resources, a reduction in the use of non-renewable assets and the application of the **precautionary principle**. Applying the precautionary principle requires that, where environmental impacts are uncertain, a business undertakes actions that are most likely to cause the least environmental impact.

BizFACT

The Cadbury factory on the banks of the Derwent River north of Hobart, Tasmania produces high-quality, satisfying and delicious chocolate while emitting relatively low amounts of greenhouse gases.

Greenhouse emissions are generated through the burning of fossil fuels for energy, including electricity and transport; however, 90 per cent of Tasmania's electricity comes from hydroelectrical and wind power. Cadbury's main culprit in emissions is transport — its products need to be moved within Australia, as well as to locations as far away as Ghana.

Cadbury has also appointed an eco-efficiency team that has introduced sustainable strategies such as:

- steam capture (reused in later stages) that reduces coal and water use
- gas collection from the factory's wastewater treatment plant for recycling, which has reduced the amount of gas used substantially and carbon dioxide emissions by 200 tonnes
- biodegradable plastic packaging (made of corn starch)
- sourcing only Fair Trade-certified cocoa beans for its manufacturing process.

carbon footprint the amount of carbon produced and entering the environment from operations processes

The operations function is significantly affected by the rise in climate change scientific understanding and the need to integrate a long-term sustainable view of resource management into business planning and practice. This can be seen in the move by businesses to reduce and minimise waste; recycling water, glass, paper and metals, and reducing their **carbon footprint**. The carbon footprint refers to the amount of carbon produced and that enters the environment from operations processes.

3.5.2 Corporate social responsibility

A growing area, affecting all key areas of business, is **corporate social responsibility (CSR)**. Corporate social responsibility refers to open and accountable business actions based on respect for people, community and the broader environment. It involves businesses doing more than just complying with the laws and regulations. Formerly called the **'triple bottom line'**, CSR places value on financial returns as well as social responsibility and environmental sustainability. This means that the driver of corporate decision making is not simply profitability, but rather something that more broadly reflects a range of community concerns and social expectations. Triple bottom line refers to the financial profitability, the social impact and the environmental impact of a business.

corporate social responsibility (CSR) open and accountable business actions based on respect for people, community/society and the broader environment. It involves businesses doing more than just complying with the laws and regulations.

triple bottom line refers to the financial profitability, social impact and the environmental impact of a business

For many public businesses, the annual report will contain significant reference to corporate social responsibility or sustainability. Some companies, such as Kathmandu (see the chapter 1 case study), produce a separate sustainability report that provides a comprehensive account of their commitment to the areas of ethical decision making that goes beyond legal requirements.

SNAPSHOT

Case study: The triple bottom line at Bulla

The Royal Agricultural Society (RAS) named Bulla Dairy Foods the best food producer for 2014. Bulla is an Australian dairy manufacturer that produces a range of chilled and frozen dairy products including cream, cottage cheese, yogurt, dairy desserts, ice-cream and frozen yogurt. The company employs more than 450 people across its manufacturing sites, head office and distribution centre in Victoria.

Bulla was presented with the RAS President's Medal after its 35 per cent Thick Cup Cream won the champion cream award at the 2014 Sydney Royal Cheese and Dairy Produce Show and gained the medal nomination.



Robert Ryan, President of the RAS, congratulated Bulla on being named the 'best of the best' in Australian food and agricultural production. 'The President's Medal recognises Australian producers that create the highest quality products by sustainable means, which is an outstanding achievement,' he said.

Judges for the best food producer award inspected the company's processing sites and found that the company was very aware about its triple bottom line. Bulla has worked hard to reduce waste, landfill volumes and greenhouse gas emissions through its 'cogeneration' project. A wellbeing program offers staff health support, including fitness programs and nutrition boosts, such as a free weekly winter soup.

Corporate social responsibility and operations management

Corporate social responsibility (CSR) is a key concern in operations management for contemporary businesses. Operations management involves processes of transformation that draw from a range of inputs to make final products. The principles of CSR require a business to manage the effects of its activities on society/community and the environment, such that negative impacts are minimised. This requires that a business understand where and how its inputs are sourced so that it only draws from suppliers that adhere to appropriate standards. It also requires that a business shapes its processes in such a way as to minimise environmental damage and waste. The operations process can further integrate principles of CSR through managers ensuring recruitment practices draw from a diverse range of employees and are inclusive of people from all backgrounds.

3.5.3 The difference between legal compliance and ethical responsibility

The government creates laws that affect business operations with an expectation that they will be followed. Penalties for a breach of business laws act as a deterrent and can assist management in understanding their obligations. Some businesses, however, go much further than simply adhering to the minimum requirements set out under the law; they demonstrate a commitment to ethical responsibility. The difference then between legal compliance and ethical responsibility is that legal requirements require businesses to follow the letter of the law — the prescribed standards of behaviour. Ethical responsibility sees businesses meeting all of their legal obligations and taking it further by following the intention and 'spirit' of the law.

In demonstrating ethical responsibility, management is indicating that it values something more than just earning maximum profits because it is demonstrating its commitment to act beyond expectations for the benefit of society, both now and in the future.

Compliance typically falls into a number of areas for business. These areas include, but are not limited to:

- labour law compliance, such as minimum wages, award wages, working hours, breaks, pay for various forms of leave, other on-costs associated with labour, workers compensation and WHS laws
- environmental and public health compliance, such as regulations stopping dumping, pollution (air, land and water), requiring certain standards of operating and of waste disposal
- business licensing rules, such as those requiring particular levels of training or certification and those placing conditions on operations (such as restricted working hours, zoning restrictions, and content and disclosure restrictions)
- taxation, such as levies and duties as well as taxes imposed on profits. Superannuation can be considered a form of taxation that is invested for retirement purposes. Taxation can be applied in such a way as to encourage particular practices or penalise particular activities
- trade practices and fair market dealings, which address issues of market power, misleading and unfair conduct, price collusion, monopoly behaviour, market concentration (competition) and product safety
- migration and rules around the use of offshore skilled labour, which aim to ensure minimum standards are applied to labour brought in from other nations.
- intellectual property, which addresses issues related to moral rights such as copyright, patents, trademarks, designs and other original ideas and artistic works.
- financial and accounting regulations and corporations law, which aim to standardise methods and rules around financial records and reports, as well as ensuring that company directors follow particular rules as fiduciaries. A **fiduciary** is a person in a position of financial trust with respect to others' money
- corporate governance, which refers to the rules, policies and decisions that have been established to direct the operations and performance of the business. For business this places a responsibility on the board of directors to ensure corporate integrity in decision making that affects its stakeholders.
- human rights, such as rules restricting discrimination on the grounds of disability, culture, sexual preference, gender, age or any other distinguishing feature.

fiduciary a person in a position of financial trust with respect to others' money

When businesses conduct their operations, so that they are abiding by all relevant and applicable local, state and federal laws, they may incur significant costs. Given that the main goal of business is to generate maximum profit, it is easy to see why many businesses opt for the lowest level of compliance permissible. This would mean that the business is incurring the lowest necessary compliance costs possible.

Outsourcing, compliance and business behaviour

One way that businesses aim to reduce compliance costs is by structuring their business operations so that different aspects are conducted by outside parties. Theprocess known as **outsourcing** involves the use of outside specialists to undertake one or more key business functions. Outsourcing may be undertaken onshore or offshore. **Onshore outsourcing** involves the use of domestic businesses as the outsourcing provider, whereas **offshore outsourcing** involves taking the activities to a provider in another country.

Offshore outsourcing takes advantage of regulatory differences between nations. This means that the compliance requirements are different between the nations chosen and allow the business to take advantage of significant cost savings. Lower taxation rates, lower standards of labour, weaker environmental and intellectual property regulations all enable businesses to reduce their compliance costs. Of course, the use of offshore outsourcing raises ethical issues concerning business behaviour. For example, should a business operate in nations with loose WHS laws when the costs saved can place employee welfare at risk? Or should a business outsource its operations to a third party that takes responsibility for compliance? Using a third party can be a screen behind which many businesses hide. In this way, breaches of compliance in other nations can be passed on to the contractor operating in its local market without any legal responsibility for the business outsourcing its production. This has caused businesses in Australia to be more responsible when choosing contractors to produce their goods or deliver their services overseas. Some have been exposed for being complicit in not 'calling out' those contractors not abiding by local labour laws.

3.5.4 Ethical responsibility

Ethical responsibility involves businesses going beyond the law and taking into account broader social, community and environmental concerns. However, when laws and regulations differ between nations, it can be hard to know how to be ethical in given business situations. Under such circumstances, businesses may guide their decision making after consulting with special interest groups or following guidelines set down by international bodies. In manufacturing operations there can be significant international differences in standards for labour in terms of wages, health and safety, and training. A business may choose to follow international labour standards articulated by the International Labour Organization (ILO).

The ILO holds annual conventions called the International Labour Conference and raises matters of importance to workplaces and the rights of employees. Such matters include:

- working women and maternity protection
- the provision of safe working conditions.

The workplace issues that are raised are put into a report. If two-thirds of the nations in the ILO agree to the report's recommendations, it becomes an International Labour Standard. Nations are expected to pass laws consistent with the International Labour Standards.

Ethical practice also has a role in businesses that provide a service. The Commonwealth Bank has recently been criticised for its management of its customer relationships. The focus of the criticism was how the business's insurance division operated. ABC's *Four Corners* and the then-Fairfax Media (now Nine Entertainment Co.) reported that there were several cases where claims assessors rejected payouts to terminally ill clients. In addition, it was alleged that the insurance division CommInsure removed medical files and ensured that doctors changed their diagnoses in order to refuse claims. The bank's then-Chief

outsourcing (or contracting out business functions) involves the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

onshore outsourcing involves the use of domestic businesses as the outsourcing provider

offshore outsourcing involves taking the activities to a provider in another country

Executive Officer was forced to apologise and insisted that ethics remains a core business value and that such circumstances would not be repeated.

FIGURE 3.7 In some developing countries, sweatshop conditions exist, in which women and children work long hours in extreme heat for very low wages and with virtually no safety precautions. There is increasing pressure to ensure such employees are not exploited by unscrupulous businesses by using contractors that abide by higher minimum legal expectations.



FIGURE 3.8 The role of the International Labour Organization (ILO)

About the ILO

The only tripartite U.N. agency, since 1919 the ILO brings together governments, employers and workers representatives of 187 member States, to set labour standards, develop policies and devise programmes promoting decent work for all women and men.

Mission and impact of the ILO

Promoting jobs, Protecting people

The International Labour Organization (ILO) is devoted to promoting social justice and internationally recognized human and labour rights, pursuing its founding mission that social justice is essential to universal and lasting peace.

As the only tripartite U.N. agency, the ILO brings together governments, employers and workers representatives of 187 member states to set labour standards, develop policies and devise programmes promoting decent work for all women and men.

Today, the *ILO's Decent Work Agenda* helps advance the economic and working conditions that give all workers, employers and governments a stake in lasting peace, prosperity and progress.

Source: www.ilo.org/global/about-the-ilo/lang–en/index.htm; www.ilo.org/global/about-the-ilo/mission-and-objectives/lang–en/

3.5.5 Environmental sustainability and social responsibility

Economic development must be accomplished sustainably — that is, using methods of production that conserve the Earth's resources for future generations. Economic growth should not occur at the expense of polluting and degrading the air, water and forests that are essential to supporting life on this planet. There needs to be a balance between economic concerns and environmental concerns — in other words, environmental sustainability.

Consequently, businesses are being asked to take increasing responsibility for the protection of the environment. The Earth is a fragile system, and needs high levels of support and informed intervention so that it may sustain itself. The social conscience of responsible business owners (and, increasingly, government legislation) has led them to adopt policies of conservation, recycling and restoration. The principle of ecological sustainability requires business's management to evaluate the full environmental effects of their operations.

Additionally, the growing consumer expectation that products should be 'clean, green and safe' is changing management practices in a number of Australian businesses. By producing new and better products in an ecologically sustainable manner, the business focus and stakeholder expectations are more closely aligned.

In response to concerns about climate change, the community increasingly expects businesses to:

- adopt greenhouse abatement (reduction) measures
- encourage the development of long-term sustainable strategies.

Corporate social responsibility (CSR) refers to a business's management of the social, environmental, political and human consequences of its actions. A socially responsible business tries to achieve two goals simultaneously: (1) expanding the business and (2) providing for the greater good of society. It recognises that business activities have an impact on society and as such management needs to give careful consideration to their actions.

Social responsibility is good business — customers eventually identify those businesses that are acting responsibly and those that are not. Customers can react and stop buying a business's product if they learn that it is exploiting employees, accepting bribes or polluting the environment directly or indirectly through contracting out its production of goods or in providing services. At the same time, customers will reward socially responsible businesses by purchasing more of their products. Obviously, socially responsible business behaviour costs money in the short term but in the long run often turns out to be in the company's best interests. Socially responsible businesses may even convert a weakness into a strength, enabling marketing opportunities that communicate the business's virtues as one driven by social and environmental goals.

BizFACT

Business owners or managers can consider establishing an environmental management system (EMS) that allows them to have a more systematic and methodical approach to the firm's environmental impact. This can also include having the EMS accedited to the ISO 14001 standard. This is an international standard that recognises an effective environmental system and gives confidence to stakeholders that the business is measuring and improving it.

SNAPSHOT

Case study: Corporate social responsibility at Mars — a key concern in operations management



Mars is a private, family-owned company that produces some of the world's leading confectionery, food and pet care products, and has growing beverage and health and nutrition businesses. Headquartered in McLean, Virginia (in the United States), Mars Incorporated operates in more than 80 countries and employs more than 100 000 associates (employees) worldwide. Mars launched in Australia in 1954. The company's global sales are approximately US$35 billion annually. Founded in 1911, the company manufactures and markets a variety of products under many of the world's most recognisable trademarks, including M&M'S®, SNICKERS®, MASTERFOODS®, DOLMIO®, PEDIGREE®, UNCLE BEN'S®, ROYAL CANIN®, WHISKAS®, EXTRA®, ECLIPSE® and STARBURST®. Mars uses high quality ingredients and employs the highest standards of quality control.

Mars has developed five principles to lead and guide the company: Quality, Responsibility, Mutuality, Efficiency and Freedom. They express the company's vision of not only what Mars is, but also where and what Mars wants to be. The Five Principles are put into practice every day by Mars associates (staff) all over the world and have developed into a practical, effective and unique way of doing business that collectively and individually sets Mars apart. For example, Mars' environmental policy is anchored in the Five Principles.

Mars has policies concerning its use of genetically modified ingredients, the health and nutrition of its foods, research involving animals and positive relations with its associates. Mars has a 2020 target — that 100 per cent of its cocoa will come from certified sources; in 2016 it was on track to certify 50 per cent of the cocoa it buys.

Mars also has policies aimed at making it a more socially responsible company. The company has a long-term goal to reduce its total environmental impact in line with what science indicates is necessary. It also aims to improve the lives of 1 million people in their value chain, while advancing science innovation and marketing in ways that help people.

Mars is a reputable employer. Teamwork is seen as very important at the company — units work with each other to achieve broad corporate objectives. The business has been recognised as a great place to work numerous times. For example, in 2019, Mars ranked in the top 25 World's Best Workplaces list for the eighth consecutive year. Vice President Eric Minvielle says, 'Being awarded a spot on the World's Best Workplaces list eight years in a row is an honour that reflects our Associates' feedback and our commitment today to building a better world for people, pets and our planet tomorrow. Thank you to each of our 125 000+ Associates who make Mars a wonderful workplace every day.'

Mars' employees shared all of the reasons why they are #ProudlyMars on the Great Place To Work survey, which covers more than 8000 organisations and represents the voices of 3.4 million employees at companies worldwide.

Source: Adapted from: Mars Ranks in Top 25 World's Best Workplaces for Eighth Consecutive Year, https://www.mars.com/news-and-stories/articles/the-worlds-best-workplaces.

on Resources

Video eLessons Environmental sustainability and Ferguson Plarre Bakehouses (eles-1089)
Di Bella Coffee and CSR (eles-2284)

Weblinks Kathmandu Sustainability Report 2020
Reebok and Adidas sustainability
Levi Strauss
International Labour Organization

KEY IDEAS

- Business operations are required to adopt environmentally sustainable practices to reduce their carbon footprint.
- Corporate social responsibility (CSR) is an important influence on business and it integrates financial, social and environmental goals.
- Legal compliance refers to businesses abiding by the word of the law, whereas ethical responsibility encompasses a much broader integration of social, community and environmental concerns.
- Compliance costs are those associated with the cost of meeting the needs imposed by regulations. Compliance applies to a wide range of business activities.
- Ethical business enterprises recognise that variation in laws can undermine social and ethical responsibility. Therefore, they may seek independent sources, such as the ILO and lobby groups, to create ways of applying ethical standards across the operations function.
- Environmental sustainability and social responsibility are features of an ethical approach to operations management.
- Economic development must be accomplished sustainably.
- Environmental sustainability refers to the economic, social and environmental performance of a business.
- Social responsibility refers to a business's management of the social, environmental, political and human consequences of its actions.

3.5 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

3.5 Quick quiz on | **3.5 Exercise** | **3.5 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 5, 8, 9, 11, 13, 16, 17, 18, 19, 21	2, 6, 7, 10, 12, 14, 15	20, 22, 23, 24

3.5 Exercise

Revision

1. **State** the three main aspects of environmental sustainability.
2. **How** does environmental sustainability affect the operations function of business?
3. **What** is 'corporate social responsibility'?
4. **What** are the main themes that support corporate social responsibility?

Read the case study 'The triple bottom line at Bulla' and answer questions 5 and 6.

5. **Outline** the business characteristics of Bulla Dairy Foods.
6. **Propose** the reasons for the company's recognition as 'the best of the best' in Australian food and agriculture.
7. **Distinguish** between legal compliance and ethical responsibility.
8. **Recall** the term applied to the expenses associated with abiding by all laws.
9. **Identify** four areas in which a business would have to demonstrate compliance.
10. **How** can businesses reduce compliance costs?
11. **State** why a business's management may decide to offshore its outsourcing of production.
12. **Distinguish** between compliance and ethical responsibility in business.
13. a. **Recall** what the acronym ILO represents.
    b. **Identify** two matters relating to workplaces and the rights of employees that the ILO might be concerned with ensuring that businesses comply with.
14. **Explain** why businesses should be concerned with environmental sustainability.

15. **Account** for the growing consumer expectation for 'clean, green and safe' products.
16. **Identify** two goals a socially responsible business tries to achieve.
17. Since an investment in CSR can be expensive, **outline** the impact on revenue and profitability if a business such as Bulla invests in CSR.

Read the 'Corporate social responsibility at Mars — a key concern in operations management' case study and answer questions 18 to 22.

18. **Outline** the development of Mars including its expansion into Australia.
19. **List** some of its trademarks.
20. **Analyse** the role of the five principles that guide the company — Quality, Responsibility, Mutuality, Efficiency and Freedom.
21. **Outline** the policies that demonstrate its socially responsible approach.
22. Reebok (a subsidiary of Adidas) and Levi Strauss both devote significant resources to corporate social responsibility. Recently the companies have taken steps to ensure the compliance of their suppliers in regard to the workplace and environmentally sustainable practices. Undertake further research to **assess** Reebok's and Levi Strauss's commitment to their suppliers' social and environmental obligations. **Create** either an oral or written report and present it to the rest of the class.

Extension

23. With reference to a large business (such as Myer, BHP Billiton, Mobil or Virgin Airlines), **identify** compliance costs specific to the business. You may need to research the corporate website of the relevant business. **Determine** how the costs you identified affect the business and its operations.
24. Investigate the role of the International Labour Organization (ILO). Use your research to **critically analyse** how ILO standards can affect the operations function of a business.

3.5 Exam questions

Question 1 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q16

Which of the following actions is an example of corporate social responsibility?

A. Sponsoring a sporting event
B. Opening a manufacturing plant
C. Introducing a community health program
D. Paying compensation for a work-related injury

Question 2 (3 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q24b

A fruit shop has experienced strong growth in its sales of fresh organic fruit since it started to sell online.

Explain why corporate social responsibility should be a key concern in operations management for this business.

Question 3 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q13

The term *compliance costs* refers to expenses associated with meeting

A. competitor prices.
B. legal requirements.
C. consumer demands.
D. supplier constraints.

Question 4 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q17

Which of the following is an example of legal compliance for a sports store?

A. Paying taxes on time
B. Offsetting carbon emissions
C. Induction of new employees
D. Paying dividends to shareholders

Question 5 (4 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q21a

How might a business benefit when an operations manager acts in an ethically and socially responsible manner? Support your answer with relevant examples.

More exam questions are available in your learnON title.

3.6 Review

3.6.1 Summary

Globalisation and technology

- Globalisation is a reference to the removal of barriers of trade between nations.
- Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and machinery), labour, intellectual capital and ideas, financial resources and technology.
- Globalisation has significantly affected the operations function of large and global businesses.
- Globalisation affects consumers who seek global brands and this, in turn, shapes the operations function.
- Technology plays a very important role in operations — from administration, through to all operations processes.

Quality expectations and cost-based competition

- Management of quality expectations in both the manufacture of products and the delivery of services is a goal of operations management.
- Quality expectations differ between goods and services.
- Whether quality expectations relate to goods or services, in both cases they lead to consumers having a perception about the standard of products, and accordingly consumers will be prepared to pay a higher price for higher quality.
- Another factor affecting and shaping operations is cost-based competition. Here a business can apply cost leadership to reduce both fixed and variable costs.

Government policies and legal regulation

- Government policy is a source of change for business.
- Government policies affect operations decisions.
- Policies from government are reflected in laws and regulations.
- Managers who do not comply with government regulations in respect to human resources, the environment and public health risk fines and, in some cases, jail.
- While some government policies restrict business practices, other policies encourage business and provide opportunities.

Environmental sustainability and corporate social responsibility

- Business operations are required to adopt environmentally sustainable practices to reduce their carbon footprint.
- Corporate social responsibility (CSR) is an important influence on business and it integrates financial, social and environmental goals.
- Legal compliance refers to businesses abiding by the word of the law, whereas ethical responsibility encompasses a much broader integration of social, community and environmental concerns.
- Compliance costs are those associated with the cost of meeting the needs imposed by regulations. Compliance applies to a wide range of business activities.
- Ethical business enterprises recognise that variation in laws can undermine social and ethical responsibility. Therefore, they may seek independent sources, such as the ILO and lobby groups, to create ways of applying ethical standards across the operations function.
- Environmental sustainability and social responsibility are features of an ethical approach to operations management.
- Economic development must be accomplished sustainably.
- Environmental sustainability refers to the economic, social and environmental performance of a business.
- Social responsibility refers to a business's management of the social, environmental, political and human consequences of its actions.

3.6.2 Key terms

carbon footprint the amount of carbon produced and entering the environment from operations processes
compliance costs the expenses associated with meeting the requirements of legal regulations, i.e. abiding by all laws
corporate social responsibility (CSR) open and accountable business actions based on respect for people, community/society and the broader environment. It involves businesses doing more than just complying with the laws and regulations.
cost-based competition derived from determining breakeven point (the level at which the firm's total revenue is exactly equal to its total costs) and applying strategies to create cost advantages over competitors
environmental sustainability (ecological sustainability) to shape business operations around practices that consume resources today without compromising access to those resources for future generations
fiduciary a person in a position of financial trust with respect to others' money
fixed costs costs that are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business.
globalisation refers to the removal of barriers of trade between nations. Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and/or machinery), labour, intellectual capital and ideas, financial resources and technology.
offshore outsourcing involves taking the activities to a provider in another country
onshore outsourcing involves the use of domestic businesses as the outsourcing provider
outsourcing (or contracting out business functions) involves the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.
precautionary principle requires that, where environmental impacts are uncertain, a business undertakes actions that are most likely to cause the least environmental impact
quality a specific reference to how well designed, well made and functional goods are, and the degree of competence with which services are organised and delivered
technology the design, construction and/or application of innovative devices, methods and machinery in operations processes
triple bottom line refers to the financial profitability, social impact and the environmental impact of a business
variable costs costs that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy.

on Resources

Digital documents	Key terms glossary (doc-35658) Chapter crossword (doc-36211)
Interactivity	Chapter crossword (int-7151)
Exam question booklet	Chapter 3 Exam question booklet (eqb-0025)

3.6 Activities

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Exercise 1: Multiple choice questions

1. Globalisation can:
   - **A.** be a threat to businesses focusing on cost leadership approaches.
   - **B.** increase integration between national economies.
   - **C.** lead to higher transfers of intellectual capital and ideas.
   - **D.** All of the above
2. Globalisation is a significant influence on operations management because of which of the following?
   - **A.** Consumers value global brands.
   - **B.** Consumers seek customised products.
   - **C.** Organisations can reduce economies of scale.
   - **D.** Operations are structured around local facilities.
3. Economies of scale advantages are achieved by global businesses through which of the following?
   - **A.** Choosing the best locations for production of components
   - **B.** Focusing on quality management
   - **C.** Using reliable supply chains
   - **D.** All of the above
4. Which technology is used in the operations process?
   - **A.** Gantt charts
   - **B.** Computer-aided design (CAD)
   - **C.** Critical path analysis
   - **D.** Spreadsheets
5. Quality of goods and services is measured by which of the following?
   - **A.** The features that satisfy stated or implied needs
   - **B.** How well designed and made goods are
   - **C.** How competently services are organised and delivered
   - **D.** All of the above
6. Cost advantages are derived from which of the following?
   - **A.** Determining breakeven point
   - **B.** Reducing prices to create advantages over competitors
   - **C.** Mass customisation for differentiated or standardised products
   - **D.** Using reliable suppliers
7. Work health and safety policies include which of the following?
   - **A.** Carbon pricing
   - **B.** Noise and pollution standards
   - **C.** Anti-discrimination
   - **D.** B and C
8. Which of the following are the key aspects of environmental sustainability?
   - **A.** Assessing carbon footprint and minimising waste
   - **B.** Reducing non-renewable resources and increasing renewable resources
   - **C.** Recycling paper and metals, and business planning to increase carbon footprint
   - **D.** Planning for carbon pricing and safe disposal of toxic waste
9. What is meant by corporate social responsibility?
   - **A.** Meeting the relevant compliance requirements
   - **B.** Using open and accountable business practices based on respect for people
   - **C.** Focusing on social responsibility and environmental sustainability as well as financial returns
   - **D.** Prioritising environmental sustainability as a business goal

10. Which of the following correctly describes onshore outsourcing?
    - **A.** It takes advantage of regulatory differences between nations.
    - **B.** It takes advantage of regulatory differences within nations.
    - **C.** It involves domestic specialists supplying a key business function.
    - **D.** It primarily involves restructuring business functions to reduce environmental costs.

Exercise 2: Exam practice questions

Question 1 (6 marks)

a. **What** is globalisation? **(2 marks)**

b. **Explain** how globalisation influences a business's operations. **(4 marks)**

Question 2 (4 marks)

Examine the breadth of government policies that affect operations management.

Question 3 (8 marks)

a. **Identify** TWO influences on operations management. **(2 marks)**

b. **Analyse** how these influences affect operations management. **(6 marks)**

Question 4 (5 marks)

Why is corporate social responsibility a key concern in operations management?

Question 5 (4 marks)

Distinguish between legal compliance and ethical responsibility in operations management.

Question 6 (6 marks)

Critically **analyse** the role of environmental sustainability and social responsibility in operations management.

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Teacher-led video Chapter 3 Exam practice solutions (tlvd-1867)

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4 Operations processes

4.1 Overview

LEARNING SEQUENCE

4.1 Overview
4.2 Inputs
4.3 Transformation processes: volume, variety, variation in demand and visibility
4.4 Transformation processes: sequencing and scheduling
4.5 Transformation processes: technology, task design and process layout
4.6 Transformation processes: monitoring, control and improvement
4.7 Outputs
4.8 Review

4.1.1 Introduction

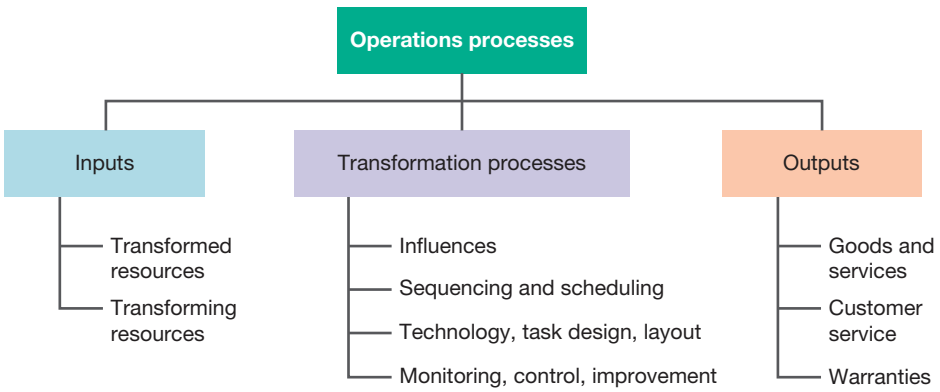
A visit to a factory to investigate the manufacturing operations process was a rite of passage for many young Australian students in years gone by. A school excursion to a local business gave these students an opportunity to gain insight into the chocolate or ice-cream that they might enjoy after school. Invariably the factory would have men and women taking up a position on the production line for hours with little variation in their role.

Fast-forward to today and getting such first-hand access to the operations process is becoming increasingly difficult for various reasons; however the basic process remains the same. The input–transformation–output process continues to provide us with a variety of goods that assist with meeting society's needs and wants.

Operations processes are those processes involved directly with transformation. The processes may be broadly classified according to their role in transformation: inputs into transformation processes, the actual processes of transformation, or outputs of the transformation process.

Inputs, transformation processes and outputs are all important and each has its own features and presents challenges for operations managers (see figure 4.1).

FIGURE 4.1 An overview of operations processes



on Resources

Digital document Key terms glossary (doc-35660)
Exam question booklet Chapter 4 Exam question booklet (eqb-0026)

4.2 Inputs

SYLLABUS LINK In this subtopic you will learn about the role of inputs in operations processes. This will include transformed resources (materials, information, customers) and transforming resources (human resources, facilities).

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Inputs are the resources used in the transformation process. Some inputs are owned by the business, while others are provided by suppliers.

4.2.1 Common direct inputs

Although different types of inputs are used in the transformation process, generally there are four that are commonly used by businesses:

- labour
- energy
- raw materials
- machinery and technology (capital equipment).

BizFACT

In Business Studies, capital refers to the money provided by the owners to finance a business's activities. In Economics, capital refers to machinery and technology used to produce goods and services.

Labour

Labour is the human effort, both mental and physical, that is a necessary input into the operations process. Employment in the field of business operations includes the areas of sourcing and supply chain, technical support and maintenance for machinery, inventory management and control, quality processes, production, logistics and distribution. Clearly labour is closely aligned to all aspects of business operations.

Energy

Energy, in the form of electricity or fuels, which can be converted into heat, movement, light, sound or other forms of energy, is an essential input into transformation. Energy is required to bring inputs to the business, to transform them and to distribute them to consumer markets. Indeed, value adding is directly proportional to the amount of energy expended. For example, the manufacture of a high value-added product such as a motor vehicle requires large amounts of energy.

inputs the resources used in the transformation (production) process

BizFACT

Raw materials are also sometimes called 'direct materials'. However, raw materials are not always 'raw'. This is because some businesses use already processed materials as their inputs. Consider, for example, a clothing designer. The cloth used is already processed — the raw materials such as cotton have already been transformed into cloth. In this case, the 'raw' materials are partially processed (or 'intermediate') materials.

Raw materials

Raw materials are essential inputs into operations processes. The basic components of manufactured goods are wood, unprocessed agricultural products, natural resources in the form of minerals and fossil fuels, and water. Raw materials are sourced through the supply chain and businesses will determine the volume of raw materials required against the level of demand for finished or partly finished goods.

FIGURE 4.2 Most manufacturing plants consume large quantities of energy and rely on a reliable source of power. In recent years, businesses have begun to implement energy-saving measures to reduce their costs and greenhouse emissions, and more significantly to pursue alternative energy sources.



Machinery and technology

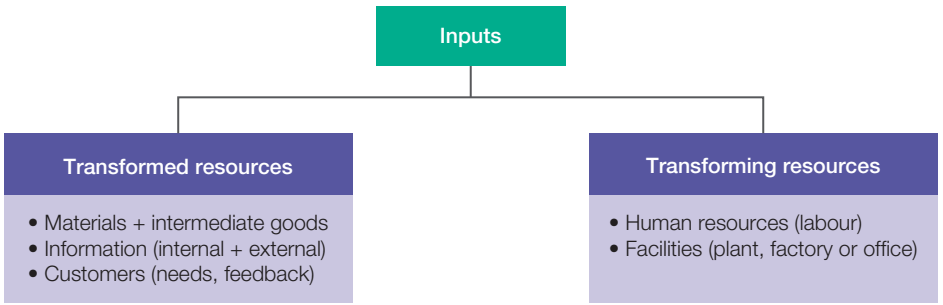
Machinery and technology are necessary to enable the transformation processes that are characteristic of operations. Machinery is used to process raw materials, as well as to design and make products. Machinery integrated with technology can perform complex tasks quickly. Indeed, over time, there has been a concern about what is called **capital–labour substitution**. Capital–labour substitution means that machinery and technology replace workers. In reality, when machinery and technology are used in business, some labour may be lost in a process known as structural change but there is then a period of retraining that takes place as people acquire new skills relevant to use with new technologies.

capital–labour substitution
machinery and technology displace people by doing the work they do

4.2.2 Input classification

Inputs may be divided into those that are transformed resources and those that are transforming resources. Figure 4.3 indicates how inputs can be classified.

FIGURE 4.3 Inputs can be classified as transformed resources (resources that are changed or converted in the operations process) and transforming resources (resources that carry out the transformation process).



4.2.3 Transformed resources

Transformed resources are those inputs that are converted in the operations process. Transformed resources are those that give the operations process its purpose or goal. The transformed resources are:

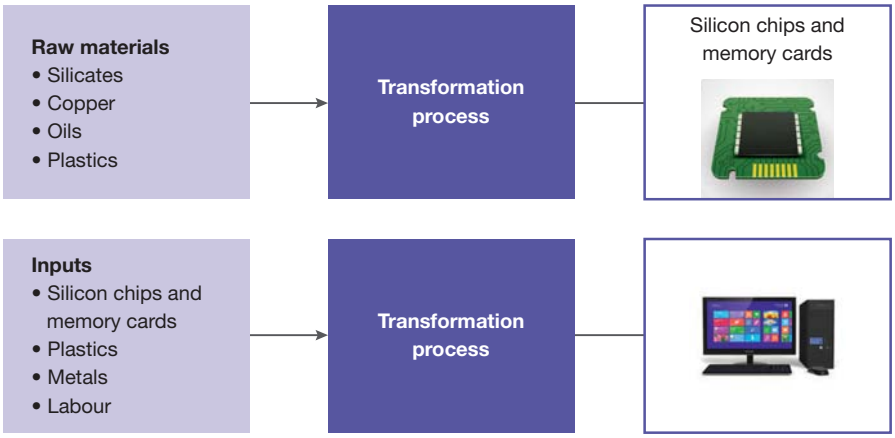
- materials
- information
- customers.

Materials

Materials are the basic elements used in the production process and consist of two types: raw materials and intermediate goods. Materials are most commonly raw materials such as oil, wood or steel. **Raw materials** are the essential substances in their unprocessed (natural) state and usually come from mines, forests, oceans or recycled waste. However, materials can also be **intermediate goods**, which are goods that are unfinished and usually undergo further processing.

The distinction here is that there is a range of materials that are *already* transformed but still become inputs into operations processes. Consider the following: computers need integrated circuits and digital memory capacity. Complex microchips are required to store memory and to enable computers to operate. The chips are outputs from businesses that transform various raw materials (plastics, silicon, copper) into microchips. These chips are both final outputs as well as inputs for further processing. A computer manufacturer will take these transformed resources and use them as essential inputs (components) in computers. This is shown in figure 4.4.

FIGURE 4.4 Transformed resources can become inputs used in the production of other goods and services.



Similarly, in a service-based business, items such as stationery, computers and furniture are outputs of other businesses that become essential inputs to the delivery of services.

Information

Information is the knowledge gained from research, investigation and instruction, which results in increased understanding. The value of information lies mainly in its ability to influence behaviour or decision making.

Information can be a very important input into the operations process. Information can come from two sources: internal and external. Information acts as a transformed resource when it is used to inform how inputs are used, where they are drawn from, which suppliers and supplies are available, and so on. That is, the information is in a form that just needs to be understood or analysed, rather than compiled.

transformed resources those inputs that are changed or converted in the operations process

materials the basic elements used in the production process, consisting of two types: raw materials and intermediate goods

raw materials the essential substances in their unprocessed state

intermediate goods goods manufactured and used in further manufacturing or processing

information the knowledge gained from research, investigation and instruction, which results in an increase in understanding

External information

This is information that comes from market reports, statistics from industry observers and bodies, official government statistics from the Australian Bureau of Statistics (ABS), media reports, academic papers and commentary, management journals and comparative studies. External information is an excellent and generally independent source for operations managers to use. It is very useful to integrate relevant information into operations processes. For example, information on the use of distribution centres will act as an input for inventory management. Similarly, information on new technology can influence which machinery is purchased and how it is applied to the operations function.

Internal information

Internal information comes from within the business and is gathered from internal sources such as financial reports, quality reports, and internal **key performance indicators (KPIs)** such as lead times, inventory turnover rates and production data. A further source of important internal information arises from customer feedback. This can come through an analysis of warranty data or from scanning social media threads. Internal information acts as a transformed resource when it informs processes and creates process improvements.

Customers

Customers are generally thought of as being relevant to outputs, not inputs. Therefore, it seems odd to think of them as a 'transformed resource'. Customers become transformed resources when their choices shape inputs. In the modern day, consumer orientation is essential to business. A consumer orientation takes the preferences and interests of consumers as the starting point to production processes. In this way, the customer acts as an input and their desires and preferences act as a transformed resource.

To better understand the desires and preferences of customers, businesses can implement a **customer relationship management (CRM)** program. CRM refers to the systems that businesses use to maintain customer contact. CRM software can be used to improve customer service, increase competitiveness and identify changes in consumer tastes.

The information can be retrieved and entered by employees from different functions within the business, such as marketing and finance, as well as operations. This approach improves services (many of which are now provided directly to customers) and reduces production costs, and customer feedback makes the operations process more directly responsive to customer preferences.

4.2.4 Transforming resources

The other collection of inputs to any operations processes are **transforming resources** which are those inputs that carry out the transformation process. They enable the change and value adding to occur. The two transforming resources are:

- human resources
- facilities.

Human resources

Employees are said to be the single most important input into business. Capable workers can bring higher productivity and efficiency to business operations. The effectiveness with which human resources carry out their work duties and responsibilities can determine the success with which transformation and value adding occurs. This is because it is employees who coordinate resources such as machinery, raw materials and finance to produce goods and services. In this sense, employees are the most crucial of all inputs.

For example, if the main business objective of management in a manufacturing company is to be the 'most efficient and reliable supplier', its human resource policies and practices should be aimed at attracting, retaining and motivating staff to ensure

key performance indicators (KPIs) specific criteria used to measure the efficiency and effectiveness of the business's performance

customer relationship management (CRM) the systems that businesses use to maintain customer contact

transforming resources those inputs that carry out the transformation process

they are able to meet their customers' supply needs and also their own management's expectations. Being efficient means having a reliable workforce that can do the job when required. To turn this objective into a reality, a strategy of improving employee skills through training and development may be used. In addition, setting performance objectives for individual staff members to improve their efficiency will help the business achieve its objectives. Other strategies that will assist the achievement of business objectives include adhering to work health and safety standards and ensuring staff motivation remains high.

Well-designed human resource management policies and practices can improve the performance of the operations processes. Well-considered job design, targeted and appropriate training, flexible work practices and open communication are all factors that assist in maximising operational efficiency, business performance and the capacity of the business to achieve the objectives.

Facilities

Once a business has determined the type of operations process to use, it will need to undertake a complex set of design-planning decisions involving its production facilities. **Facilities** refer to the plant (factory or office) and machinery used in the operations processes. Major decisions for management will include the design layout, the number of facilities to be used,and their location and capacity. In particular, business management needs to decide:

- whether the required facilities should be located in one or two large sites or divided among numerous smaller sites
- what impact zoning and other restrictions will have upon the facilities' size and location
- special conditions, such as energy and water requirements
- the most efficient plant design
- the optimum plant and process layout — the arrangement of machinery, equipment and people within the facility.

Plant and machinery selection by management can make a very significant difference to a business and its capacity to transform. Clearly the facilities can determine the nature of the operations environment. Modern facilities that integrate modern technology, have adequate lighting, are well designed and promote a positive workplace culture for staff, will be highly conducive to productive operations.

facilities the plant (factory or office) and machinery used in the operations processes

KEY IDEAS

- The operations process refers to the input–transformation–output process.
- Inputs are the resources used in the transformation process and can be classified as either transformed resources or transforming resources.
- Transformed resources are those inputs that are changed or converted in the operations process and include:
  - materials — the basic elements used in the production process, consisting of raw materials and intermediate goods
  - information — the knowledge gained from research, investigation and instruction, which results in an increase in understanding
  - customers — their desires and preferences are the starting point to production processes.
- Transforming resources are those inputs that carry out the transformation process and include:
  - human resources — they coordinate and combine other resources to produce goods and services
  - facilities — the plant (office or factory) and machinery used in the operations process.

4.2 Activities

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4.2 Quick quiz on	4.2 Exercise	4.2 Exam questions

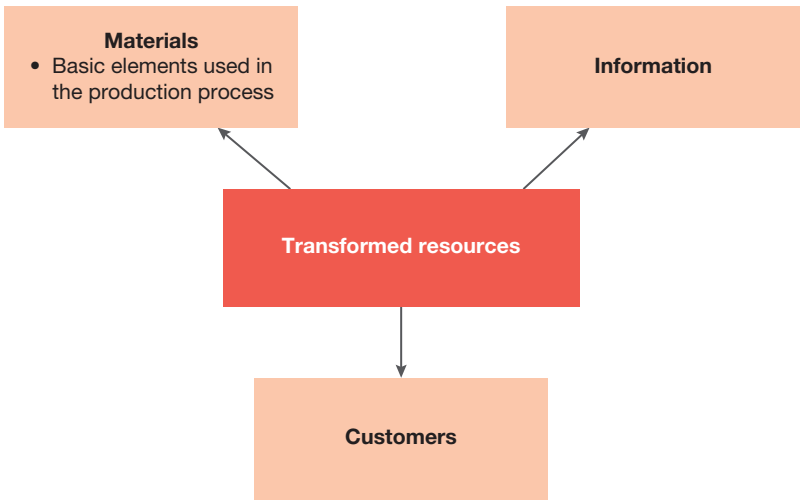
Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 10, 11, 12, 13	5, 6, 7, 8, 9, 14	15, 16, 17

4.2 Exercise

Revision

1. **What** are the three elements of an operations process?
2. **Outline** the 'input–transformation–output' process.
3. **Identify** the main inputs, transformation and outputs in an operations process such as that used in a chocolate factory.
4. **Outline** the four common direct inputs used in operations.
5. **Construct** a diagram that illustrates the transformation process for making a take - away cup of coffee. Begin your diagram with the barista taking the customer's order and finish with the delivery of the coffee order.
6. **Distinguish** between transformed resources and transforming resources.
7. Use the concept map example provided to construct **how** transformed resources can be used within the operations process.



8. **How** can materials be either raw or intermediate in nature?
9. **Why** are customers classified as a 'transformed resource'?
10. **What** makes information a transformed resource, and how does it shape the operations processes?
11. **Explain** the relationship between human resources and the effectiveness of operations.
12. **Outline** the term 'facilities'.
13. **Recount** four decisions a business needs to consider in relation to facilities.
14. **Explore** how facilities can shape operations processes by researching two different types of production facilities.

Extension

15. Use examples to **demonstrate** the three elements of the operations process (inputs–transformation–outputs) and how each is performed in business.
16. Ron's Roofing and Gutters is a large manufacturing business that employs 485 employees. **Identify** four ways Ron's management could use employees to maximise output.
17. What is 'capital–labour substitution'? Prepare either a written or an oral report **discussing** the advantages and disadvantages of this system of production.

4.2 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q16

Which of the following lists three examples of transformed resources?

A. Customers, information, materials
B. Facilities, information, technology
C. Customers, human resources, materials
D. Facilities, human resources, technology

Question 2 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q5

Which of the following includes two examples of transforming resources?

A. Facilities and customers
B. Materials and customers
C. Facilities and human resources
D. Materials and human resources

Question 3 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q14

Which of the following includes two examples of transforming resources?

A. Materials and energy
B. Information and customers
C. Task design and technology
D. Human resources and facilities

Question 4 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q4

Which of the following is the correct sequence for an operations process?

A. Facilities — controls — waste
B. Materials — design — product
C. Information — services — improvement
D. Human resources — planning — customers

Question 5 (1 mark)

Jayden's Carpet Laying is a business located in the western part of Sydney. Describe TWO inputs to the operations of this business.

More exam questions are available in your learnON title.

4.3 Transformation processes: volume, variety, variation in demand and visibility

SYLLABUS LINK In this subtopic you will learn about transformation as an operation process, including the influence of volume, variety, variation in demand and visibility (customer contact).

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The main factor shaping operations processes is **transformation**, which involves the conversion of inputs (resources) into outputs (goods or services). Samsung, for example, takes plastic, metal, glass and electronic parts and transforms each through design, manufacturing and assembly into numerous electronic products.

transformation the conversion of inputs (resources) into outputs (goods and services)

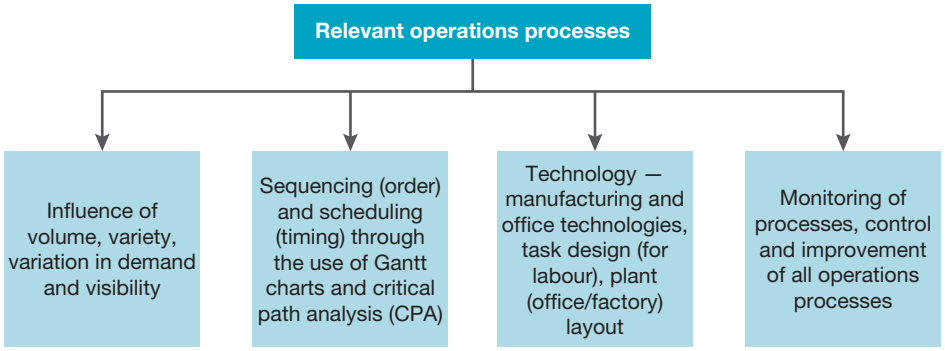
The term 'transformation' implies physical changes, but it also includes the conversion of resources into services. For example, your school takes its main inputs — students, the syllabus, staff and buildings — and produces educated, employable students. Similarly, legal firms can utilise resources, experience and legal knowledge to transform a legal conflict into a resolution. A service organisation transforms inputs into intangible products (services that cannot be touched but that have effects that can be felt). The operations process for a manufacturer tends to be highly automated. Manufacturers use machinery, robots and computers to transform inputs into outputs. Service providers rely heavily on an interaction with the customer and their processes tend to be more labour-intensive; that is, staff are integral to the process. A service provider applies time, skill and experience in assisting consumers to improve their quality of life through consuming its product.

FIGURE 4.5 The term 'transformation' implies physical changes, but today it includes process and service improvements. Training and accreditation boost skills and deliver services of greater overall quality and effectiveness.



There are several aspects to operations processes that are directly involved with the process of transformation and they are identified in figure 4.6.

FIGURE 4.6 An overview of the operations processes relevant to transformation



4.3.1 The influence of volume, variety, variation in demand and visibility (customer contact)

A key aspect to operational processes relates to the question 'how much'? That is, in the process of transformation, decisions will need to be made about the following questions.

- How much to make — what volume of input to draw in and to process?
- How much variation — what range of outputs should be made in the process of transformation?
- How much variation in demand will there be — and how quickly can the operations processes respond to changes in demand?
- How much customer contact should there be and what, if any, role should it have on transformation processes?

The influence of volume

Volume refers to how much of a product is made. Volume flexibility refers to how quickly the transformation process can adjust to increases or decreases in demand. This responsiveness to the required changes in volume is essential to effectively managing **lead times**. Lead time is the time it takes for an order to be fulfilled from the moment it is made. If businesses cannot quickly adjust to changes in market demand, they can over - produce, which may lead to waste and increased inventory costs. Alternatively, if back orders cannot be quickly fulfilled, it can lead to lost sales. A customer may, for example, go to a competing business. See the following case study for an example.

volume refers to how much of a product is made

lead time the time it takes for an order to be filled from the moment it is made

SNAPSHOT

Case study: Strong retail competitors in Australia — Zara, Uniqlo and H&M



The introduction of a number of so-called fast fashion brands (clothing that moves quickly from fashion shows to stores to meet new trends) has changed the traditional approach to volume, variety and variation in demand experienced by more established businesses. Zara, Uniqlo and H&M are among the most highly sought-after clothing brands, leading to a loss of sales revenue for established brands such as Marcs, Willow and David Lawrence.

Zara's, Uniqlo's and H&M's management of the four Vs characteristic of operations processes — volume, variety, variation in demand and visibility — is interconnected. Each of the brands is able to respond to increases in volume quickly — indicating highly responsive supply chain management. Variety, a key to success in fast fashion, is led by Zara and its high number of new designs entering the market each couple of months. Variety, as evidenced by a wide product range, can only be effectively managed when there is a very good understanding of consumer preferences.

Variation in demand, which used to be seasonal in respect to fashion, has now become characterised by shorter cycles, initiated by smart business practices. Thus, the release of new designs to market six times per year, instead of two to four times per year, helps maintain market demand, although there has been some supply chain disruptions due to the global pandemic.

Each of the businesses, Zara, H&M and Uniqlo, are placed in a highly visible location that has ready access to passing trade. Physically located in large shopping centres, each is also strongly represented on social media platforms.

Accordingly, through effective operations processes and management of the four Vs, each of these businesses is reshaping the clothing retail sector in Australia.

The influence of variety

The mix of products made, or services delivered, through the transformations process is sometimes called mix flexibility. **Mix flexibility** is known by consumers as product range or variety of choice. The influence of variety on transformation processes is: the greater the variety, the more the operations process needs to allow for this variation.

mix flexibility the mix of products made, or services delivered, through the information process

SNAPSHOT

Case study: Whitegoods — mix flexibility

In Australia, Electrolux make the Electrolux, AEG-Electrolux, Simpson, Chef, Dishlex, Kelvinator and Westinghouse brands. These brands are attached to a range of household electrical whitegoods such as refrigerators, washing machines, ovens, dishwashers and dryers. Similarly, Whirlpool, a competitor, also makes this range of household appliances. If you were to investigate the electronic components within the range of devices, you would find that there are many similarities: they heat and cool, have rotating parts and timers. So, despite the apparent diversity in these products, many of them are electronically very similar. In this way, the company behind the brands can sell a variety of products made with largely similar production processes.



The influence of variation in demand

A variation in demand can impact significantly on transformation resources. An increase in demand will require inputs from suppliers, human resources, energy use and use of machinery and technology. However, increased demand may prove problematic if:

- suppliers cannot deliver quickly enough
- labour is not agile, skilled or available in adequate numbers
- machinery cannot adjust to increased requirements, either because it is not capable or proves unreliable
- increased energy and power requirements are not accessible.

A decrease in demand will also require operational flexibility as staff numbers may be reduced, production slowed or contract suppliers may insist that orders be filled despite being unnecessary.

Anticipating demand

All businesses will try to forecast demand so that adjustments can be made. Annually, some variations are predictable: Christmas, for example, can be a time when increased toy sales might be expected. Seasonal factors also cause predictable variations in demand; for example, more air conditioners will be sold in late spring just before summer than are sold in mid-winter.

The influence of visibility (customer contact)

Customer contact or 'feedback' can directly affect transformation processes. This is because customers and their preferences can shape production decisions. Customer contact may be direct or indirect. Direct contact takes the form of customer feedback through surveys, interviews, warranty claims, letters, social media posts and verbal contact. Indirect feedback occurs through a review of sales data that gives an indication of customer preferences or market share, through an observation of people's decision-making processes or consumer reviews. Because businesses seek to maximise sales, customer contact is essential and ultimately shapes the transformation processes.

Resources

Weblink Domino's Pizza

KEY IDEAS

- Transformation is the conversion of inputs (resources) into outputs (goods or services).
- Transformation differs between manufacturing businesses and service businesses.
- A manufacturer transforms inputs into tangible products.
- A service organisation transforms inputs into intangible products.
- Transformation processes are influenced by:
  - volume — how much of a product is made
  - variety — the range of products made
  - variation in demand — the amount of a product desired by consumers
  - visibility — the nature and amount of customer contact (feedback).

4.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

4.3 Quick quiz | **4.3 Exercise** | **4.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 6, 7	8, 9, 10, 12	11, 13

4.3 Exercise

Revision

1. **What** does 'transformation' mean?
2. **Recall** the most appropriate words from below to complete the following sentences.

outputs	manufacturing	intangible	conversion
interaction	services	labour	customer
physical	automated	tangible	

a. The main concept of operations processes is transformation, which is the _____ of inputs (resources) into _____ (goods or services).
b. The term 'transformation' implies _____ changes, but today it also includes the conversion of resources into _____.
c. It is important to understand that the transformation process differs between _____ businesses and service businesses.
d. A manufacturer transforms inputs into _____ products (goods which can be touched).
e. A service organisation transforms inputs into _____ products (services which cannot be touched).
f. The operations process of a manufacturer tends to be highly _____ or mechanised.
g. Service providers rely heavily on _____ with the _____ and their processes tend to be more _____-intensive.

Read the 'Strong retail competitors in Australia — Zara, Uniqlo and H&M' case study and answer questions 3 to 6.

3. **Identify** the 4 Vs.
4. **List** three businesses that are increasing sales volumes in Australia.
5. **How** does variation in demand affect the volume of product brought to the market by Zara, Uniqlo and H&M?
6. **What** is the importance of visibility to clothing retailers?
7. 'The transformation process is influenced by the four Vs: volume, variety, variation and visibility.' **Summarise** the influence of the four Vs by completing the following table. The first one is provided to assist you.

Influencing factor	Summary
Volume	• Refers to how much of a product is made.
Variety	
Variation (in demand)	
Visibility	

8. Project into the role of the operations manager for an ice-cream factory.
   a. **Explain** why it would be important to understand the concept of 'lead time'.
   b. **How** would you respond to the supply chain issues caused by seasonal changes in consumer demand? Share your answer with the rest of the class.
   c. Detail the importance of variety to the market and factory.

Read the 'Whitegoods — mix flexibility' case study and answer questions 9 and 10.

9. **Identify** the brands manufactured by Electrolux.
10. **Account** for why, while there may be wide range of products, the processes remain narrow.

Extension

11. Research a manufacturing business such as ASICS or Samsung, and investigate the transformation processes used in the business. **Synthesise** your findings and present them to the class.
12. **Investigate** what happens when a customer makes an online order for a delivered at Domino's Pizza. Use this information to create a schematic diagram to **explain** the concept of 'lead time' with respect to the business.
13. **Analyse** the effect of customer contact on transformation processes. In your answer, examine the benefits of a business undertaking direct feedback methods such as surveys, wikis and blogs. You may refer to the Myer website or the David Jones website as a source of inspiration.

4.3 Exam questions

Question 1 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q7

In winter, the number of beach lifeguards employed by a local council is reduced. What has influenced the transformation process in this situation?

A. Variation in demand
B. Variation in visibility
C. Variety
D. Volume

Question 2 (1 mark)

A restaurant decides to organise its premises so that customers can see work done in the kitchen. Which influence on the transformation process best describes this decision?

A. Variety
B. Variation in demand
C. Volume
D. Visibility

Question 3 (1 mark)

During the winter months a lawn mowing business cuts back on its casual staff. Which influence on the transformation process has caused this action?

A. Variety
B. Variation in demand
C. Volume
D. Visibility

Question 4 (6 marks)

Sandeep wishes to open an organic food café. He wishes to know the best way to operate his café. Analyse TWO influences on the transformation process Sandeep should consider.

Question 5 (1 mark)

A call centre requires its operators to make 20 calls an hour with the aim of making one sale for every 10 calls. Which of the following has influenced this transformation process?

A. Variety
B. Variation in demand
C. Volume
D. Visibility

More exam questions are available in your learnON title.

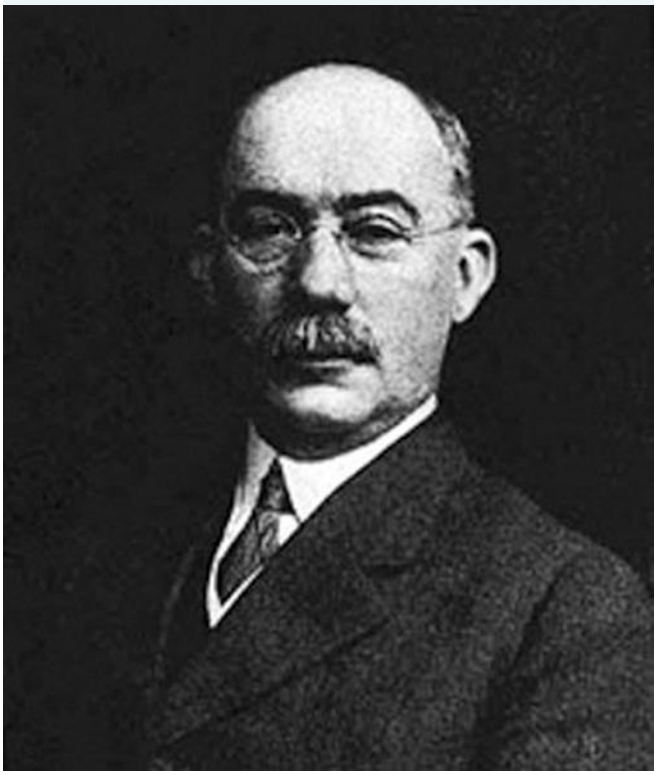
4.4 Transformation processes: sequencing and scheduling

SYLLABUS LINK In this subtopic you will learn about how sequencing and scheduling can influence the operations process, using tools such as Gantt charts and critical path analysis.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Sequencing and **scheduling** are two aspects that assist with structuring and ordering the transformation processes. Sequencing refers to the order in which activities in the operations process occur. Scheduling refers to the length of time activities take within the operations process. An understanding of both sequencing and scheduling is necessary for operations managers. When planning operations processes that involve activities central to transformation, various scheduling tools will be used. The two scheduling tools referred to here are Gantt charts and critical path analysis (CPA).

FIGURE 4.7 Henry Laurence Gantt (1861–1919) was an engineer and management consultant who developed Gantt charts — a visual tool to show scheduled and actual progress and considered as a routine project management tool



4.4.1 Gantt charts

The **Gantt chart** was created by Henry Gantt in 1917. The Gantt chart outlines the activities that need to be performed, the order in which they should occur and how long each activity is expected to take. Gantt charts are used for any process that has several steps and involves a number of different activities that need to be performed. A typical Gantt chart is shown in figure 4.8. This chart shows the steps a clothing store would take when setting up and preparing for an opening.

Gantt charts can be used for scheduling simple routine tasks such as completing a homework assignment and for larger, more complex projects such as building a dam. They can be used to schedule the work activities of one employee or a team.

There are two main advantages of using Gantt charts. Firstly, it forces a manager to plan the steps needed to complete a task and to specify the time required for each task. Secondly, they make it easy to monitor actual progress against planned activities.

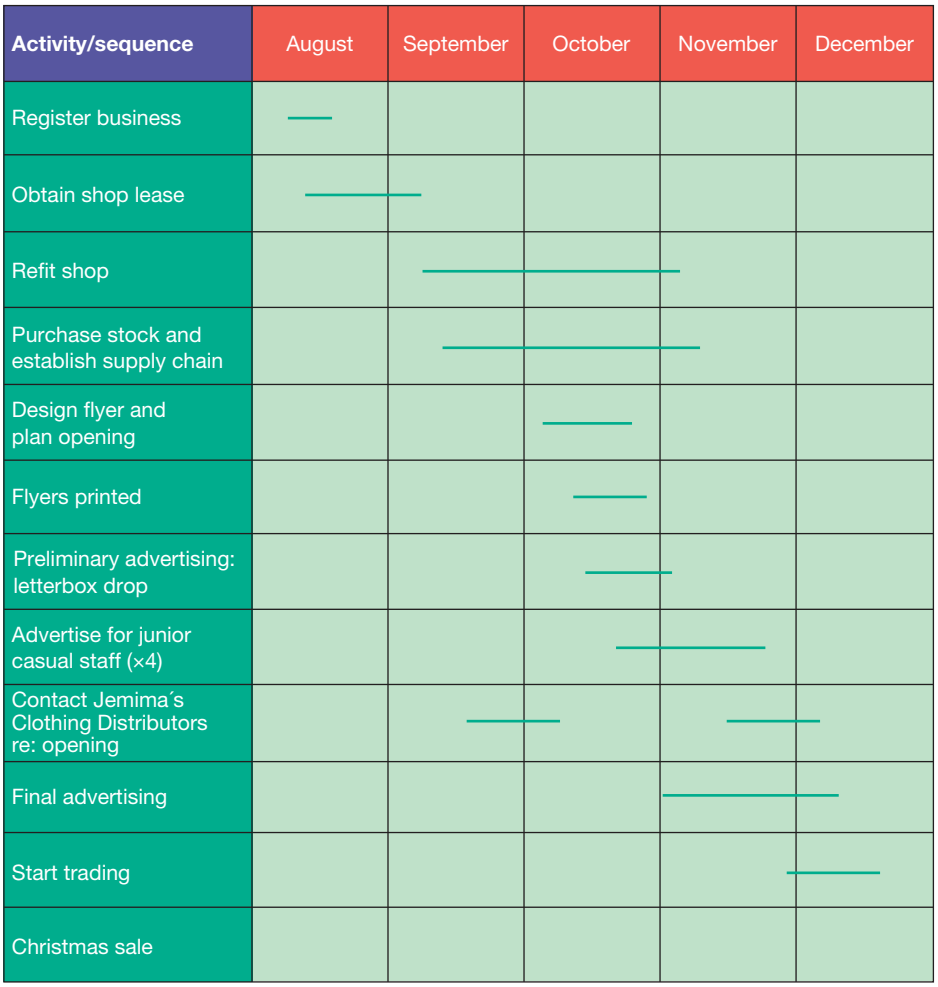
sequencing the order in which activities in the operations process occur

scheduling the length of time activities take within the operations process

Gantt chart a type of bar chart that shows both the scheduled and completed work over a period of time. It is often used in planning and tracking a project.

FIGURE 4.8 Gantt chart showing sequence and scheduling (timing)

Gantt chart for opening of Stitched Up P/L 2018



4.4.2 Critical path analysis (CPA)

Critical path analysis (CPA) is a scheduling method or technique that shows what tasks need to be done, how long each takes and the order necessary to complete those tasks. A typical CPA is shown in figure 4.9.

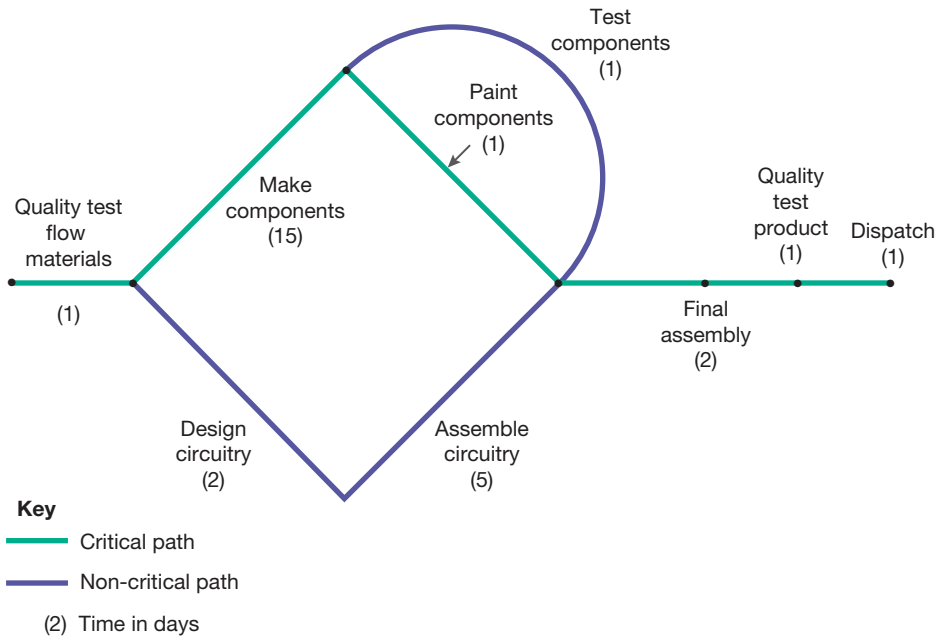
The critical path is the *shortest* length of time it takes to complete *all tasks* necessary to complete the process or project. Since all necessary tasks must be completed, in practical terms, the critical path will be the longest path through a process. You will see that some tasks can be performed simultaneously (for example, painting and testing components, or making the circuitry and assembling the components). Because *each activity* on the schedule must be completed to make the final product, the critical path ensures all tasks have been completed. In this case, the critical path is:

critical path analysis (CPA) a scheduling method or technique that shows what tasks need to be done, how long they take and what order is necessary to complete those tasks

(1) day	+ (15) days	+ (1) day	+ (2) days	+ (1) day	+ (1) day = 21 days
Quality test materials	Make components	Paint components	Final assembly	Quality test product	Dispatch

Note: the shortest path is *NOT* (1) + (2) + (5) + (2) + (1) + (1) = 12 days, because, though this appears to be the shortest processing path, it does not even allow time for the making of the components, which takes 15 days by itself.

FIGURE 4.9 Critical path analysis (CPA) for the manufacture of an electronic switchgear



The benefit of this type of analysis is that scheduling enables a manager to identify what needs to be done and also allows the timing of tasks to be considered. With this information, a manager will be able to see the order of activities that need to be undertaken. They will also be able to see which tasks can be done simultaneously. In this manner, scheduling gives direction and organisation to operations processes, provides overall coordination and enables a means of control.

on Resources

Weblink Gantt chart

KEY IDEAS

- Sequencing and scheduling are essential activities in operations processes.
- Sequencing refers to the order in which activities in the operations process occur.
- Scheduling refers to the length of time activities take within the operations process.
- Two tools that assist with sequencing and scheduling are:
  - Gantt charts — a type of bar chart that shows both the scheduled and completed work over a period of time
  - critical path analysis — a scheduling method that shows what tasks need to be done, how long they will take and what order is necessary to complete the tasks.

4.4 Activities

learnON

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4.4 Quick quiz	4.4 Exercise	4.4 Exam questions

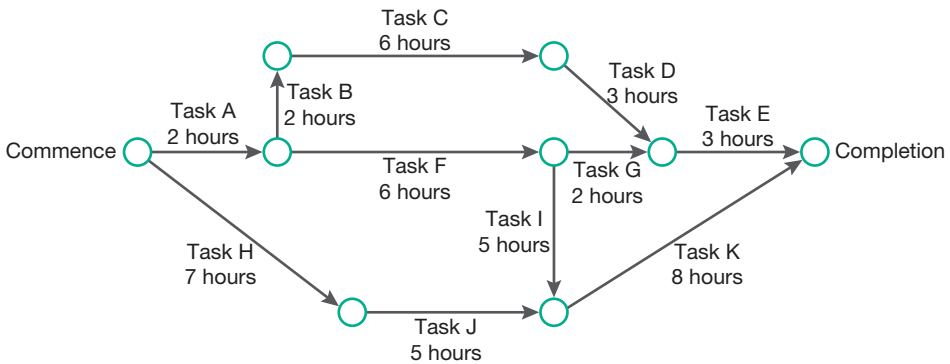
Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 4, 5, 7	1, 2, 6, 8, 9, 10	11, 12

4.4 Exercise

Revision

1. **How** do sequencing and scheduling differ?
2. **Construct** a flowchart showing the sequencing of your day commencing from when you arrived at school until you complete your last period.
3. **Why** would your school timetable be considered as both a sequencing and scheduling document?
4. **What** is the function of a Gantt chart?
5. **Identify** two advantages of using Gantt charts.
6. **Consider** figure 4.8 and use the information to answer questions a to d.
   - **a.** How long will it take to do each of the following activities?
     - i. Purchasing stock and establishing the supply chain
     - ii. Shop refit
     - iii. Contacting Jemima's Clothing Distributors regarding the opening
   - **b.** Identify the least time-consuming activity.
   - **c.** Recommend the activities that can be performed concurrently.
   - **d.** Clarify the benefits to Stitched Up Pty Ltd of constructing a Gantt chart.
7. **What** is a critical path analysis?
8. **How** does a critical path analysis assist in transformation processes?
9. If there are predictable variations in demand based on seasonal factors, **how** will this affect a critical path analysis?
10. **Examine** the following figure showing a planning tool for the creation of an advertisment by Digital Production Enterprises. Use the information to answer questions a to c.
    - **a.** Identify the tool being used by Digital Production Enterprises.
    - **b.** Which task determines when Task K will be performed?
    - **c.** Calculate the shortest time for the completion of the task (show full working).



Extension

11. Using information from the internet, examine the evolution of the Gantt chart. **Assess** the value of a Gantt chart if you had to develop the Year 11 Business Studies assessment schedule for your school.
12. **Determine** the advantages of using a Gantt chart instead of a critical path analysis for a project.

4.4 Exam questions

Question 1 (1 mark)

Source: Adapted from HSC 2019 Business Studies Exam, Section I, Q13

The table below shows a Gantt chart.

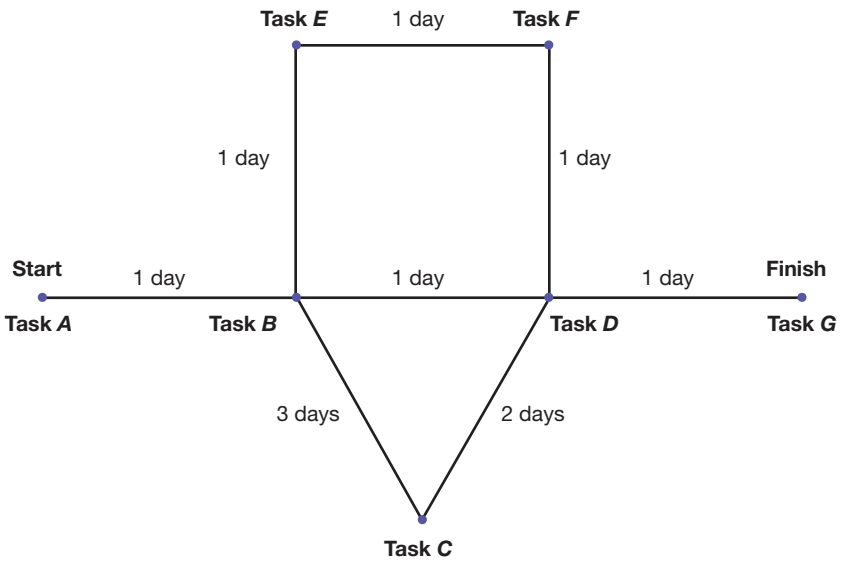
	31/1/20	*29/2/20*	*31/3/20*	*30/4/20*
Receive customer order				
Purchase stock				
Prepare tools for manufacture				
Receive raw materials				
Manufacture item				
Quality improvement				
Deliver finished item				

In which month could this business begin manufacturing the item?

A. Before January
B. January
C. February
D. March

Question 2 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q19



Which tasks need to be completed prior to completing Task *D*?

A. *A, B* only
B. *A, B, C* only
C. *A, B, E, F* only
D. *A, B, C, E, F* only

Question 3 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q9

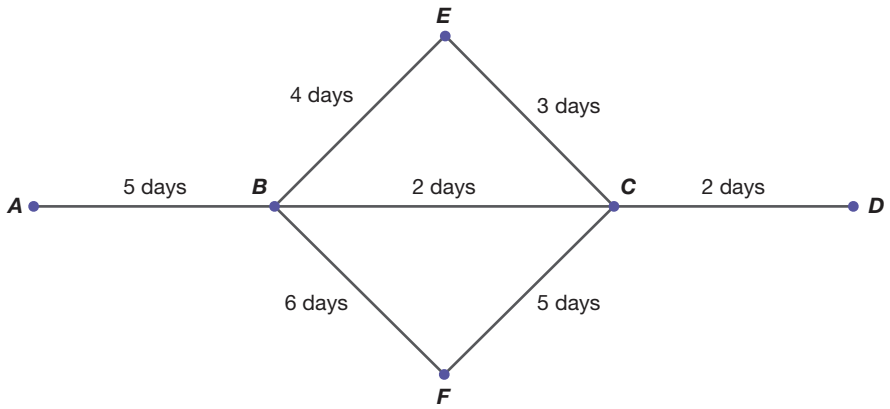
Which operations process uses a Gantt chart?

A. Customisation
B. Input
C. Output
D. Transformation

Question 4 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q15

If activity ***EC*** is delayed and takes 6 days, by how long will the project be delayed?



A. 0 days
B. 3 days
C. 6 days
D. 17 days

Question 5 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q18

A Gantt chart for Sam's Chocolate Shop is shown.

	Jan	*Feb*	*March*	*April*	*May*	*June*
Obtain lease and refit shop						
Purchase stock						
Select and train staff						
Advertising campaign						
Commence trading						

What does this Gantt chart show?

A. Selection and training of staff will begin in May.
B. The shop will be open for business at the end of April.
C. Stock purchases and advertising will be done simultaneously.
D. Some stock will be purchased before the shop is completely refitted.

Question 6 (6 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q21b

Analyse the use of sequencing and scheduling to improve business operations.

More exam questions are available in your learnON title.

4.5 Transformation processes: technology, task design and process layout

SYLLABUS LINK In this subtopic you will learn about how technology, task design and process layout influence the operations process.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

4.5.1 Technology

Generally, technology is the application of science or knowledge that enables people to do new things or perform established tasks in new and better ways. More specifically, business technology involves the use of machinery and systems that enable business to undertake the transformation process more effectively and efficiently. Most technology affects all aspects of business, assisting employees to work more productively.

BizFACT

A pair of scissors is classified as low-technology (lo-tech) compared to computers and robotics, which are highly advanced and developed (hi-tech).

Increasingly, businesses are acquiring up-to-date technology in order to compete effectively. In the manufacturing sector, technology can be used to speed up processes and enable a more complete utilisation of raw materials. This makes the operations processes more cost effective.

In the services sector, smart devices and office and communications technology have enabled whole markets to open up and allow for a small to medium business to trade globally.

The cost of technology is relatively high, so businesses need to decide whether to purchase or lease it. Leasing is more common because it is cheaper (lease payments are tax deductible), which allows money saved to be spent elsewhere. Additional costs that accompany technology include set-up and siting, cabling and the loss of workers who may be displaced due to the new processes it brings. For workers not displaced, there is the cost of training or retraining, continual upgrading of their skills and time lost in adapting to new work techniques.

Office technology

You will be familiar with a range of business technology. The list of business technology items that are commonplace today includes:

- computer or tablet
- keyboard and mouse
- USB and other data storage devices such as external hard drives and Cloud storage
- modem
- mobile telephones/hands-free telephones/wireless enabled phones
- combined printer, photocopier, scanner and facsimile machine
- ability to electronically transfer funds (EFT) and EFTPOS machines.

Developments of the above types of technology have created the opportunity for people to do more work in less time, which means a greater range of tasks can be completed in their working time. These technologies have also enabled office workers to work at a great distance from the office. Increasingly people **telecommute** and work from home. Emails are checked from home, and research and meetings can be

telecommute to 'commute', or travel to work, electronically. This means that home or another location becomes the worksite and work is delivered via email or the internet.

conducted online or through video/webcam chat. In many businesses, the 'virtual office' and 'paperless trading' are becoming a reality and, as office structures change, 'hot desking' is not uncommon.

SNAPSHOT

Case study: Technology — the virtual office



Mehrnoosh has a full-time job for one of the major Australian banks, working in an innovation hub. She acts as an IT specialist and that job allows her the flexibility of working either onsite in central Sydney or offsite. Working remotely means that Mehrnoosh can run her own web design business. She started this business in high school and worked on it throughout her university studies. At university Mehrnoosh won awards for her studies in technology and she was even designated one of the 'young entrepreneurs of the year'.

Mehrnoosh finds that her work for the bank allows her the time to successfully run her own business. That business is growing. The technological advances, including the use of 'cloud'-based solutions, means that Mehrnoosh can access her work from anywhere. It also means that her staff can log into email, the customer database and social media accounts from remote locations. In effect, this means that when she or her staff are travelling, work can continue uninterrupted. Technology assists the process, as a series of notifications are sent to Mehrnoosh's phone. These notifications include payments made, customer inquiries, Facebook and phone inquiries, as well as when staff log into the business accounts and when they log off. The technology also means Mehrnoosh can perform her IT functions for both the bank and her own business regardless of whether she is onsite or offsite. Email and mobile phone access enable her to reach clients with ease and mean she is always available for inquiries arising in her banking job as well as her business.

BizFACT

The shift to working from home due to COVID-19 resulted in a heavy reliance on digital collaboration platforms — Zoom, Skype and Microsoft Teams.

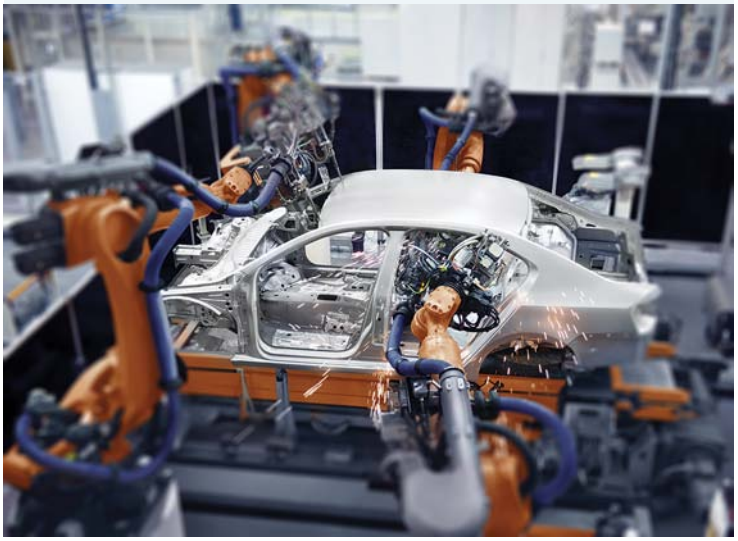
With all knowledge workers operating remotely, these platforms became the only option for communicating and collaborating. Fewer options for in-person meetings and discussions meant that frequent check-ins, formal meetings, coffee catch-ups or Friday drinks, and assorted networking events and conferences were undertaken online.

Brad McKenna, Lena Waizenegger and Wenjie Cai are the authors of an article in *The Conversation*, 'Zoom meetings help marginalised staff feel included — we should keep having them even after offices reopen', published 12 August 2020. In the wake of the pandemic, the authors argued that more flexible work arrangements will be commonplace and managers need to ensure that they create a culture of inclusion and allow staff to make the best of both worlds — use the home office for focused, uninterrupted work (where circumstances permit) and use the corporate office for collaborating, socialising and innovating.

Manufacturing technology

Key manufacturing technology includes robotics, computer-aided design (CAD) and computer-aided manufacturing (CAM).

FIGURE 4.10 Robotics are used in the car manufacturing industry.



Robotics applies to highly specialised forms of technology, capable of complex tasks. Robots are used in engineering and specialised areas of research, as well as on assembly lines where a programmable machine capable of doing several different tasks is required. Robotics can shape the transformation process so that it achieves quality of a consistently high standard, is efficient and minimises waste.

Robotics allows a degree of precision and accuracy generally unattainable by human labour. In addition, robots work without complaint or demands for wage rises in conditions that would be repetitive, boring and often dangerous for employees. Robots and robotics, however, are very high-cost items that are unaffordable for most small and medium-scale manufacturers.

Computer-aided design (CAD) is a computerised design tool that allows businesses to create product possibilities in the form of three-dimensional diagrams from a series of input data which can then be viewed from multiple angles. It is used in a range of business sizes and types. This process assists both the designer and the end user to visualise what will be produced.

Using the design, material usage and the time required for the task can then be calculated. This enables the costing of the project to be quantified, however if the cost is too high or the design is too limited, the input data can be altered to reflect these requirements. CAD programs are linked to printers so that 'hard', or paper, copies can be made and distributed to the client for assessment. Given the speed of CAD software, it is easy to customise a series of options that meets the client's needs. More traditional drafting processes would cost more, take longer and be less accurate as an added bonus! CAD software can be used by designing the sequence of steps that would need to be taken to create the desired good in the shortest possible lead time using the least amount of material.

Computer-aided manufacturing (CAM) is software used to alter the manufacturing process so that it makes greater use of computer technology. CAD software can be linked to CAM software to allow the instantaneous production of designs that are accepted by clients. CAM can also be used more broadly to calculate the quantity of each input resource that would be required in production. CAM software can be used to store historic purchasing records to assist with present decisions.

robotics used in engineering and specialised areas of research, as well as on assembly lines where a programmable machine capable of doing several different tasks is required

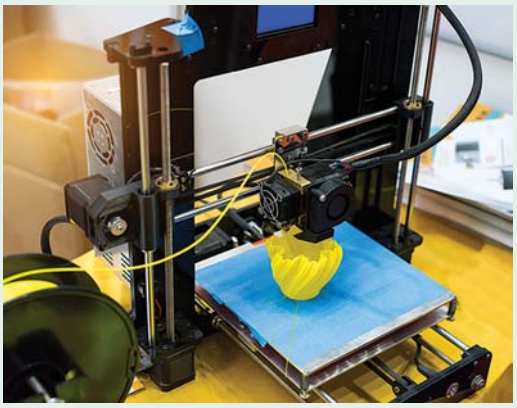
computer-aided design (CAD) a computerised design tool that allows businesses to create product possibilities from a series of input parameters

computer-aided manufacturing (CAM) software that controls manufacturing processes

SNAPSHOT

Case study: Technology in production and services

All car manufacturers use CAD and CAM when translating motor vehicle design into actual products. Architects and engineers also use these technologies. Toyota Motorsport, for example, uses a combination of CAD, CAM and CAE (computer-aided engineering) to create designs and to align production with design.



Service providers such as dentists are also increasingly using CAD. In the case of dental specialists, CAD and CAM can assist to repair damaged teeth, meaning that clients can have their dental problems addressed in one session rather than over repeat visits. This is because the technology can design and create veneers, inlays and dentures very quickly and accurately.

In undertaking the use of technologies such as these, businesses can ensure production standards are consistent, quality is maintained and wastage is minimal. For manufacturers, further benefits include direct communication between marketing (design) and operations (production), reduced lead times and minimal possibility of errors in translation between processes.

3D printing

Recently there has been significant development in 3D printing technologies. Such technologies allow a digital design to make an actual product through the use of polymers and other materials. The field of engineering and product design is being re-shaped through these new technologies that enable innovation and new methods of production to arise.

SNAPSHOT

Case study: Printing surfboard components

3D printers are now being used to print surfboard components such as fins. Due to the nature of the materials used in the manufacture of surfboards, 3D printers can be used to help surfers design and customise their fins. As fin size and shape determine the manoeuvrability of the surfboard, surfers can design their own 3D printed fins to complement their style and the prevailing conditions. In this way the surfer can ensure the fins they attach to their boards are specific to the use of the board and the actual surf on the day — be it riding larger or smaller waves. A further benefit of this new technology is that the fins are replaceable, lowering the cost of maintenance of boards. Clearly, 3D printing (also called additive manufacturing) brings significant possibilities to innovative market sectors.



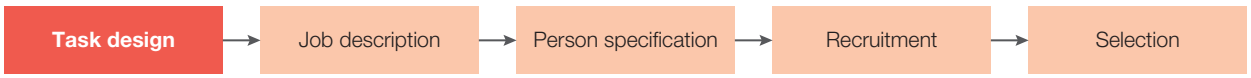
The size of the market for fins is estimated to be worth over $70 million per annum in Australia alone. Thus, the creation of the 3D printed fin options takes advantage of a significant market opportunity.

4.5.2 Task design

Task design involves classifying job activities in ways that make it easier for an employee to successfully perform and complete the task. Task design overlaps the employment relations functions of job analysis, job description and person specification. It starts with an operations manager asking 'What needs to be done?' In the context of the business goals, task design is breaking down the work into a series of jobs where each contributes to the final goal. (The steps involved in the task design process are identified in table 4.1.)

Typically, there is a separation between manufacturing and administrative operations. In task design, it is necessary to group skills and competencies because this assists with staff recruitment. A prospective employee will be screened against these skills and competencies to ensure a match. For example, an intelligent and skilled barista who has no experience in electrical installations is unlikely to be a proficient electrician.

Attracting the right candidate for the task or job is the final part of a process that starts with task design and ends with selection, that is:



A business may formalise the task design process while a job is already being done. Under these circumstances it is usual for the task to be analysed to see whether it could be done more efficiently. This involves a process called job analysis, and requires determining who does what and why in the business. The purpose of job analysis is to improve the business's productivity.

task design involves classifying job activities in ways that make it easy for an employee to successfully perform and complete the task

TABLE 4.1 The steps involved in the task design process

Step	Example
Define what needs to be done in a general statement	• A skilled competent electrician
Analyse the general job into specific duties	• Understand electrical circuits • Ability to work carefully and independently to prescribed electrical standards • Capacity to correctly install electrical devices and adjust capacity as required • Identify where to source correct parts and then use them in the prescribed manner • Follow directions • Communicate clearly with builders and site managers
Determine the degree of difficulty and allocate time	• Difficulty: 8/10 • Supervision: 10 minutes supervision per hour
Match tasks to existing state/federal awards (base)	• $30/hour first year licensed electrician
Articulate the task via job descriptors and a pay scale to allow for a range of experiences in different work settings. (This indicates the types of skills/experience and qualifications needed to successfully complete the task.)	• Licensed electrician $73 000 p.a. Duties: to plan and install a range of electrical items and associated circuitry into a range of building types (residential, commercial and educational).

Skills audit

Sometimes, a business may have staff, however they may not have the requisite skills for the circumstances at that time. As a consequence, managers may wish to conduct a skills audit. The **skills audit** is a formal process used to determine the present level of organisational skills (and any shortfalls) that need to be addressed through recruitment or training and development.

4.5.3 Process layout

There are a number of different considerations when organising the physical layout of a workplace. The method adopted by managers will depend on the type of manufacturing operations or services performed by the business. The way in which machinery and technology is arranged will strongly shape the operations processes. There are alternative ways to lay out machinery on the workplace floor, depending on what is being made and the volume of output required. Workplace layout options include:

- process layout
- product layout
- fixed position layout.

BizFACT

Britax Childcare Pty Ltd manufactures child car restraints, and imports strollers and prams. As an innovative business, it installed new ergonomic workstations designed for the assembly areas to ensure that any part needed by operators was presented directly to them. The working environment, operator efficiency and flow of materials dramatically improved.

Process layout is the arrangement of machines such that the machines and equipment are grouped together by the function (or process) they perform. The process layout is sometimes called functional layout. This type of layout is typical of hospitals, for example, where areas are dedicated to particular types of medical care, such as maternity wards and intensive care units.

Process layout for intermittent production

Process production deals with high-variety, low-volume production. In this process, each good has a different sequence of production and the steps involved are intermittent, moving from one department to another. The necessary machinery is arranged according to this sequence. This approach also lends itself to 'job lots' — that is, the manufacture of parts in small quantities. Many small to medium-sized manufacturers employ this process. In service businesses, such as banks or insurance companies, process layout is used to accommodate the handling of customers with different needs.

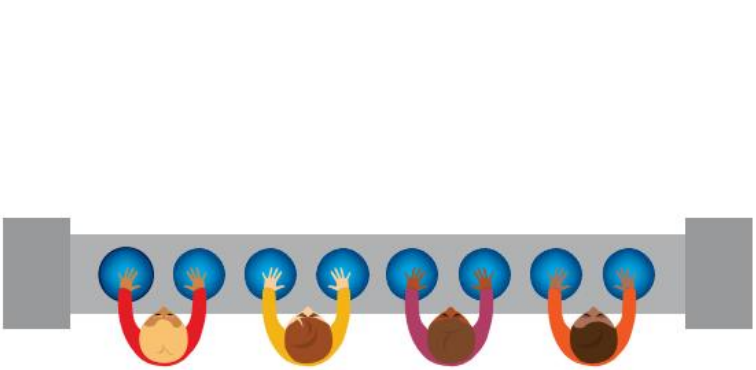
A feature of this approach, often used by businesses, is the creation of work cells or work teams (see figure 4.11). Cellular or team-based work arrangements can be used to create combinations of machinery and equipment to produce a single product or a range of similar products.

skills audit a formal process used to determine the present level of skilling and any skill shortfalls that need to be made up either through recruitment or training

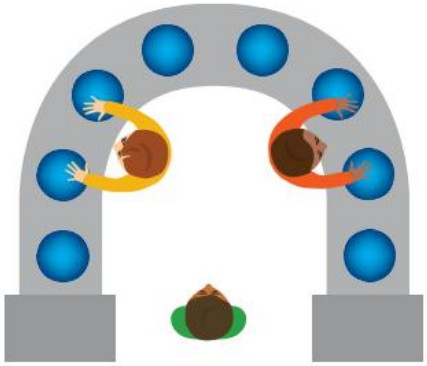
process layout the arrangement of machines so that the machines and equipment are grouped together by the function (or process) they perform

process production deals with high-variety, low-volume production

FIGURE 4.11 Various work cell layouts. This approach may also be adapted for new social distancing requirements stemming from the COVID-19 pandemic.



Current layout — straight lines make it hard to divide tasks.



Improved layout — workers have improved access. Fewer workers are needed.

Product layout

Product production (mass production) is characterised by the manufacturing of a high volume of constant quality goods. An assembly line is the most common layout for this type of production because it aims to achieve the best possible combination of personnel and machine use — 'assembly line balancing'. This type of layout is referred to as **product layout** where the equipment arrangement relates to the sequence of tasks performed in manufacturing a good. Work stations are arranged to match the sequence of operations, as work flows from station to station. Operations managers must set times for the assembly task, which requires an understanding of not only the nature of the task but also the tools and skills required. Examples of this process are the assembly of motor vehicles or the production of television sets. Emphasis is placed on sequencing the flow from one work cell to another.

product production (mass production) production that is characterised by the manufacturing of a high volume of constant quality goods

product layout layout in which the equipment arrangement relates to the sequence of tasks performed in manufacturing a product

FIGURE 4.12 An assembly line production method is the best example of a product layout.



Fixed position layout

Project production deals with layout requirements for large-scale, bulky activities such as the construction of bridges, ships, aircraft or buildings. With project production, it is more efficient to bring materials to the site; workers and equipment come to the one work area.

A **fixed position layout** is where a product remains in one location due to its weight or bulk.

FIGURE 4.13 Project production — the inputs are brought to the site.



Office layout

Again, the focus of an office layout is to enable the work to be performed efficiently (with minimal unnecessary disruption and time wastage) in a safe office environment. Typically an office space is organised around discrete **workstations**. This may be seen as the approach applied to a service-based business.

Office layout is tailored to meet the needs of the business. In a manufacturing business the office layout is often informal. It may even overlook the factory floor so that managers can supervise from their desk. In an accountant's office, clients need to feel welcome as they seek advice and information. In a doctor's surgery, privacy is a concern for patients so the layout of the surgery reflects this.

An office needs to be designed in a way that allows for smooth workflow; it should also
provide a space (lunch room, games room) that enables employees to take a break from the work environment if required.

A post-pandemic office layout will look significantly different. Some ideas include:

- hot desking — no personal objects to identify 'your' desk and minimal IT hardware that connects to your own laptop computer/device is available to all
- more space, fewer desks
- staggered shifts — team 'red' week 1, team 'green' week 2
- offices being used mainly for collaborations and meeting clients
- increased use of common areas where open space is preferable to small offices
- one-way systems in offices or on stairs, including the use of floor marking for quantifying social distance

project production deals with layout requirements for large-scale, bulky activities such as the construction of bridges, ships, aircraft or buildings

fixed position layout an operational arrangement in which employees and equipment come to the product

workstations the desk areas required by office workers, usually fitted with access to a computer monitor, keyboard, telephone, mouse and mouse pad and storage, and close access to a printer and scanner

- open windows wherever possible
- hand-sanitising stations in high-traffic areas
- open plan wherever possible but with airflow systems that filter and reduce the amount of exhaled air
- removing shared touch points — sensor-operated doors and windows rather than more traditional operating switches
- plastic dividing screens between desks.

Finally, the future could also see more effective workplace design — open spaces, flexible walls, open windows where possible, larger meeting areas or even the possibility of temporary hubs where people within the organisation can meet and then return to their homes to continue working remotely. These hubs can also be leased to other businesses.

FIGURE 4.14 The new office layout in a post-COVID-19 work environment that allows for social distancing.



SNAPSHOT

Case study: The office is dead! Long live the office in a post-pandemic world

Will office workers flock back to their cubicles and water coolers when the pandemic ends? Or will employees want to hold on to their newfound freedom and flexibility, while employers eye the lower costs of the lack of a physical footprint?

At least a few companies have already answered this question: Twitter, for example, says most of its employees can continue working from home forever, making the office merely a place to meet clients.

So what is he future of the 'traditional' office?

Organisational life is founded on relationships. Sure, the current remote work experiment has demonstrated that more jobs can be done virtually than many managers previously assumed. But jobs are comprised of tasks; organisations are comprised of relationships. And relationships require ongoing — and often unintended — interactions.

Decades of research provide important insight into how effective work relationships are built. We know that they require mutual trust and cooperation, and that physical proximity is critical to fostering trusting and cooperative relationships.

This is especially true in the knowledge and creative economies, as shared space promotes information sharing and collaboration. A 2009 study found that Google employees sharing physical space exchanged information more effectively than those located even on separate floors in the same building.

A similar study from 2013 showed that when scientists had to walk further from the lab to places like the restroom or the printer, they developed more research collaborations.

And a more recent study found that 'water cooler' socialisation was critical to new idea generation at business incubators, which support the growth of startup companies.

And as robots take over more human jobs thanks to automation and artificial intelligence, these relationships will matter more than ever.

So we believe that it's not the office itself that will remain but the necessity of physical proximity to keeping the modern organisation — and our work relationships — running smoothly.

That's why I believe the future of office work is likely to be much more flexible than ever before. Overall, including those who previously worked from home, a full 26 per cent said they plan to work remotely at least a few times each week when the pandemic is over — double the 13 per cent that said they did so prior to it.

Only 9 per cent of the workers we surveyed, however, said they want to completely abandon the traditional office. They seem to just want more balance. Given the option, many office workers would like to commute to a traditional office on some days and work from home on others.

Source: Beth Humberd, Deborah Salon & Scott F. Latham, 'The office is dead! Long live the office in a post-pandemic world',*The Conversation*, 24 July 2020.

on Resources

Weblinks Telstra
Toyota

KEY IDEAS

- Technology is the application of science or knowledge that enables people to do new things or perform established tasks in new and better ways.
- Business technology involves the use of machinery and systems that enable managers to undertake the transformation process more effectively and efficiently.
- Office or administrative technologies include a range of computers, communications devices and software applications.
- Manufacturing technologies include:
  - robotics — a programmable machine capable of doing several different tasks
  - computer-aided design (CAD) — a computerised design tool that creates products from a series of input parameters
  - computer-aided manufacturing (CAM) — software that controls manufacturing processes
  - 3D printing — allows a digital design to make an actual product through the use of polymers and other materials.
- Task design — classifying job activities so that employees can successfully perform and complete the task — is an essential aspect of transformations processes.
- Task design involves job analysis and can be done after a skills audit has been completed.
- There are three different forms of layout for manufacturing plants:
  - Process layout — machines and equipment are grouped together by the function (process) they perform
  - Product layout — machines and equipment relate to the sequence of tasks performed in manufacturing a product; for example, assembly line arrangement
  - Fixed position layout — employees and equipment come to the product.
- Modern office layout uses a workstation arrangement and in many cases an open office format.

4.5 Activities

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4.5 Quick quiz on	4.5 Exercise	4.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 6, 8, 9, 13, 16, 18, 19, 21, 22	4, 5, 7, 10, 11, 12, 14, 15, 17, 20, 23, 24, 25, 26, 27, 28	29

4.5 Exercise

Revision

1. **What** is the difference between technology and business technology?

Read the 'Technology — the virtual office' case study and answer questions 2 to 4.

2. **Identify** the types of technology that will be used by Mehrnoosh.
3. **Describe** how the use of cloud-based storage allows for greater workplace flexibility.
4. **How** does the use of technology enable flexibility and productivity, despite a staff member not being 'at work' in the usual sense of the term?
5. **How** does technology improve the transformation process in the (a) manufacturing sector and (b) service sector?
6. **State** two benefits and two costs of manufacturing technology.
7. **Why** is robotics set to be used increasingly by businesses?
8. **Identify** two benefits and two costs of robotics.
9. **Match** each term with the correct definition.

Term	Definition
a. Computer-aided design (CAD)	**A.** software that controls manufacturing processes
b. Robotics	**B.** a computerised design tool that allows businesses to create possibilities from a series of input parameters
c. Computer-aided manufacturing (CAM)	**C.** highly specialised forms of technology capable of complex tasks allowing a degree of precision and accuracy unmatched by human labour
d. 3D printers	**D.** allow a digital design to make an actual product through the use of polymers and other materials

10. **Detail** how technology can be used to optimise the transformation process in large-scale businesses. Include the terms 'computer-aided design', 'computer-aided manufacturing' and 'robotics' in your answer.

Read the 'Technology in production and services' case study and answer questions 11 and 12.

11. **Propose** two costs that would be associated with the use of integrated IT systems such as the use of computer-integrated manufacture (CIM) technology.
12. **Explain** the impact that 3D technology could have on production processes.

Read the 'Printing surfboard components' case study and answer questions 13 and 14.

13. **Identify** the alternative term used for 3D printing.
14. **Why** might surfers seek to to take advantage of 3D-printed surfboard fins.
15. What is task design and **why** is it important?
16. Consider table 4.1. Use the information provided and your own knowledge to **summarise** the steps involved in the task design process.
17. **Why** does Flight Centre carefully plan the layout of its stores?
18. **What** are the most important factors to consider when determining which layout to use?

19. Consider the layout of the last three stores you have visited. **State** which aspects of layout enhanced the customer experience and which could be improved.
20. **Distinguish** between process layout and product layout.
21. **Which** form of layout would suit the building of a bridge across a wide river and why?
22. **Outline** the usual layout for an office.

Read the case study 'The office is dead! Long live the office in a post-pandemic world' in section 4.5.3 and answer questions 23 and 24.

23. **How** could some modern workplaces in the future look in regard to the number of staff attending each day?
24. **Investigate** possible office layouts in a post-pandemic workplace.

Extension

25. **Demonstrate** how the use of technology can increase speed, accuracy and overall quality of the transformation process.
26. **Compare** the types of technology Telstra and Toyota use. **Explain** why the technologies they use are different. Use the weblinks in your Resources tab to help with your research.
27. 'Costs are high, people seem expendable and the work environment is too clinical — apart from that, technology is wonderful!' **Discuss**.
28. **Investigate** the operations needs that influence:
    a. process layout
    b. product layout
    c. fixed position layout.
29. Gemma has recently bought a fitness centre. She plans to renovate the premises and change the layout of the equipment. **Determine** the most suitable layout and justify your recommendation. **Create** a sketch for Gemma of the recommended layout. You may wish to use a multimedia application.

4.5 Exam questions

Question 1 (6 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q23a & b

North Coast Manufacturing makes customised furniture for its clients.

a. How could technology influence the transformation process at North Coast Manufacturing? **(2 marks)**
b. Explain TWO factors that it should consider when designing the process layout. **(4 marks)**

Question 2 (1 mark)

An operations manager is deciding how best to use resources during the operations process. Which operations process best describes this action?

A. Task design
B. Process layout
C. Monitoring
D. Scheduling

Question 3 (2 marks)

Describe the use of technology in the transformation process.

Question 4 (4 marks)

LO's Country Furniture manufacture furniture using recycled and plantation timber. The manager wants to reduce the time taken to produce each item. Due to increasing demand, she also wants to increase the quantity made per day. Explain TWO strategies that could achieve these operation process goals.

Question 5 (1 mark)

A small clothing business specialises in making event clothing. The five employees are assigned their own work station, separate from others, so that each may concentrate on their own creations. Which of the following best describes the operation process used by this business?

A. Technology
B. Task design
C. Process layout
D. Sequencing

More exam questions are available in your learnON title.

4.6 Transformation processes: monitoring, control and improvement

SYLLABUS LINK In this subtopic you will learn about how monitoring, control and improvement influence operations processes.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

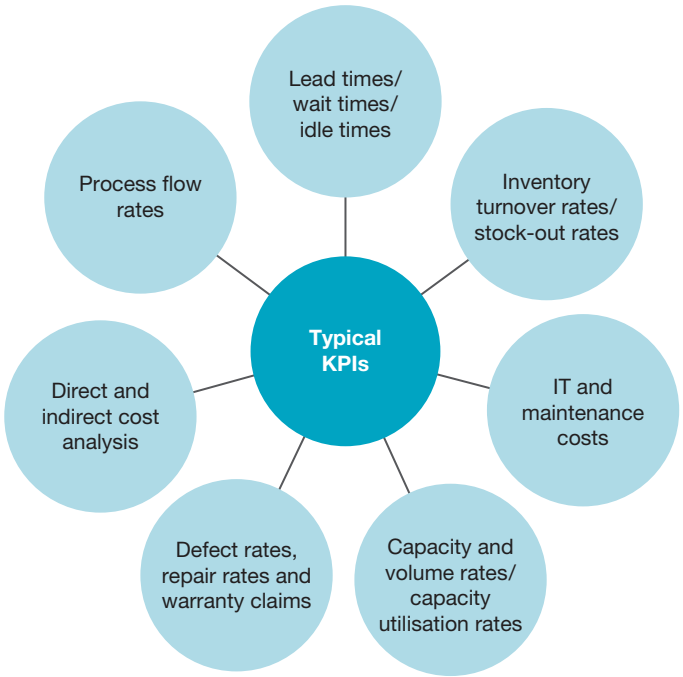
All operations processes should be monitored for effectiveness. The main transformational processes should be subject to control and this will require effective monitoring and a focus on continuous improvement. Monitoring and control lead to improvements when there is a focus on quality and standards.

4.6.1 Monitoring

Monitoring is the process of measuring actual performance against planned performance. During operations processes, monitoring is crucial. Monitoring involves the measurement of all aspects of operations, from supply chain management and the use of inputs, through to transformation processes and outputs.

monitoring the process of measuring actual performance against planned performance

FIGURE 4.15 Key performance indicators (KPIs) are measured as part of the monitoring process.



Monitoring typically is arranged around the need to measure key performance indicators (KPIs). KPIs are predetermined variables that are measured so that appropriate controls to operations processes can be made.

Monitoring of the KPIs gives operations managers a chance to measure how the business is going and to assess performance against targeted levels of performance.

4.6.2 Control

Control occurs when KPIs are assessed against predetermined targets and corrective action is taken if required. This means controlling compares what was intended to happen with what has actually occurred. If there is a discrepancy between performance and goals, changes and improvements can be made. All operations managers should exercise strict controls over the transformation processes. This can be done by setting challenging but reasonable performance targets. The business performance is then assessed regularly. The regular performance review is crucial because it should indicate any problems and if necessary intervention or corrective action can be taken.

Control requires operations managers to take corrective action. That is, the operations manager will make changes to the transformation process such as redesigning the facilities layout or adjusting the level of technology in order to correct the problem. Improvements in processes are often framed around quality. Quality controls, assurance and improvements are addressed fully in chapter 5.

control occurs when KPIs are assessed against predetermined targets and corrective action is taken if required

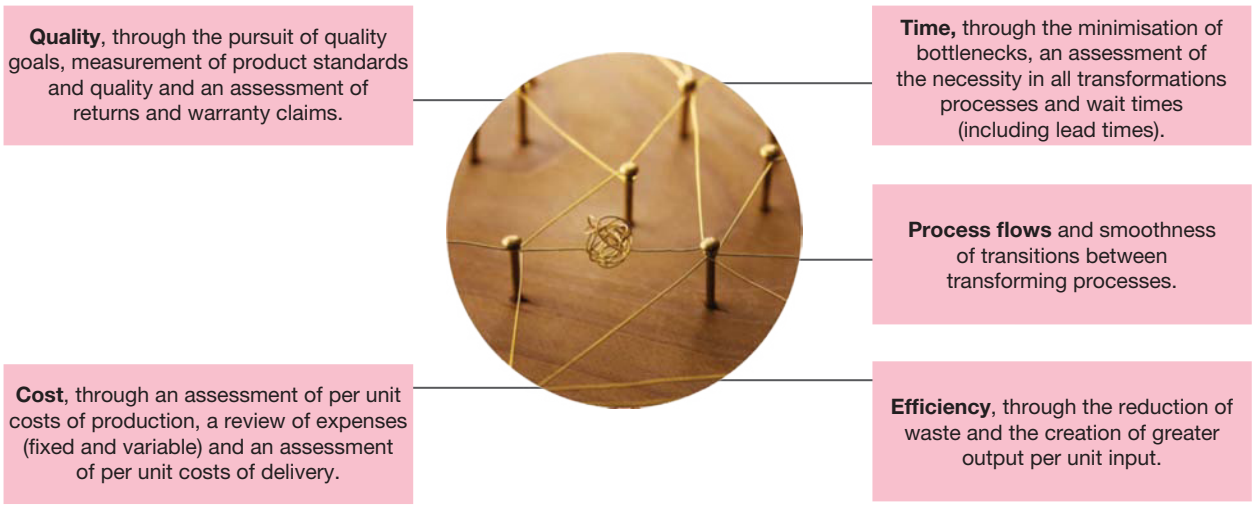
improvement refers to systematic reduction of inefficiencies and wastage, poor work processes and the elimination of any bottlenecks

bottleneck an aspect of the transformation process that slows down the overall processing speed or creates an impediment, leading to a backlog of incompletely processed products

4.6.3 Improvement

Improvement refers to systematic reduction of inefficiencies and wastage, poor work processes and the elimination of any bottlenecks. A **bottleneck** is an aspect of the transformation process that slows down the overall processing speed or creates an impediment leading to a backlog of incompletely processed products. Improvement typically is sought in time, process flows, quality, cost and efficiency.

FIGURE 4.16 Improvement refers to systematic reduction of inefficiencies and wastage, poor work processes and the elimination of any bottlenecks.



KEY IDEAS

- All operations should be monitored against KPIs for their effectiveness.
- Control occurs when corrective action is taken if there is a discrepancy between performance and goals.
- Improvements lead to reduction in inefficiencies such as bottlenecks.
- Continuous improvement involves ongoing commitment to achieving perfection.

4.6 Activities

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4.6 Quick quiz on	4.6 Exercise	4.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 5	3, 4, 6, 7, 8	2, 9

4.6 Exercise

Revision

1. **Define** each of the following terms: monitoring, control and improvement.
2. How would you monitor the performance of a retailer? **Support** your answer with reference to relevant examples.
3. From the list of KPIs shown in section 4.6.1 select which two you consider to be the most important. **Justify** your selection.
4. **Explain** why controls are important in the operations process.
5. **Define** two corrective actions you could implement if sales returns and warranty claims were increasing.
6. **a.** What would happen if a person visited a store to buy an item they wanted and the store had run out of stock?
   b. Propose two improvements you would implement to overcome the bottlenecks in supply that lead to lost sales.
7. **Recommend** why management should always strive for continuous improvement in business.
8. **How** can a business's management improve both its (a) quantity and (b) efficiency?

Extension

9. **Evaluate** the role of monitoring and controlling when it comes to creating improvements in transformation processes.

4.6 Exam questions

Question 1 (2 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q23c

Recommend a method of monitoring the effectiveness of the process layout.

Question 2 (1 mark)

Jacinta gathers information about staff sales and production. She is also responsible for checking turnover of inventory.

Which task of the operations processes is Jacinta performing?

A. Monitoring
B. Controlling
C. Organising
D. Scheduling

Question 3 (1 mark)

Bon is a manager in a hotel. He is to meet with other managers to evaluate the performance of each part of the transformation process as it applies to the hotel. Identify the task to be performed at this meeting.

A. Monitoring
B. Controlling
C. Organising
D. Scheduling

Question 4 (6 marks)

Bon is a manager in a hotel. He is to meet with other managers to evaluate the performance of each part of the transformation process as it applies to the hotel. Analyse TWO ways managers may undertake the process of monitoring, controlling and improving the processes at the hotel.

Question 5 (2 marks)

Distinguish between monitoring and controlling in the transformation process.

More exam questions are available in your learnON title.

4.7 Outputs

SYLLABUS LINK In this subtopic you will learn about outputs as an operations process, including customer service and warranties.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Essentially **outputs** are the result of a business's efforts — the final good or service that is delivered or provided to the consumer (see subtopic 2.1). While there is a distinction between service and manufacturing operations, in many cases, businesses carry out both types of operation. Mazda Australia, for example, separates its vehicle manufacturing operation from its customer service operation, although both elements are critical to the business's overall success. The operations manager must be able to link transformation processes to the activities performed by other areas of the business. Output must always be responsive to customer demands. Issues of quality, efficiency and flexibility must be balanced against the resources and strategic plan of the business.

The most obvious output of the operations process is the goods made or services provided. However, there are other, more subtle outputs. Customer service refers to how well a business meets and exceeds the expectations of customers in all aspects of its operations. Warranties are a business's promise to correct any defects in their goods provided or in the services delivered. Combined, customer service and warranties imply that the inputs and transformations processes are subject to scrutiny as the outputs will be assessed by consumers.

4.7.1 Customer service

A customer focus increasingly shapes operations processes, inputs, transformations processes and outputs that are all directed to meeting or exceeding customer expectations. In its totality, this is **customer service**. If a customer expresses dissatisfaction with a good on account of it being defective or not meeting quality expectations, finds wait times/lead times too long, returns the good or makes a warranty claim, then the operations processes need review.

outputs the end result of the business efforts — the good or service that is provided or delivered to the customer

customer service refers to how well a business meets and exceeds the expectations of customers in all aspects of its operations

Central to customer service is to ensure that the correct good or service is delivered or provided at the right place at the right time. Market research has shown that those businesses capable of providing superior customer service can:

- charge an average of 10 per cent more for the same goods and services
- grow twice as fast as their competitors
- increase their market share and profits.

FIGURE 4.17 Customers are the life-blood of any business. Without a customer base, a business will not be able to survive. Customer service, therefore, should always be of prime concern for any business.



BizFACT

The word 'customer' in Japan translates to mean 'honoured guest'. Australian businesses must remember that an 'honoured guest' will lead to repeat sales.

To maintain existing customers and attract new ones, the business needs to communicate with customers — there is anecdotal evidence that one dissatisfied customer usually tells 11 others, who in turn will tell another five.

Customer service can no longer be regarded as merely explaining the refund policy or providing a complaints section. Rather, it is an attitude that should be adopted by all departments and employees within the business. Exceeding customers' expectations is likely to be the key in developing long-term customer relationships; however, failure to do so will drive customers away.

4.7.2 Warranties

A good way to assess the effectiveness of operations processes is to measure the number of **warranty** claims. Warranty claims are made against goods that have defects arising from an issue in transformation. Although a small proportion of warranty claims are false, the number of claims made against a business on a particular product line or product range will give an indication of problems in the processing. Consider the example of the recent recall of cars carrying Takata airbags and sold in Australia. The recall of tens of thousands of cars led to the replacement of the faulty bags. However, these rectification costs are expensive. Operations managers need to trace the source of the fault in manufacturing and rectify it. In this way, the warranty claims lead the business to improve transformation processes.

Warranties will also apply to services. The supply of services must come with the statements that enable customers to cancel service contracts or to refund them the unused portion or be compensated for the reduced value if a major failure occurs.

warranty a promise made by a business that they will correct any defects in the goods they produce or services they deliver

KEY IDEAS

- The outputs of transformations processes include:
  - the goods made or services provided
  - customer service
  - warranties.
- Customer service refers to how well a business meets or exceeds the expectations of consumers.
- Exceeding customers' expectations is likely to be the key in developing long-term customer relationships.
- Warranties are an agreement to fix defects in products. An assessment of warranty claims can help a business to adjust transformations processes so that they become more effective.
- Warranties apply to services and enable customers to cancel contracts or seek a refund for the unused portion or be compensated for the reduced value should a major failure occurs.

4.7 Activities

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4.7 Quick quiz on	4.7 Exercise	4.7 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4	3, 5, 6, 7, 9	8

4.7 Exercise

Revision

1. **List** the three outputs of an operations process.
2. **What** is the aim of customer service?
3. 'Businesses that offer high levels of customer service have a much greater chance of success.' **Explain** why this is so.
4. **Describe** how customer service influences operations processes.
5. If good customer service is so important to the success of a business, **investigate** why customers often complain about the level of service they receive. Share your answer with the rest of the class.

6. **Why** is measuring the number of warranty claims a good way to assess the effectiveness of operations processes?
7. **Research** the recall of cars carrying Takata arbags. With reference to Takata and consumer warranties, **explain** the importance of honouring warranties to business success.

Extension

8. **Analyse** the effect of customer service on inputs, transformation processes and outputs.
9. From your own experience, **demonstrate** a business that offers (a) exceptional customer service and (b) poor customer service.

4.7 Exam questions

Question 1 (4 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q21b

A recently established bank has branches in Australian capital cities and online customers across Australia. The management of this bank wants to focus on improving operations processes. Explain how improving operations processes may lead to better customer service.

Question 2 (2 marks)

Explain outputs as a part of operations processes.

Question 3 (1 mark)

A mechanic guarantees her work and the quality of the parts used in her repair business. Which of the following best describes this part of her business operations?

A. Customer service
B. Warranties
C. Outputs
D. Transformation

Question 4 (1 mark)

Outline customer service as an output in operations.

Question 5 (2 marks)

Mohan Audio Visual Products (MAVP) advertises that all products sold have a shop and a manufacturer's warranty. Outline how a warranty can be included as an output of MAVP.

More exam questions are available in your learnON title.

4.8 Review

4.8.1 Summary

Inputs

- The operations process refers to the input–transformation–output process.
- Inputs are the resources used in the transformation process and can be classified as either transformed resources or transforming resources.
- Transformed resources are those inputs that are changed or converted in the operations process and include:
  - materials — the basic elements used in the production process, consisting of raw materials and intermediate goods
  - information — the knowledge gained from research, investigation and instruction, which results in an increase in understanding
  - customers — their desires and preferences are the starting point to production processes.
- Transforming resources are those inputs that carry out the transformation process and include:
  - human resources — they coordinate and combine other resources to produce goods and services
  - facilities — the plant (office or factory) and machinery used in the operations process.

Transformation processes: volume, variety, variation in demand and visibility

- Transformation is the conversion of inputs (resources) into outputs (goods or services).
- Transformation differs between manufacturing businesses and service businesses.
- A manufacturer transforms inputs into tangible products.
- A service organisation transforms inputs into intangible products.
- Transformation processes are influenced by:
  - volume — how much of a product is made
  - variety — the range of products made
  - variation in demand — the amount of a product desired by consumers
  - visibility — the nature and amount of customer contact (feedback).

Transformation processes: sequencing and scheduling

- Sequencing and scheduling are essential activities in operations processes.
- Sequencing refers to the order in which activities in the operations process occur.
- Scheduling refers to the length of time activities take within the operations process.
- Two tools that assist with sequencing and scheduling are:
  - Gantt charts — a type of bar chart that shows both the scheduled and completed work over a period of time
  - critical path analysis — a scheduling method that shows what tasks need to be done, how long they will take and what order is necessary to complete the tasks.

Transformation processes: technology, task design and process layout

- Technology is the application of science or knowledge that enables people to do new things or perform established tasks in new and better ways.
- Business technology involves the use of machinery and systems that enable managers to undertake the transformation process more effectively and efficiently.
- Office or administrative technologies include a range of computers, communications devices and software applications.
- Manufacturing technologies include:
  - robotics — a programmable machine capable of doing several different tasks
  - computer-aided design (CAD) — a computerised design tool that creates products from a series of input parameters
  - computer-aided manufacturing (CAM) — software that controls manufacturing processes
  - 3D printing — allows a digital design to make an actual product through the use of polymers and other materials.

- Task design — classifying job activities so that employees can successfully perform and complete the task — is an essential aspect of transformations processes.
- Task design involves job analysis and can be done after a skills audit has been completed.
- There are three different forms of layout for manufacturing plants:
  - Process layout — machines and equipment are grouped together by the function (process) they perform
  - Product layout — machines and equipment relate to the sequence of tasks performed in manufacturing a product; for example, assembly line arrangement.
  - Fixed position layout — employees and equipment come to the product.
- Modern office layout uses a workstation arrangement and in many cases an open office format.

Transformation processes: monitoring, control and improvement

- All operations should be monitored against KPIs for their effectiveness.
- Control occurs when corrective action is taken if there is a discrepancy between performance and goals.
- Improvements lead to reduction in inefficiencies such as bottlenecks.
- Continuous improvement involves ongoing commitment to achieving perfection.

Outputs

- The outputs of transformations processes include:
  - the goods made or services provided
  - customer service
  - warranties.
- Customer service refers to how well a business meets or exceeds the expectations of consumers.
- Exceeding customers' expectations is likely to be the key in developing long-term customer relationships.
- Warranties are an agreement to fix defects in products. An assessment of warranty claims can help a business to adjust transformations processes so that they become more effective.
- Warranties apply to services and enable customers to cancel contracts or seek a refund for the unused portion or be compensated for the reduced value should a major failure occurs.

4.8.2 Key terms

bottleneck an aspect of the transformation process that slows down the overall processing speed or creates an impediment, leading to a backlog of incompletely processed products
capital–labour substitution machinery and technology displace people by doing the work they do
computer-aided design (CAD) a computerised design tool that allows businesses to create product possibilities from a series of input parameters
computer-aided manufacturing (CAM) software that controls manufacturing processes
control occurs when KPIs are assessed against predetermined targets and corrective action is taken if required
critical path analysis (CPA) a scheduling method or technique that shows what tasks need to be done, how long they take and what order is necessary to complete those tasks
customer relationship management (CRM) the systems that businesses use to maintain customer contact
customer service refers to how well a business meets and exceeds the expectations of customers in all aspects of its operations
facilities the plant (factory or office) and machinery used in the operations processes
fixed position layout an operational arrangement in which employees and equipment come to the product
Gantt chart a type of bar chart that shows both the scheduled and completed work over a period of time. It is often used in planning and tracking a project.
improvement refers to systematic reduction of inefficiencies and wastage, poor work processes and the elimination of any bottlenecks
information the knowledge gained from research, investigation and instruction, which results in an increase in understanding
inputs the resources used in the transformation (production) process
intermediate goods goods manufactured and used in further manufacturing or processing
key performance indicators (KPIs) specific criteria used to measure the efficiency and effectiveness of the business's performance

lead time the time it takes for an order to be filled from the moment it is made
materials the basic elements used in the production process, consisting of two types: raw materials and intermediate goods
mix flexibility the mix of products made, or services delivered, through the information process
monitoring the process of measuring actual performance against planned performance
outputs the end result of the business efforts — the good or service that is provided or delivered to the customer
process layout the arrangement of machines so that the machines and equipment are grouped together by the function (or process) they perform
process production deals with high-variety, low-volume production
product layout layout in which the equipment arrangement relates to the sequence of tasks performed in manufacturing a product
product production (mass production) production that is characterised by the manufacturing of a high volume of constant quality goods
project production deals with layout requirements for large-scale, bulky activities such as the construction of bridges, ships, aircraft or buildings
raw materials the essential substances in their unprocessed state
robotics used in engineering and specialised areas of research, as well as on assembly lines where a programmable machine capable of doing several different tasks is required
scheduling the length of time activities take within the operations process
sequencing the order in which activities in the operations process occur
skills audit a formal process used to determine the present level of skilling and any skill shortfalls that need to be made up either through recruitment or training
task design involves classifying job activities in ways that make it easy for an employee to successfully perform and complete the task
telecommute to 'commute', or travel to work, electronically. This means that home or another location becomes the worksite and work is delivered via email or the internet.
transformation the conversion of inputs (resources) into outputs (goods and services)
transformed resources those inputs that are changed or converted in the operations process
transforming resources those inputs that carry out the transformation process
volume refers to how much of a product is made
warranty a promise made by a business that they will correct any defects in the goods they produce or services they deliver
workstations the desk areas required by office workers, usually fitted with access to a computer monitor, keyboard, telephone, mouse and mouse pad and storage, and close access to a printer and scanner

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Digital documents	Key terms glossary (doc-35660) Chapter crossword (doc-36212)
Interactivity	Chapter crossword (int-7153)
Exam question booklet	Chapter 4 Exam question booklet (eqb-0026)

4.8 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

Exercise 1: Multiple choice questions

1. Operations processes include which of the following?
   - **A.** Transforming raw materials, energy and human resources into a finished good or service
   - **B.** Transforming labour to produce higher quality products
   - **C.** Using transformation processes such as goods and services to produce outputs
   - **D.** Innovative distribution strategies
2. Which of the following is an example of capital in a business?
   - **A.** Technology
   - **B.** Funds used to finance business activities
   - **C.** Machinery
   - **D.** Transportation
3. What is the difference between a manufacturing business and a service business?
   - **A.** Manufacturing processes are highly automated whereas services rely more on customers.
   - **B.** Manufacturing is labour intensive whereas services are customer intensive.
   - **C.** Value-adding in manufacturing involves additional inputs, however, services do not.
   - **D.** Manufacturing creates tangible products whereas services create intangible products.
4. Managing lead times and volume is critical to avoid which of the following?
   - **A.** Underproduction and increased inventory costs
   - **B.** Overproduction and increased inventory costs
   - **C.** Lost back orders, leading to the need for discounting
   - **D.** Decreased wastage
5. Decreased demand creates operational challenges that include which of the following?
   - **A.** Labour is not readily available.
   - **B.** Energy and power cannot be readily sourced.
   - **C.** Suppliers cannot supply quickly enough.
   - **D.** Production may need to slow to avoid inventory build up.
6. Transformation processes are influenced by which of the following?
   - **A.** Volume, variety, value-adding
   - **B.** Variety, value-adding, visibility
   - **C.** Variety, variation in demand, visibility
   - **D.** Volume, variation in production, visibility
7. Which of the following is correct in relation to Gantt charts?
   - **A.** They help identify steps in a process that need to be undertaken to produce a good or service.
   - **B.** They show sequence and scheduling of the process of maximising sales.
   - **C.** They make it easy to monitor planned activities against business goals.
   - **D.** They are different to CPA because they show the shortest path through the production process.
8. The benefits of CAM include which of the following?
   - **A.** It enables affordable robotics for small- and medium-scale producers.
   - **B.** The software can design the steps required to create the product in the shortest lead time.
   - **C.** It links with CAD software for instant manufacturing.
   - **D.** A and C
9. Task design allows managers to break down work in which of the following ways?
   - **A.** Into a series of jobs in which each contributes to the final product
   - **B.** By skills, to analyse any skills shortfalls
   - **C.** To assist in maximising product layout
   - **D.** To develop key performance indicators

10. Output must always be responsive to customer demands because of which of the following?
    - **A.** Companies with superior customer service grow five times as fast as their competitors.
    - **B.** Companies can charge an average of 10 per cent more for the same goods and services.
    - **C.** Companies can increase their market share and profits by 100 per cent.
    - **D.** Companies lose 10 customers for every complaint.

Exercise 2: Exam practice questions

Question 1 (6 marks)

a. **Clarify** the inputs used in the operations process. **(2 marks)**

b. **Explain** the role of transformed and transforming resources in the operations process. **(4 marks)**

Question 2 (4 marks)

Distinguish between transformed and transforming resources.

Question 3 (6 marks)

Analyse the transformation process in operations management.

Question 4 (8 marks)

a. **What** are outputs in the operations management process? **(2 marks)**

b. **Assess** the role of customer service and warranties as outputs in the operations management process. **(6 marks)**

Question 5 (6 marks)

Examine the transformation process and the role of sequencing and scheduling in the operations management process.

Question 6 (6 marks)

Analyse the input–transformation–output process in operations management.

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5 Operations strategies

5.1 Overview

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5.1 Overview
5.2 Performance objectives
5.3 New product or service design and development
5.4 Supply chain management
5.5 Outsourcing
5.6 Technology: leading edge, established
5.7 Inventory management
5.8 Quality management
5.9 Overcoming resistance to change
5.10 Global factors
5.11 Review

5.1.1 Introduction

Business managers will have a range of operations strategies to ensure that they continue to work towards achieving broader business goals — financial, social and/or environmental.

An initial focus on performance objectives (quality, speed, dependability, flexibility, customisation and cost) will provide managers with the stepping stone to other strategies that may be highly relevant now or may gain greater significance over time. It is important to ensure that quality is not compromised in an effort to cut costs. Aiming to meet this objective can provide the catalyst that ensures a business establishes and maintains a competitive advantage over its rivals.

A business's management in the maturity stage may decide that new goods and/or services ought to replace those which it offers but that are no longer in demand. It may be that a change in direction in the form of extending its line of goods and/or services may provide a worthwhile addition to current lines. If so, the new products will go through a comprehensive process of design and development before their market release.

Increasingly the role of supply chain management is prominent in businesses delivering goods, especially when external shocks disrupt their ability to meet customer demand. Effective logistics and the use of e-commerce have assisted businesses enormously but the situation can be complicated when global supply chains are affected by decisions beyond the business's control; for example, border closures.

Increasing labour costs, among other reasons, have prompted some businesses in Australia to outsource the manufacture of goods and delivery of some services to overseas suppliers. This offshoring of jobs has caused some adjustment as people are released from traditional employment to work in other growing sectors of the economy where their skills can be put to better use.

Australia's businesses continue to make use of the latest technology to develop new products that have achieved international recognition.

Inventory management, especially in respect to maximising often scarce financial resources, has begun to place greater emphasis on effective strategies to ensure it is used to its best advantage.

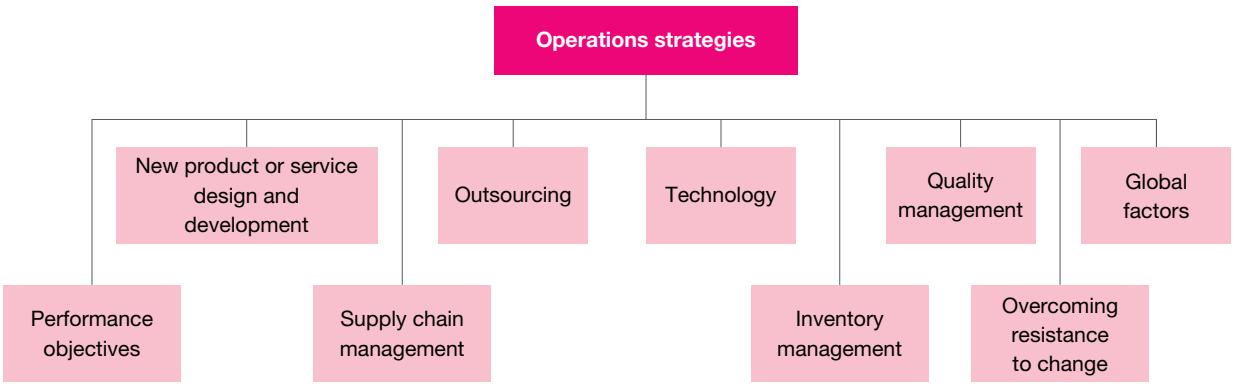
An ever-changing business environment will require management that is aware of implications for its business. Overcoming resistance to change is one of the operations strategies that may present more complex decisions for managers, with respect to balancing financial costs while avoiding the possibility of inertia.

Increased globalisation presents opportunities for business but also a degree of risk. Sourcing decisions can be complicated, especially with regards to exchange rates that can be volatile or contracts that can be difficult to enforce.

Smaller domestic markets make economies of scale difficult to achieve. However, opening to global markets may assist with reducing costs, learning from global contractors and engaging more fully in research and development. All of these factors present management with opportunities for more effective operations strategies.

To achieve operations goals and broader business goals, operations managers can apply numerous operations strategies. An overview of the operations strategies that can be applied are shown in figure 5.1. Note that the full range of operations activities is subject to the strategies. You can see that the strategies relate to inputs, sourcing and supply chain management, and transformation (or throughput) processes that involve technology, quality management and inventory management as well as outputs.

FIGURE 5.1 An overview of operations strategies



As with all strategies or tactics, the starting point is a set of goals or performance objectives. These performance objectives help define what inputs are required and influence all aspects of the transformation processes.

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Digital document Key terms glossary (doc-35662)
Exam question booklet Chapter 5 Exam question booklet (eqb-0027)

5.2 Performance objectives

SYLLABUS LINK In this subtopic you will learn about performance objectives as an operation strategy, including quality, speed, dependability, flexibility, customisation and cost.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Performance objectives are goals that relate to particular aspects of the transformation processes. These objectives or targets will be set so that the business becomes more efficient, productive and profitable. Performance objectives help to inform all of the strategies that are discussed in this chapter. The operations strategies seek to achieve one or more of the performance objectives detailed below. The six main performance objectives that can be allocated to particular key performance indicators (KPIs) are:

- quality
- flexibility
- speed
- customisation
- dependability
- cost.

5.2.1 Quality

Quality is often determined by consumer expectations, which are then used to inform the production standards applied by the business. Quality performance objectives include:

- quality of design
- quality of conformance
- quality of service.

Quality of design

Quality of design arises from an understanding of consumers and their preferences. It extends to how well a good is made or a service is delivered. Design begins prior to the creation of a product and will determine inputs, and how the transformation processes will be arranged and will perform in relation to the production of the good or service. Typically, a high-quality design for a good will be clear from the high-grade materials used in manufacturing, its care and presentation, how aesthetically pleasing and functional it is, and how robust and long-lasting it hopes it will be when it finds its way to the customer. Further, a well designed and produced goods will normally attract a higher price. As a performance objective, a business needs to decide the quality of product it will deliver to the market. As quality inputs add cost, this will be reflected in a higher price that some consumers may not want to pay.

FIGURE 5.2 Mercedes-Benz — an example of an organisation that competes on quality



Quality of conformance

Quality of conformance is the focus on how well the product meets the standard of a prescribed design with certain specifications. The specifications do not have to require high-quality inputs. Quality of conformance is a measure of how consistently products achieve compliance (conformance with) the desired specifications regardless of the standard of the specifications. Consider this: a Mercedes Benz vehicle combines very high-quality design with high standards of conformance. A cheap plastic toy is of very low-quality design but if it meets the low-quality design specifications, it would have a high standard of conformance, indicating a certain quality of process.

performance objectives goals that relate to particular aspects of the transformation processes

quality of conformance the focus on how well the product meets the standard of a prescribed design with certain specifications

Quality of service

Quality of design and quality of conformance can be applied to the design and delivery of services. In this sense quality refers to:

- service reliability
- does the service meet the client's needs
- is the service delivery responsive consumer expectations.

SNAPSHOT

Case study: Apple and Samsung — quality and price



While Apple is the most recognisable smartphone, it is not the most-sold or most-purchased brand. Samsung makes the most-used smartphone. Both Apple and Samsung are noted for their quality. High quality is achieved when a business focuses on its operations processes and implements strategies to achieve performance objectives such as quality. Global brands such as Apple and Samsung invest huge amounts resources into product design development and testing. Such commitment to investment as well as the focus on innovation means that these brands can charge a premium price that reflects the cost of investment as well as the quality of the products.

5.2.2 Speed

Speed refers to the time it takes for the production processes to respond to changes in demand. Speed requires that changes in input levels and processing times can align with consumer expectations.

As a performance objective, speed aims to satisfy customer demand as quickly as possible. Therefore, goals for speed include reduced waiting, shorter lead and speedier processing times.

To achieve these goals requires fewer procedural and technical bottlenecks and smooth internal communications. A procedural bottleneck can occur when internal processes that ensure smooth operations are not followed.

speed refers the time it takes for the production and the operations process to respond to changes in market demand

SNAPSHOT

Case study: FurnDesign — avoiding bottlenecks



FurnDesign Pty Ltd accepts orders for handmade furniture. The sketches from the clients must be scanned then emailed, and FurnDesign turns these sketches into computer-generated images. All emails arrive in a common inbox and are generally held there until viewed by sales representatives. The senior sales representative and designer, Johnson, has requested that staff send his clients' emails directly to him. However, his staff are often forgetful and do not comply with his request. To complicate matters further, Johnson often forgets to check the common inbox and when this happens, the business has the potential to lose sales, and has already lost three this year. This is a procedural bottleneck that can be overcome with some additional training. To avoid technical bottlenecks, FurnDesign has formed an alliance with another furniture maker and will send excess orders to that business when demand exceeds their capacity. This change has required staff training to ensure they follow procedures carefully.

5.2.3 Dependability

Also referred to as reliability, **dependability**, as a performance objective, refers to how consistent and reliable a business's products are. Dependability, in respect to goods, refers to how robust the item is before it fails. One measure of dependability is measured by warranty claims. A highly durable good is often a dependable good. Perishable goods can also be dependable if they are of a consistent and predictable standard.

In respect to services, dependability refers to consistency of service standards and reliability. A measure for service dependability is the number of complaints received; the fewer the complaints, the more likely the service is dependable.

5.2.4 Flexibility

Also identified as adaptability, **flexibility** refers to how quickly operations processes can adjust to changes in the market. For example, changes in market demand cause a pressure on capacity. However, it may take three months for the business to change capacity. Similarly, it can take a business months to create a new product or extend a product line. It is important to note that time and flexibility are related; the faster the processing time, the greater the likelihood that processes can be adjusted quickly.

Flexibility can be best achieved by increasing the capacity of production and, in particular, by using plant and machinery better. Alternatively a business can buy new technology that increases its flexibility and capacity. Another option is changing product design, thus creating a broader variety. These options enable the business to better meet a broader range of consumer requirements.

With services, flexibility can be achieved through increasing the number of service providers, increasing their skill level and also by improving the level of technology used when delivering the service.

5.2.5 Customisation

Most products tend to be standardised; however, over time customer preferences are creating a custom option for goods. **Customisation** refers to creation of individualised products to meet the specific needs of customers. Services are often customised, however aspects of services can be standardised, as seen in the fast-food sector.

A customer orientation to operations might imply that over time businesses would orient processes towards customisation; however, while there is greater choice for consumers these days than at any time in history, standardisation of products is still the most widely used option. Variations in the features of goods such as colour, size and functionality offer some level of differentiation. In regard to services, a customer focus also offers some differences between competing businesses but in many cases there remains a high degree of standardisation.

Production of many of today's goods and services is based on the principle of **mass customisation**; a process that creates a standard, mass-produced item such as a motor vehicle or computer, which is then modified to specific customer requirements. However, full customisation is rare and can only be offered when products (goods or services) are created after an order specifying the requirements is received. The cost of full customisation is significantly higher than the cost of producing standardised products. For this reason, only those businesses with a product that can be easily adapted tend to customise unless the actual business model is one of a customised approach to all products, as often seen in niche markets.

dependability as a performance objective, refers to how consistent and reliable a business's products are

flexibility how quickly operations processes can adjust to changes in the market

customisation refers to creation of individualised products to meet the specific needs of the customers

mass customisation a process that allows a standard, mass-produced item to be personally modified to specific customer requirements

SNAPSHOT

Case study: Adidas — mass customisation

Adidas has come up with a unique mass production strategy. It undertakes mass customisation. In order to do so Adidas varies the standard product offerings for a range of shoes and clothing. Allowing people to personalise their purchase through detailing their specific size requirements, Adidas enables consumers to experience the benefits of mass customisation. The customisation aspect of Adidas is called 'miAdidas' — a reference to the individual consumer's chance to order customised (personalised) products. The level of personalisation can extend to varying the size (length and width) of shoes for either foot and can opt for colour, style and size variations in clothing. However, in order to allow production processes to adapt to variation in orders, choices are limited. In this way the process may be termed 'constrained customisation'.



FIGURE 5.3 In what may sound like a contradiction in terms, many businesses are integrating mass production/standardisation principles with customisation: mass customisation. Most vehicle manufacturers use this process in their production and operations processes. Customers can add optional extras to suit their personal tastes.



5.2.6 Cost

Cost as a performance objective refers to the minimisation of expenses such that operations processes are conducted with cost reduction and how to achieve it both playing a role in management decision making. When a business establishes its operations processes, costs incurred often determine the product's selling price. Over time, businesses seek to become more efficient and thus reduce costs. The acquisition of new capital equipment, more efficient use of inputs and strategies to reduce waste are all ways of reducing production costs. Moreover, a business will also seek to negotiate discounts with suppliers, and manage inventory in such ways as by minimising warehousing and identifying efficient distribution processes.

cost as a performance objective, refers to the minimisation of expenses so that operations processes are conducted as cheaply as possible

All of the performance objectives will be allocated particular targets or goals, and will be measured against the achievement of those targets. In this way, the performance objectives are expressed as KPIs, with particular goals for each. Although not all performance objectives may be fully realised, a business will have targets for each and will allocate resources to target the performance objective that is most likely to have the best result for business profitability.

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Weblink Adidas

KEY IDEAS

- Operations strategies are based around the need to achieve performance objectives.
- Performance objectives are goals that relate to particular aspects of the transformation function and can be allocated to particular key performance indicators (KPIs) in the following areas.
  - Quality, including:
    - design: how well a good is made or a service is delivered
    - conformance: how well the good or service meets a prescribed design with a certain specification
    - service: how reliable, suitable and timely the service delivery is
  - Speed: the time it takes for the production and the operations processes to respond to changes in market demand
  - Dependability: how consistent and reliable a business's goods or services are
  - Flexibility: how quickly operations processes can adjust to changes in the market
  - Customisation: the creation of individualised goods or services to meet the specific needs of the customers
  - Cost: the minimisation of expenses so that operations processes are conducted as cheaply as possible
- Each of the performance objectives will be allocated targets or goals.

5.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.2 Quick quiz on	5.2 Exercise	5.2 Exam questions

Select your pathway

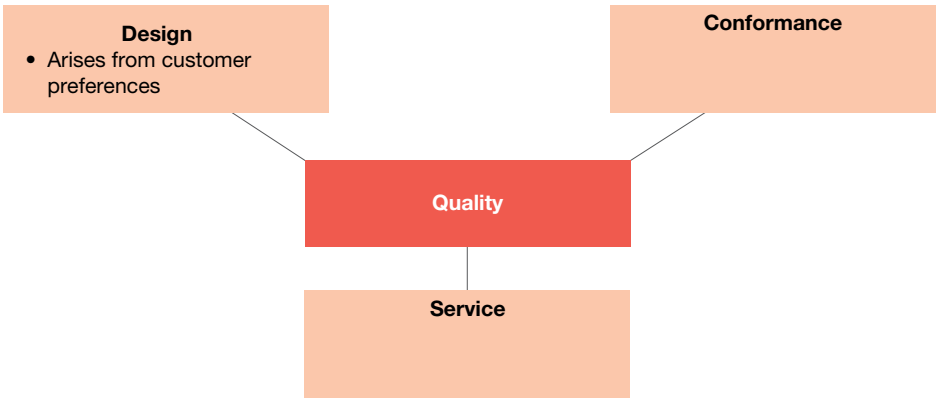
LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 7, 11, 12, 15, 16, 18	5, 6, 8, 9, 10, 13, 14, 17, 21	4, 19, 20

5.2 Exercise

Revision

1. **List** six performance objectives used by operations managers.
2. **a. Identify** a performance objective for a business that makes cars.
   b. How can a service-based business, such as an accountant, use performance objectives?
   c. When are performance objectives necessary for a business?

3. Complete a concept map to **summarise** the three quality performance objectives. The concept map has been started for you.



Read the 'Apple and Samsung — quality and price' case study and answer questions 4 and 5.

4. **Analyse** the role of quality in the reputation of smartphones.
5. **Explain how** quality and price are related in respect to smartphones.
6. **Demonstrate** what is meant by the term 'speed' in relation to operations processes.
7. **Recall** three goals for speed.
8. **Demonstrate** the impact of a bottleneck on speed in operations processes.

Read the 'FurnDesign — avoiding bottlenecks' case study and answer questions 9 and 10.

9. **Distinguish** between procedural and technical bottlenecks.
10. **Explain** how a procedural bottleneck can be overcome.
11. **What** is the relationship between dependability and the number of warranty claims or complaints received about a product?
12. **Describe** how flexibility of processes is linked to market demand.
13. **Why** is full customisation of products rare?
14. **Account** for why many businesses offer mass customised products.
15. **Identify** three operations strategies a business can use to reduce cost.

Read the 'Adidas — mass customisation' case study and answer questions 16 to 18.

16. **What** is customisation?
17. **How** does mass customisation affect sales?
18. Navigate to the miAdidas website and **Identify** some of the customisable options available for potential customers.

Extension

19. **Assess** the role of performance objectives in achieving maximum productivity.
20. In small groups, use the brainstorm technique to **determine** what happens when the product's performance:
    a. does not meet customer expectations
    b. meets customer expectations
    c. exceeds customer expectations.

    Select a representative to share your group's comments with the rest of the class.
21. Using the table that follows, **propose** how the performance objectives you have learned about can be used to evaluate the operations processes.

Key performance indicator	How the KPI can be used to evaluate the operations processes
Quality	
Speed	
Dependability	
Flexibility	
Customisation	
Cost	

5.2 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q15

A sandwich shop bakes a variety of breads throughout the day. Customers select their choice of bread and filling(s) and sandwiches are then made to order.

Which pair of performance objectives would have influenced the development of this approach?

A. Cost and efficiency
B. Efficiency and quality
C. Cost and customisation
D. Quality and customisation

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q9

A soup manufacturer finds it difficult to cope with the increase in demand for soup in winter.

Which performance objective could assist this business to meet the demand?

A. Cost
B. Customisation
C. Dependability
D. Flexibility

Question 3 (6 mark)

Source: HSC 2016 Business Studies Exam, Section II, Q25

With reference to a business you have studied, analyse the relationship between cost and quality in the operations of the business.

Question 4 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q9

Which performance objective measures how well a product meets the prescribed design specifications?

A. Cost
B. Flexibility
C. Quality
D. Speed

Question 5 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q9

A business wants to minimise the volume of its waste.

Which performance objective is the business trying to achieve?

A. Cost
B. Customisation
C. Flexibility
D. Speed

More exam questions are available in your learnON title.

5.3 New product or service design and development

SYLLABUS LINK In this subtopic you will learn about new product or service design and development as an operations strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The operations processes of business require the creation, or design and development, of new products (goods and services). The design, development, launch and sale of new products enables a business to grow and to attain a competitive advantage.

5.3.1 New product design and development

There are different approaches to new product design and development. The first arises from a specific approach to product development, in which the preferences of consumers, as identified by market research, determine which products are designed and developed.

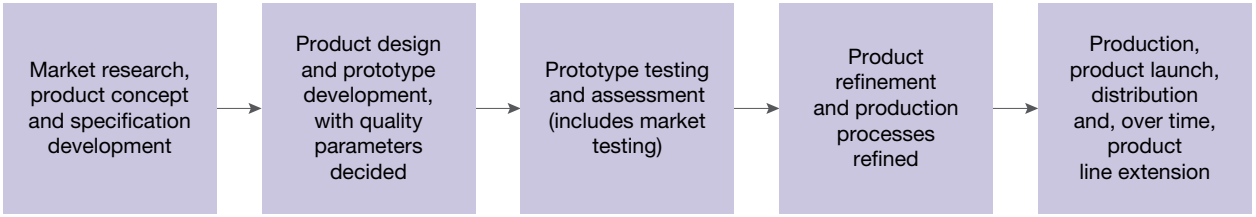
The second arises from changes and innovations in technology that enable new, appealing products to be made because they use advanced techniques that give products greater functionality. For example this is the approach used by smartphone manufacturers. Apple's major strength is that it maintains complete control over the design and development of both software and hardware, unlike many other companies that outsource product design to save on costs.

FIGURE 5.4 Apple's continued success can be attributed to the power of product design and development. Apple has established a reputation as a company that produces goods that focus on innovative, consumer-oriented technology.



The steps in the product design and development process are identified in figure 5.5.

FIGURE 5.5 The steps in the product design and development process



Designing and developing a product requires careful consideration of quality, supply chain management, output capacity and cost. These factors should be taken into account throughout the design and development process. Quality is a factor that must be considered because in this market-orientated production, the customers will demand particular quality, and certain attributes and features. Supply chain management, as a factor, is an important consideration, because a new product will draw from suppliers and may extend the range of supplies sought, and the timing or the volume of supplies. Furthermore, any new product will have an impact on capacity and may increase the use or range of present resources, or require an investment in new capital equipment. Finally, cost can be determined through the quantity and type of inputs, time and energy used in processing. Value is directly related to cost but also includes the customer's perception of product utility. **Product utility** is defined as the usefulness and value that a product has from the consumer's point of view. These four factors (quality, supply chain management, output capacity and cost) should be considered by operations managers while proceeding through all aspects of product design and development.

5.3.2 Service design and development

Service design, being customised in nature, has always taken the position of the customer or client as the starting point in the design process. Some services do not require customer interaction (or have very limited interaction) and therefore they tend to be largely standardised in nature. For example, consider the work of a shelf packer in a grocer, a short-order cook in a fast-food outlet or a petrol station attendant. Contrast this work with the work of an accountant, lawyer, medical specialist or journalist. Each of the latter professions will customise their work to the needs of a client.

When designing services, factors such as whether the business will provide **explicit service**, what the anticipated **implicit service** will be and what, if any, goods will be required with the delivery of the service must all be taken into consideration. Cost will be determined once service features have been determined.

Explicit service is the tangible aspect of the service being provided such as the application of time, expertise, skill and effort. Implicit service is based on a feeling and is therefore intangible. The implicit aspects of a service are the psychological wellbeing — the feeling of being looked after — that comes with the provision of the service. In design, both the explicit and implicit aspects need to be addressed. All clients or customers using a service need to feel that their particular needs are being met. Therefore, when it comes to design, the service, level of skill, time and expertise must be embedded so that as the service is being delivered, the customer knows that they have been specifically catered for. This would give implicit satisfaction.

FIGURE 5.6 New services arise from technological breakthroughs. For example, developments in laser technology have led to the creation of new types of businesses. Laser technology is used in eye correction surgery, cosmetic surgery, hair removal and skin treatments.



product utility the usefulness and value that a product has from the consumer's point of view

explicit service the tangible aspect of the service being provided, such as the application of time, expertise, skill and effort

implicit service is based on a feeling and is therefore intangible. The implicit aspects of a service are the psychological wellbeing — the feeling of being looked after — that comes with the provision of the service.

Services using goods

Sometimes in the delivery of services, goods may also be required. For example, a surgeon performing knee surgery will require swabs, bandages, sutures, medical equipment and an operating theatre. Similarly, a tutor may need specialised books, access to a networked computer, paper and stationery. These additional aspects must be considered when designing and developing a service because each can complement the delivery of the service. For example, technological breakthroughs in equipment can create a range of services that did not previously exist, as shown in figure 5.6.

KEY IDEAS

- A business needs to design and develop new products and services.
- Two different approaches determine product design and development:
  - consumer preferences
  - changes and innovations in technology.
- Important factors in new product design and development include quality, supply chain management, output capacity and cost.
- Service design and development differs from the design and development of products as services are intangible and 'consumed' as they are produced.
- A service can be:
  - explicit — the application of time, expertise, skill and effort
  - implicit — the feeling of being looked after.

5.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.3 Quick quiz on | **5.3 Exercise** | **5.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 5, 6	1, 2, 4	7, 8

5.3 Exercise

Revision

1. **Distinguish** between the approaches that can be used for product design and development.
2. **Explain** the role of innovation in Samsung's success as a producer of consumer electronic goods.
3. **Describe** the four factors that should be given consideration when undertaking new product design and development.
4. **Why** are customers important to the design and development of services?
5. **Outline** the role of explicit and implicit service for business success.
6. **What** is the role of design as a factor that influences the price of goods and services?

Extension

7. Research the designs created by a furniture-maker, clothing brand or car manufacturer and **assess** how well that producer takes into account customer needs when making designs. Make direct reference to a range of products in their portfolio.
8. 'The best designs are those that accommodate what people need now and should need in the future. Thus they anticipate how the thinking of people is changing.' With reference to actual examples, **evaluate** the accuracy of this statement.

5.3 Exam questions

Question 1 (1 mark)

Katarina has the task of presenting the prototype of a product to a target market. She will report reactions back to her operations team. Which part of operations strategies is Katarina performing?

A. Designing
B. Supply chain management
C. Development
D. Outsourcing

Question 2 (1 mark)

A part of the operations team at Oral and Dental Care Pty Ltd has created a new, more flexible toothbrush. It is an innovation on their existing range. The feedback from a sample test market has been positive and has helped with the choices of colour for production.

The changes to operations processes are currently being discussed.

Identify the operations strategy described in this example.

Question 3 (6 marks)

A part of the operations team at Oral and Dental Care Pty Ltd has created a new, more flexible toothbrush. It is an innovation on their existing range. The feedback from a sample test market has been positive and has helped with the choices of colour for production.

The changes to operations processes are currently being discussed.

Analyse the role of this strategy in operations at Oral and Dental Care Pty Ltd.

Question 4 (1 mark)

Jerome's Fine Food is a restaurant in the city. The owners have identified an opportunity for delivery of corporate lunches. They have trialled a menu and are presently assessing the reaction. Which of the following best describes this operations strategy?

A. Development
B. Design
C. Monitoring
D. Outsourcing

Question 5 (2 marks)

Distinguish between design and development as operations strategies.

More exam questions are available in your learnON title.

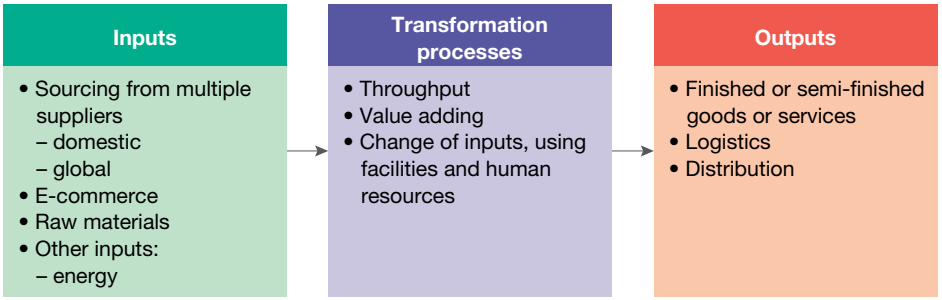
5.4 Supply chain management

SYLLABUS LINK In this subtopic you will learn about supply chain management, including logistics, e-commerce and global sourcing.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Supply chain management (SCM) involves integrating and managing the flow of supplies throughout the inputs, transformation processes (throughput and value adding) and outputs to best meet the needs of customers. Since the supply chain is influenced by what is sold and what is returned, supply chain management involves both sourcing (supply-side) as well as logistics and distribution (see figure 5.7).

FIGURE 5.7 A representation of the supply chain for contemporary business



The supply chain for a good can be better understood by starting with the final good and then tracing backwards through all processes that add value, all the way to its inputs. This process demonstrates that the supply chain includes production processes, suppliers of raw materials, energy, labour, distribution and all sources (domestic and global). This type of analysis of supply, which is a 'top-down' or systems approach, is necessary when creating strategies for supply chain management.

There are three key aspects to supply chain management:

- logistics
- e-commerce
- global sourcing.

supply chain management (SCM) involves integrating and managing the flow of supplies throughout the inputs, transformation processes (throughput and value adding) and outputs in order to best meet the needs of customers

logistics a term broadly referring to distribution but includes transportation (including transportation modes), the use of storage, warehousing and distribution centres, materials handling and packaging

distribution the ways of getting the goods or services to the customer

5.4.1 Logistics

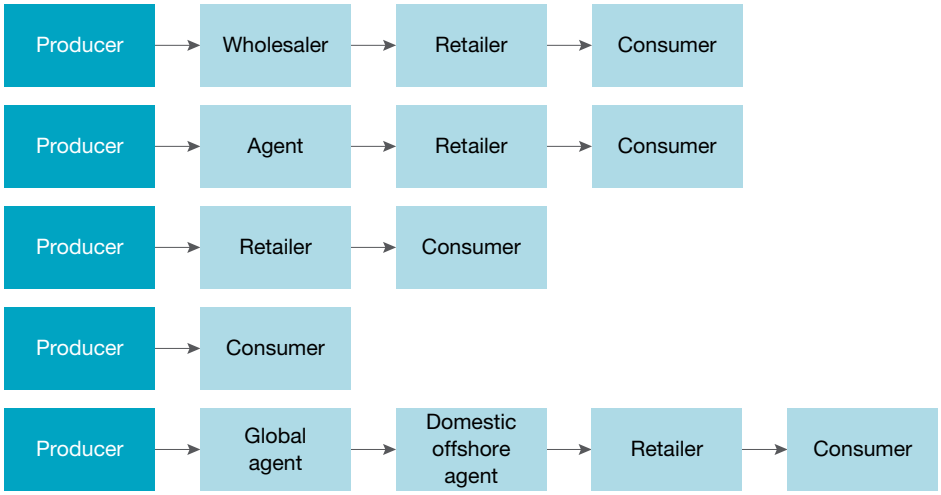
Logistics is a term broadly referring to distribution but also includes:

- transportation (including transportation modes)
- the use of storage, warehousing and distribution centres
- materials handling and packaging.

Distribution

Distribution is the method of delivering goods or services to the customer. A business may use different forms of physical distribution. These are shown in figure 5.8.

FIGURE 5.8 The different forms of distribution channel or channel choices that may be used in physical distribution



Transportation and distribution

This aspect of logistics is concerned with the physical movement of inventories. Various modes of transportation can be used and each has its own strengths and weaknesses, as shown in table 5.1.

TABLE 5.1 A comparison of different modes of transport used in distribution

Mode of transport	Speed	Distance	Cost	Capacity
Bicycle or motorbike courier	High in inner city areas	Low (under 10 km)	Low	Documents and files
Van	Moderate	Up to 100 km	Moderate	Up to 500 kg
Truck	Moderate	Up to 4000 km	Moderate	Large items, up to 20 tonnes
Train	Slow/moderate	Up to 8000 km	Low/moderate	High volume, up to 40 000 tonnes/train
Aeroplane	High	Up to 40 000 km	Very high	Moderate volume of between 100 and 150 tonnes
Ship	Slow/moderate	Up to 40 000 km	Low	Large coal carriers, up to 200 000 tonnes, but oil carriers may be able to carry twice this weight

The type of good and the cost of transportation will determine the mode of transportation selected. Some goods, due to their nature, can be transported only by particular modes (for example, coal and crude oil, which can be transported only by freighter on the seas or by train on land), whereas for other goods there is a variety of choices (for example, native Australian flowers).

Storage, warehousing and distribution centres

Storage involves finding a secure place to hold stock until it is required. When dealing with inventories a business must address the issues of storage, warehousing and the use and location of distribution centres. Storage of inventory is necessary when there are numerous sales outlets and where demand is variable and needs a responsive supply chain. Storage may be long term or short term and goods may have particular characteristics that necessitate special storage requirements. For example, cold storage is used for perishable goods and

storage involves finding a secure place to hold stock until it is required

assists to increase their shelf-life. Storage is closely associated with warehousing, although storage does not always require the use of warehouses.

Warehousing

Warehousing is the use of a facility for the storage, protection and, later, distribution of stock. Warehouses, also called distribution centres or distribution hubs, are places for holding inventories and therefore particular costs are associated with warehousing, including the cost of:

- the premises
- insurance and security for the stock
- stacking and moving the stock
- carrying excess stock or redundant stock if not sold
- shrinkage costs and losses from theft or reasons not accounted for
- stock subject to damage (e.g. water damage) if not correctly stored.

warehousing the use of warehouses for the storage, protection and, later, distribution of stock

BizFACT

Major retailers such as Aldi, Coles and Woolworths use a network of distribution centres to assist with inventory management, distribution and costs management. The location of the centres is very carefully assessed and they are often highly technologically advanced facilities. The location of the centres is designed to lower lead times and also avoid stock out (shortages).

Distribution centres (DCs)

A distribution centre is slightly different to a warehouse in that it is not intended for long-term storage. Rather, distribution centres are strategically located so as to minimise the time it take to supply stock to retail outlets. The use of distribution centres is an important operations strategy and requires managers to balance the cost of such centres with the time saved in logistics. Distribution centres may be air-conditioned and/or have cold storage facilities, and they may also be co-located with transportation hubs.

FIGURE 5.9 The main purpose of distribution centres is the short-term storing, handling and wholesale distribution of goods. They have easy access to either a railway hub or a major road network. They allow a business to consolidate local operations and centralise the distribution hub, providing operational efficiencies and cost savings.



BizFACT

In the very competitive supermarket sector, Coles has undertaken two innovations that affect how it distributes product. The first is the creation of a 'dark store' that services the online market. The second is the use of Deliveroo — a business that can distribute product within thirty minutes of the order. Both these developments were in response to increased competition and, it is argued, the entry of Amazon into the Australian market.

Materials handling and packaging

A final aspect of logistics concerns materials handling and packaging. Materials handling is an important aspect of the movement and storage of goods, and therefore particular standards and methods of operating need to be applied. because some products require particular skills, care or attention when being moved. For example, delicate glassware needs to be transported and stored carefully, and it needs to be packaged in a way that protects it from damage. Similarly, some goods can be dangerous (such as chemicals and fuels) and their transportation and storage can carry particular hazards. The government has regulations that require dangerous goods be stored and handled in particular ways, and it also requires packaging to be of a particular standard and to carry warnings.

5.4.2 E-commerce

E-commerce involves the buying and selling of goods and services via the internet. With reference to supply chain management, e-commerce is relevant to particular forms of sourcing. The impact of e-commerce may be explained with reference to the business and its sourcing, and the customer and their orders that are received electronically.

Business sourcing and e-commerce (e-procurement)

Many businesses have decided that their supply chain is best managed through electronic ordering. **E-procurement**, or the use of online systems to manage supply, allows suppliers direct access to the business's level of supplies. When stock falls to a pre-determined point, replacement occurs even without a formal request from the buyer. This process is enabled by what is called business-to-business arrangement (B2B). **B2B** refers to direct access from one business (the supplier) to another (the buyer), allowing the supplier to assess the needs of the buyer and meet them in a timely manner. B2B e-commerce has exceeded all growth expectations as the internet facilitates a more efficient approach to supply chain management.

B2B is common in manufacturing. For example, Samsung is a major supplier to Apple in its production of the iPhone. Apple also has B2B relationships with Intel, Panasonic and Micron technology.

e-commerce the buying and selling of goods and services via the internet

e-procurement the use of online systems to manage supply, which allows suppliers direct access to the business's level of supplies

B2B direct access from one business (the supplier) to another (the buyer), allowing the supplier to assess the needs of the buyer and meet them in a timely manner

B2C the selling of goods and services to consumers over the internet, with payment usually by credit card

E-commerce and the consumer

The increasing use of e-commerce by consumers also has an effect on the supply chain. Businesses may opt to sell directly to consumers in transactions called business-to-consumer — **B2C**. Alternatively, technology may allow specialist sites to enagage with customers. An example is Agoda.com, which sells accommodation to travellers on behalf of hotels. A business that sells direct to consumers via the internet or that allows other internet-based businesses to do so clearly must be able to manage supplies that are affected by this diversity of ordering options. In this case, it should be clear that stock levels must be managed well and information exchanged frequently so that accurate stock levels can be presented to prospective customers.

BizFACT

Note that e-commerce has had a significant impact on physical distribution. Consumers in Australia and other nations are increasingly shopping and buying online. This means that distribution from the business to the consumer must be quick, efficient and secure.

FIGURE 5.10 The internet is revolutionising how businesses and consumers interact. When the Australian dollar trades at high levels, then online purchases are relatively cheap. Sometimes purchasing from other nations can be lower than half the cost of purchasing from a local retailer and delivery may be free. This represents a very significant challenge for domestic retailers, who were successful in calling for the federal government to ensure that overseas sellers impose the Goods and Services Tax (GST) on all of their sales to consumers in Australia.



5.4.3 Global sourcing

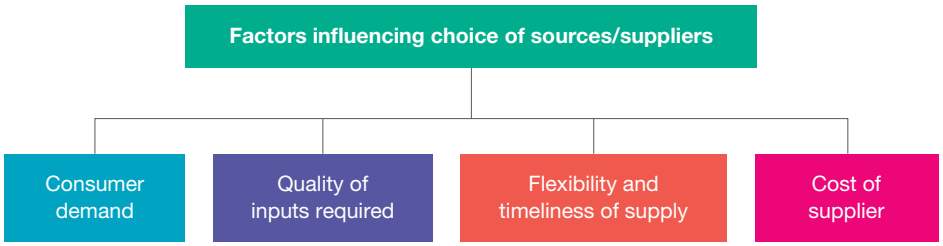
Before considering the role of global sourcing, it is worthwhile to consider 'sourcing' as a general concept. Also referred to as 'procurement' or 'purchasing', **sourcing** refers to the purchasing of inputs for the transformation process. Sources or inputs are drawn from a range of suppliers. When determining which sources to use (choosing a supplier), a business will need to do each of the following.

- Assess consumer demand so that the volume of inputs required is known.
- Determine the quality of inputs that match the quality of the products that the business would like to deliver to the market in produced goods.
- Assess how responsive (flexible) and timely the supplier is with respect to changes in demand.
- Evaluate the cost of supplies/inputs from the supplier against other suppliers offering supplies of similar quality.

sourcing the purchasing of inputs for the transformation process

Sourcing strategy typically revolves around these four factors as shown in figure 5.11.

FIGURE 5.11 The factors influencing choice of sources/suppliers



SNAPSHOT

Case study: Desperately seeking toilet paper, pasta or hand sanitiser? Some relief is just weeks away



Panic buying, shop shelves emptied of toilet paper, hand sanitiser, pasta and other household supplies, supermarkets policing limits on buying products, Amazon and eBay stopping opportunists from selling items at exorbitant prices.

When will things get back to normal?

The good news: well before the coronavirus crisis is over.

Usually a well-oiled supply chain guarantees no shortages or excesses in products. Products bought in the supermarket are quickly replenished, ensuring stock is always available.

Logistics for toilet paper, hand sanitiser and pasta are usually highly efficient. Companies are pleased to have lean, skinny supply chains. These products sell at low margins. For the profit they return, they can take up a lot of space in a store (as in the case of toilet paper). So distributors want to keep inventory at a minimum.



Happily, demand is usually highly predictable, so product moves slowly and continuously from factory to distribution centre to store and finally to you.

These, however, are not usual days.

The shelves for these products (and others) are empty as everyone goes into 'hoard mode' simultaneously. If a product is sold out, all you can do is wait for more to arrive. And because these supply chains are slow and unresponsive, you might also buy as much as you can the next time.

The information of a spike in demand made its way from shops and distributors to manufacturers a few weeks ago. Now manufacturers, suppliers and transporters – all profit driven – are moving to answer the call.

Their challenge is finding a balance between being too conservative and underproducing (leaving shelves empty) or being too exuberant and overproducing (getting lumbered with the cost of unsold stock). Ramping down production and distribution will take as much time as it did to ramp up.

Manufacturers and distributors, however, now have weeks of information about the degree of extra demand being put on usually very predictable supply chains. With that information, the only things stopping supply returning to normal well before coronavirus contamination reaches a peak is a major disruption to production or transportation — and so far there's no sign that will occur.

So which shelves will be replenished sooner? If you have a product at home, take a look at the package. Where is it made?

Local supply chains are much more responsive. Products made in your country, especially in your region, will hit the shelves sooner. If the product comes from overseas, response rates are significantly different and you have to allow 10 to 12 weeks to be safe.

Some quick research on lead times in the toilet paper industry shows most orders are fulfilled in about 10 days (three weeks at most).

Expansion can be accelerated but still depends on new buildings, new equipment, new skilled employees and possibly new suppliers. This can't be achieved in weeks or months.

Fortunately hand sanitiser is what economists call a substitute good. It's quite replaceable with some other form of soap. So too is pasta. You can always have noodles, or rice, or wraps, tacos and so on.

Even toilet paper has its substitutes. But all the indications are it shouldn't come to that.

Source: Flavio Romero Macau, 'Desperately seeking toilet paper, pasta or hand sanitiser? Some relief is just weeks away', *The Conversation*, 18 March 2020.

Businesses are increasingly utilising technologies and structuring their operations in such a way as to take advantage of global sourcing. **Global sourcing** refers to the decision by management to acquire supplies or services without being constrained by location; that is, to engage with the suppliers that best meet its sourcing requirements. While global sourcing carries particular benefits, it may also present challenges. For example, benefits include cost and expertise advantages, and access to new technology and resources. Challenges arise with the possible relocation of aspects of the operations process, the increased cost of logistics, storage and distribution, managing different regulatory conditions between nations, and the increasing complexity of overall operations when sourcing from diverse locations.

global sourcing a broad term that refers to businesses purchasing supplies or services without being constrained by location. In the supply chain management activity, global sourcing means buying or sourcing from wherever the suppliers are that best meet the sourcing requirements.

KEY IDEAS

- Supply chain management (SCM) involves the management and flow of supplies throughout all inputs, transformations processes and outputs.
- There are three key aspects to SCM: logistics, e-commerce (including e-procurement) and sourcing (including global sourcing).
- Logistics refers to the physical distribution and transportation of products. The use of warehouses and distribution centres is crucial to the successful management and movement of inventories.
- E-commerce enables businesses to source through online links to suppliers through business-to-business (B2B) processes and also enables customers direct access to products through business-to-consumer (B2C) processes.
- Sourcing, in the context of SCM, involves the purchasing of inputs for transformations processes.
- Global sourcing involves the use of global markets for the purchasing of any supplies; however, in the context of SCM, global sourcing refers to where and how supplies are sourced within the limitation of geography.

5.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.4 Quick quiz on | **5.4 Exercise** | **5.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 6, 7, 8, 9, 11, 12	2, 5	10, 13

5.4 Exercise

Revision

1. Match the term by **identifying** the correct definition.

Term	Definition
a. Supply chain management	A. Involves the buying and selling of goods and services via the internet
b. B2B	B. The distribution, transportation, storage, warehousing, and materials handling and packaging
c. Sourcing	C. Involves assessing the number of suppliers in order to reduce the number of suppliers to the least amount
d. E-commerce	D. Businesses purchasing supplies of services without being constrained by location
e. E-procurement	E. Involves integrating and managing the flow of supplies throughout the inputs, transformations and outputs
f. Global sourcing	F. The purchasing of inputs for the transformation process
g. Supplier rationalisation	G. The use of online systems to manage supply, which allows suppliers direct access to the business's level of supplies
h. Logistics	H. Business-to-business transactions

2. **Why** is it important that the supply chain be well managed?
3. **Identify** three key aspects of supply chain management.
4. **What** are the four factors a business should consider when choosing a supplier (sourcing)?

Read the 'Desperately seeking toilet paper, pasta or hand sanitiser? Some relief is just weeks away' case study and answer questions 5 to 7.

5. **How** has COVID-19 affected usually reliable supply chains for toilet paper, hand sanitiser and pasta?
6. **Outline** the challenges supply chains have in meeting additional demand for toilet paper, hand sanitiser and pasta.
7. **Describe** the factors that affect the ability of the supply chain to meet demand and ensure that goods are re-stocked on shelves sooner rather than later.
8. **Outline** the benefits and challenges of global sourcing.
9. Complete the sentences by **identifying** the correct term from the following list:

consumers	chain
e-procurement	stock
information	supply

a. Many businesses today have their supply _____ managed through electronic ordering referred to as _____.
b. The increasing use of e-commerce by _____ has an effect on the _____ chain.
c. When a business engages in e-commerce, _____ levels must be managed well and _____ exchanged frequently so that accurate stock levels can be presented to prospective customers.

10. **Determine** the most suitable method of transportation for the following items. Justify your answer.
    a. Coal from the Hunter Valley to China
    b. Motor vehicles from the factory to a retailer
    c. A legal document from one office to another within the same city
    d. A small parcel from Sydney to London
    e. Food from a local fast-food restaurant to a household
    f. Cartons of fresh and packaged food from a warehouse to the local supermarket
11. With reference to appropriate examples, provide a brief **summary** of storage, warehousing and distribution centres.
12. **What** is the importance of materials handling and packaging?

Extension

13. **Assess** the role and importance of transportation and distribution in effective supply chain management.

5.4 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q13

Sani works for a large manufacturing business. She organises the transport of raw materials and finished products across Australia.

Which of the following describes her area of responsibility?
A. Logistics
B. Service design
C. Global sourcing
D. Leading edge technology

Question 2 (6 marks)

Source: Adapted from HSC 2013 Business Studies Exam, Section II, Q23a & c

Casey owns and operates an independent discount fuel and convenience store.
a. Outline ONE way that e-commerce could assist Casey with supply chain management. **(2 marks)**
b. Is supply chain management important to Casey's business? Justify your answer. **(4 marks)**

Question 3 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q11

Which of the following is an essential aspect of logistics?
A. Undertaking a skills audit
B. Checking the quality of all output
C. Materials handling and packaging
D. The creation of a budget for new machinery

Question 4 (1 mark)

Which of the following are activities in supply chain management?
A. Movement and storage of raw materials
B. Internet delivery instructions by customers
C. Sourcing materials from around the globe
D. All of the above

Question 5 (2 marks)

Regent Consultants help businesses to improve their business performance by improving supply chain management (SCM). Describe how supply chain management can improve business performance.

More exam questions are available in your learnON title.

5.5 Outsourcing

SYLLABUS LINK In this subtopic you will learn about the advantages and disadvantages of outsourcing as an operations strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Outsourcing involves the use of external providers to perform business activities. The theory behind outsourcing is that when a service is performed by an external provider that specialises in a particular business function, it will do so at a lower cost and with a greater effectiveness than the same task done within the business hierarchy. The term 'outsourcing' is often called business process outsourcing (BPO). Business process outsourcing is a term that captures a range of outsourced business processes including:

- operations such as manufacturing, value-adding manufactures, design, merchandising, sourcing, distribution and logistics
- human resources including employee remuneration, employee counselling, pensions, data management, training and development, and travel and expenses management
- administrative work including data entry and 'back office' work
- information technology (IT) including data work, desktop outsourcing and network outsourcing (remotely hosted software applications).

Other types of outsourcing include:

- finance and accounting outsourcing (FAO) including preparation of financial accounts and reports, analytics and taxation compliance
- knowledge process outsourcing (KPO) including the outsourcing of managerial work such as marketing strategy, public relations and management decision making
- legal process outsourcing (LPO) including paralegal support, legal support (including drafting, research and counsel) and other legal services (such as patents and trademarks).

The different forms of outsourcing that may be used by business are shown in table 5.2.

TABLE 5.2 Forms of outsourcing

Forms of outsourcing	Onshore	Offshore
Captive or in house (do-it-yourself)	Commonwealth Bank of Australia (CBA), Sydney	Dell or Intel in Penang, serving all of Dell or Intel globally
Non-captive (outsourced to third parties through the market) External providers/vendors	Unilever India, using Capgemini in Bangalore and Dairy Farm in Hong Kong using Capgemini	British Airways (UK) using WNS Global Services (Mumbai, India) or General Motors using AT&T (Americas)

5.5.1 The outsourcing decision

Before a business decides to use outsourcing as an operations strategy, managers need to assess whether the use of outsourcing is viable. The factors that must be considered when assessing whether and when to use outsourcing are:

- Whether to outsource or not: this requires assessing whether the use of outsourcing is cheaper and more efficient than performing the work in house.
- If deciding to outsource, the managers must decide which geographical location is favoured.
- The managers must also decide which vendors to use.
- If the decision is to outsource then details such as the management of the outsourcing contract, the length of contract, the KPIs and service levels are required.

Four different outsourcing options can be used, as shown in table 5.3.

TABLE 5.3 Outsourcing options

Outsourcing option	Name of outsourcing option	Features of the outsourcing option
Option 1	Creation of shared services centres (SSC)	This is an in-house outsourcing option that involves the creation of an in-house centre that performs work for multiple subsidiaries.
Option 2	Use of 'fee-for-service' arrangement	A low-risk, short-term strategy that involves engaging a supplier for fixed services at a pre-determined price. It allows the business to test the outsourcing market prior to making a change.
Option 3	Joint ventures	The business engages an outsourcing services provider but the provider is also free to outsource to other businesses in the same industry. An example of such a provider is WNS Global Services (Mumbai, India), which British Airways used for ticketing. WNS Global Services now provides ticketing for at least 26 other major airlines including Virgin Atlantic.
Option 4	Use of a 'build-operate-transfer' approach	This involves offshore outsourcing and involves contracting with external organisations. The use of contracts that detail agreed levels of service against pre-determined KPIs is a feature. The relocation of services to a new offshore location (build-operate) is then transferred to an independent vendor that the company contracts.

The incidence of outsourcing, either domestically or globally, is increasing with business structures changing to benefit from lower costs and greater efficiency.

SNAPSHOT

Case study: Outsourcing — for and against



The term outsourcing describes a range of different types of arrangements where a business takes on contractors to do work that can be performed by the business. Outsourcing may be *onshore* (in the same nation), *near-shore* (in a close nation within the region) or *offshore* (a third nation that can be outside of the immediate region). Technological advances have enabled a high degree of outsourcing. As all facets of business can be outsourced, technology can enhance communications and allow for management of outsourced activities.

Outsourcing brings a number of benefits, including cost savings, the capacity to have specialised support, the simplification of business processes and improvements in quality. This can be seen in the outsourcing of financial processes to India by Australia's 'big four' banks that have become both increasingly efficient and also profitable.

However, outsourcing has also been criticised. For example, when Bonds decided to outsource there was a perception by Australian consumers that quality would be compromised. Moreover, the loss of domestic employment caused negative publicity. Nevertheless, the same consumers who criticise businesses that use outsourcing as an option often take advantage of the lower prices that result. For example, Virgin and Optus customers benefit from discounted telecommunications costs in part as a result of the use of outsourcing of the call centre to the Philippines.

5.5.2 Advantages of outsourcing

The advantages or benefits of outsourcing are the following.

- *Simplification*. This arises from reducing the number of activities performed within the business.
- *Efficiency and cost savings*. Access to cheaper labour, regulatory differences and skilled labour in offshore locations all lead to cost savings for business.
- *Increased process capability*. This comes from access to improved technologies and highly skilled labour. Improved process capability means products are produced and delivered to the market with improved levels of service.
- *Increased accountability*. This is achieved through the use of service level agreements (SLAs), which contractually bind the vendor to pre-determined targets on KPIs
- *Access to skills/resources lacking within the business*. A business outsourcing to a nation such as India or Vietnam, may well find that there is access to highly skilled and disciplined labour at low cost. This gives a double saving as there is then no need to spend money on training and developing labour resources.
- *Capacity to focus on core business or key competencies*. The use of outsourcing enables a business to focus on that which it cannot outsource: its vision, purpose, sustainable advantage through innovation, and so on.
- *Strategic benefits*. There are four important aspects to this.
  - The first benefit arises from using outsourcing to avoid trade barriers. For example, global businesses may offshore into different Chinese provinces to become a 'local' supplier and hence get around barriers that prevent foreign companies from trading.
  - A second benefit is that the use of a vendor that outsources for others within the same industry can bring the benefit of expertise gained from outsourcing to competitors.
  - A third benefit arises from trading in different time zones. The use of India, Malaysia, the Philippines, Vietnam and China for processing work allows businesses in Australia, USA and Europe to conduct operations during the day and to have processing work done overnight by the outsourcing vendor.
  - A fourth benefit is that strong partnerships between the business and the outsourcing vendor can lead to the vendor suggesting innovative solutions to the business that may increase the business efficiency and productivity over time.
- *Improvements to in-house performance*. A business using outsourcing and therefore focusing on core competencies can improve in-house performance as it can really focus on making internal changes that reduce cost and improve profitability.

There are also issues arising with the use of outsourcing, which businesses must address or overcome if they are to realise its benefits.

FIGURE 5.12 There are many advantages and disadvantages of outsourcing to offshore locations.



5.5.3 Disadvantages of outsourcing

The challenges facing businesses that use outsourcing include the following.

- *Cost versus benefits.* This refers to how long it takes to repay the cost of organising outsourcing and make the required organisational changes. Over time businesses will experience cost savings; however, it could take two or three years. If a business reduces internal inefficiencies, businesses may become more efficient and productive without using outsourcing.
- *Communication and language.* This is an issue between the business and the outsourcing vendor, and is a key issue in managing the relationship. When negotiating to outsource, the business might focus too much on the decision to outsource rather than consider the ongoing relationship with the vendor (which typically lasts three to five years). This can lead to confusion over expectations. Moreover, as outsourcing often occurs across two or more regions, there can be cultural differences, language differences and differences in the way business issues and problems are managed. This can lead to a misalignment between the business and the outsourcing vendor. There may also be misunderstandings about what the agreed service levels are and what KPI measures are acceptable.
- *Loss of control of standards and information security*. When a business opts to outsource, it can feel a loss of control over standards and also over how information is used. Recent issues have occurred where a Chinese manufacturer of toys for the Mattel brand (a leading USA toy brand) did not adhere to the design specifications outlined in the SLA and used too much lead in toys. Similarly, Australian banks have found privacy within outsourced operations in India may not be as secure as it is was when the functions were performed in-house.
- *Hierarchies.* A business using outsourcing may be aiming to eliminate costs associated with hierarchies, yet managing complex outsourcing agreements can create its own hierarchies, thereby maintaining business inefficiency.
- *Organisational change and redesign.* Outsourcing may be accompanied by a high level of business change and organisational redesign. There may be downsizing, causing the loss of domestic employment. An option can exist for job migration for employees who may be losing work to gain employment in the outsourcing vendor business. However, even if desired, work permits/work visas may prevent this from being an option.
- *Loss of corporate memory and vulnerability.* A significant disadvantage arises from the reliance on the outsourcing provider. Key knowledge of processes and solutions may be lost with the transfer of business processes to outside parties. To counter this, some businesses such as the banks create 'shadow teams' to retain corporate knowledge and, if required, processing capability. Business may also require that the outsourcing vendor have strategies in place in case there is a regional crisis (such as an earthquake) that severely disrupts communication and leads to information losses.
- *Information technology.* As the use of outsourcing grows so too does the need for supporting information technology (IT). There is a cost and time associated with the use and adaptation of IT to the specific requirements of the business and the outsourcing vendor. The cost and time can significantly reduce any financial advantages accruing in the short term with the use of outsourcing.

SNAPSHOT

Case study: Global outsourcing at Optus

Optus is an Australian company with headquarters in Macquarie Park, New South Wales. It is wholly owned by Singtel, a Singaporean multinational telecommunications company. Optus outsources some of its customer service functions to call centres located in India and the Philippines. It does so to reduce costs of labour and to ensure that the business remains competitive, as well as to ensure that its customers are provided with quality service as its call centre operations continue to grow.

Optus recently spent three years setting common standards across its outsourced call centres, relying heavily on data and analytics. The standards program incorporated three business process outsourcing (BPO) partners and

approximately 4000 offshore staff. The standards covered a range of aspects in the management of employees including recruitment and training through to how well staff serve Optus' customers.



Vaughan Paul, Vice President of Digital Consumer at Optus said that the program had helped Optus to improve its net promoter scores (NPS). The net promoter score measures the willingness of customers to recommend a business to others. It therefore indicates the customer's overall satisfaction with a business's product or its customer service, as well as the customer's loyalty to the business.

Optus believed that its three-country presence in call centre operations would protect it from any disruptions. However, like other telecommunications companies, Optus was affected by lockdown requirements in India and the Philippines due to the COVID-19 pandemic. The lockdowns meant that its outsourced call centres were unable to operate as they did previously. To cover the shortfall in customer service and support, the business was required to develop its local call centre operations. Optus therefore retrained 1500 existing Australian staff and recruited a further 500 new employees to better serve customers.

Optus also made efforts to restart call centre operations in the Philippines and India. For example, call centre 'microsites' were set up in the Philippines — call centres within walking distance of where staff live which met restrictions by not requiring staff to leave a certain area, and which also met social distancing and sanitary regulations. Optus set up some of its India-based staff to provide support for other locations who were taking service calls.

KEY IDEAS

- Outsourcing involves taking to market those internal business processes and activities that can be done better and at lower cost when given to external vendors.
- The term 'outsourcing' is often called business process outsourcing (BPO) and captures a range of outsourced business processes including:
  - finance and accounting outsourcing (FAO)
  - knowledge process outsourcing (KPO)
  - legal process outsourcing (LPO).
- The outsourcing decision should consider several factors and can involve the use of different options.
- Numerous advantages are associated with outsourcing:
  - simplification
  - efficiency and cost savings
  - increased process capability
  - increased accountability
  - access to skill/resources lacking within the business
  - provides a capacity to focus on core competencies, thus improving in-house performance and several strategic benefits.
- The disadvantages associated with outsourcing include:
  - the cost and uncertainty associated with payback
  - issues with communication and language
  - loss of control of standards and information security
  - loss of corporate memory and costs associated with IT, organisational change, redesign and management of hierarchies.

5.5 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.5 Quick quiz on | **5.5 Exercise** | **5.5 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 6, 8, 10, 13, 14	7, 9, 11, 12, 15, 17	16

5.5 Exercise

Revision

Read the case study 'Outsourcing — for and against' and answer questions 1 to 4.

1. **What** is outsourcing?
2. **List** two advantages of outsourcing.
3. **Describe** two potential issues when a business uses outsourcing.
4. **When** is it appropriate to offshore outsourcing?

5. **State** the theory behind outsourcing.
6. **Clarify** four different outsourced business processes.
7. **Examine** table 5.2. **Distinguish** between onshore and offshore outsourcing.
8. **What** are the factors that a business must consider when assessing whether and when to use outsourcing?
9. **Detail** the four outsourcing options that may be applied.
10. Use a 'T' table to **summarise** the advantages and disadvantages of outsourcing. The 'T' table has been started for you.

Outsourcing	
Advantages	**Disadvantages**
1. Simplification: fewer activities performed within the business	2. Payback periods and costs: how long it takes to recoup costs

11. Carefully look at all the advantages and disadvantages you listed in question 10. If you were a business manager and owner, would you choose to use outsourcing or not? Provide reasons for your decision.

Read the 'Global outsourcing at Optus' case study and answer questions 12 to 15.

12. **How** does Optus make use of outsourcing?
13. **Identify** reasons for Optus's decision to outsource.
14. **List** some concerns for business when outsourcing overseas.
15. **How** did Optus respond to the difficulties presented by COVID-19?

Extension

16. Over the past few years, Qantas has outsourced a number of functions, including aircraft maintenance, information technology, and reservations and bookings, to both onshore and offshore companies. Use the internet to investigate and **assess** the possible impact of outsourcing on Qantas employees.
17. **Investigate** the use of co-sourcing and, through providing relevant business examples, state why it is increasingly popular.

5.5 Exam questions

Question 1 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q1

An accountant decides to use the services of a cleaning company for one day per week.

What is this an example of?

A. Development
B. Downsizing
C. Global contracting
D. Outsourcing

Question 2 (8 marks)

Source: HSC 2008 Business Studies Exam, Section II, Q23a & b

Edpro designs software and employs its own software programming team. It plans to outsource programming in 2009.

a. Outline ONE external change that may have led *Edpro* to decide to outsource programming. **(2 marks)**
b. Analyse the possible impact on management AND employees of outsourcing programming. **(6 marks)**

Question 3 (1 mark)

Source: HSC 2007 Business Studies Exam, Section I, Q19

Which of the following best describes *outsourcing*?

A. Leasing an asset from another business
B. Management considering stakeholders' needs
C. Purchasing support services from another business
D. Establishing a close long-term relationship between businesses

Question 4 (4 marks)

Barrack Building Supplies (BBS) is deciding whether to outsource some of its non-core activities. Discuss the use of outsourcing for BBS.

More exam questions are available in your learnON title.

5.6 Technology: leading edge, established

SYLLABUS LINK In this subtopic you will learn about leading edge and established technology as an operations strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Businesses benefit from the thoughtful application of technology. The use of technology can be an operations strategy particularly if it helps the business to create a competitive advantage. Some businesses innovate and thereby create new technology. Whether a business is leading the industry through innovation or adapting to use technology once it has already been established, technology plays a crucial part in business success.

Technology in the operations function may be classified according to whether it applies to and improves inputs, transformations processes and outputs; or whether it makes the managerial and administrative functions work more smoothly.

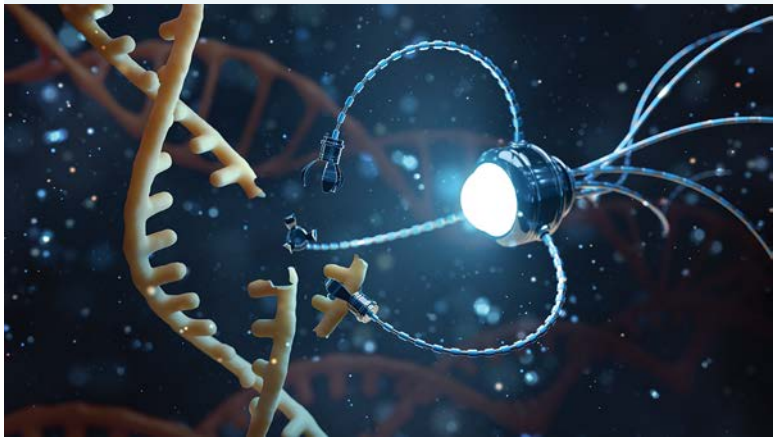
BizFACT

Bleeding edge technology refers to technology that is so new it has a greater degree of risk in terms of unreliability for those who adopt it.

5.6.1 Leading edge technology

Leading edge technology is the technology that is the most advanced or innovative at a point in time. Operations managers can distinguish their operations processes by utilising the best available leading edge technology. This can help businesses to create products more quickly and achieve higher standards, with less waste, and may also help them operate more effectively.

FIGURE 5.13 Nanotechnology is an example of leading edge technology. Nanotechnology is the manipulation of molecules and atoms at a 'nanoscale' — one nanometre is about a million times smaller than the diameter of a pinhead. This technology is expected to affect all parts of human life, including energy, food, healthcare, computers and consumer products.



Leading edge technology, in both the use of inputs and processes, has assisted in making the Australian company CSL Ltd one of the world's most innovative pharmaceutical companies. CSL has a team of over 1700 R&D experts dedicated to developing new therapies to solve unmet medical needs or enhance current treatments in immunology, haematology, and cardiovascular, metabolic, respiratory and transplant therapeutic areas. Similarly, Woolworths demonstrated considerable innovation and set the benchmark in Australia when it used leading edge technologies integrated with distribution centres.

Note that leading edge technologies are created by processes and thinking. When inventive inputs are created, new products can be made, which can change markets. Consider the current development of nanotechnology that allows for water to be purified when scooped into water bottles. This is revolutionising the cosmetics industry and has medical applications.

leading edge technology the technology that is the most advanced or innovative at any point in time

SNAPSHOT

Case study: Advice from algorithms — cutting edge technology



Leading edge technology is also called 'cutting edge' technology and refers to innovations that drive change in business. An example is the development of fintech and robo-advisors — two technologies being used by banks to help customers make financial and investment decisions. These technologies are used with smartphones or through computer-enabled access. The software development underpinning the technology uses computer algorithms to determine what investors seek and to give them various investment options based on their risk preferences, volume of investment, preferred term of investment, and so on.

By embedding options based on customer responses, the technology adapts to present choices aligned to the customer's needs. In this way, the advice can be accurate and specific, while being available 24-hours a day. This can reduce legal complications arising from financial advice given by financial advisers and can make the options far more tailored to individual customers. Over time the software will map a history of the customer's choices and thus be better able to help customers make informed choices about future investments.

5.6.2 Established technology

Established technology is technology that has already been developed and is widely used, and widely accepted. Such technologies include the use of computers and various software packages in managing business operations and functions. Established technologies are functionally sound and help to establish basic standards in productivity and speed. In the operations function, established technologies include:

- barcoding and point-of-sale (POS) data for inventory management
- robotics for complex and detailed manufacturing
- computer-aided design (CAD), computer-aided manufacturing (CAM) and computer-integrated manufacturing (CIM) for integrating transformations processes
- information processing technologies and information technologies (IT) for administration, logistics, input modelling, demand analysis and distribution
- flexible manufacturing systems (FMS) for transformations processes.

established technology technology that has been developed and is widely used and simply accepted without question

on Resources

Weblink Micromine

KEY IDEAS

- The thoughtful application of technology helps a business create a competitive advantage.
- Leading edge technology — the most advanced or innovative at any point in time — can help businesses to:
  - create more products quickly and to higher standards
  - reduce waste
  - operate more effectively.
- Established technology — that is widely accepted and used — helps to establish basic standards for productivity and speed.
- Both forms of technology give businesses efficiencies, productivity gains and a capacity to improve operations processes.

5.6 Activities

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5.6 Quick quiz on	5.6 Exercise	5.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 6, 9	5, 7, 8	10

5.6 Exercise

Revision

1. **What** is the difference between leading edge and established technology?
2. **List** two leading edge technologies and two established technologies you have seen used by businesses.
3. **Outline** two benefits of leading edge technology.

Read the 'Advice from algorithms — cutting edge technology' case study and answer questions 4 to 6.

4. **Identify** the alternative term used for leading edge technology.
5. **Explain** how fintech and robo-advisor algorithms are used by business.
6. **Outline** three benefits of robo-advisors.
7. **How** are innovation and technology related?
8. 'Businesses need to acquire leading edge technology in order to compete effectively.' **Discuss**.
9. **Recall** four forms of established technology.

Extension

10. Examine the work of Micromine, a Perth-based global provider of innovative software solutions and services for the mining and exploration industry. **Determine** the benefits to a mining or exploration business in using Micromine's cutting edge technology.

5.6 Exam questions

Question 1 (1 mark)

As a part of improving the operations process at her business, Zalina has introduced hands-free communication sets for all managers.

Which operations strategy has Zalina implemented?

A. Outsourcing
B. Technology
C. Quality management
D. Inventory management

Question 2 (4 marks)

Compare the use of leading edge and established technology as an operations strategy.

Question 3 (2 marks)

Outline the advantages and disadvantages of using established technology.

Question 4 (2 marks)

Describe the role of technology as an operations strategy.

More exam questions are available in your learnON title.

5.7 Inventory management

SYLLABUS LINK In this subtopic you will learn about inventory management as an operations strategy, including the advantages and disadvantages of holding stock, LIFO (last-in-first-out), FIFO (first-in-first-out) and JIT (just-in-time).

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Inventory or **stock** refers to the quantity of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time. Inventory management will have a significant impact on transformations processes and in operations strategies.

5.7.1 Advantages of holding stock

All businesses will carry some stock; however, the real issue is exactly how much to carry. There are several advantages associated with holding stock:

- Consumer demand can be met when stock is available. This may prevent the consumer from buying from a competitor. This is a risk reduction strategy.
- If a particular line of goods runs out, an alternative can be offered, thereby generating income for the business instead of losing sales.
- It reduces lead times between order and delivery.
- Stock give the opportunity for a business to generate immediate revenue. It is very hard to generate revenue from partially transformed inputs.
- Stock can be moved to distribution centres, which can then ensure that it is transported to customers as required.
- A reserve of stock allows the business to promote use of goods in non-traditional or even new markets.
- Older stock can be sold at reduced prices and thereby encourage cash flow and perhaps attract sales of other goods.
- Stock is an asset and is of value to the business, and if managed effectively can reflect sound financial management.
- Making goods in bulk may reduce costs as there are economies of scale in purchasing discounted inputs.

5.7.2 Disadvantages of holding stock

The trend for many businesses is to hold as little stock as possible and to adopt a 'make-to-order' approach. That is, there are many perceived disadvantages of holding inventory. These include:

- costs (see figure 5.14), including storage charges, spoilage, insurance, theft and handling expenses
- the invested capital, labour and energy cannot be used elsewhere as it has been used to create the stock
- the cost of obsolescence, which can occur if stock remains unsold for an extended period of time.

inventory or **stock** the amount of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time

LIFO (last-in-first-out) a method of pricing inventory that assumes that the last goods purchased are also the first goods sold and therefore the cost of each unit sold is the last cost recorded

FIFO (first-in-first-out) a method of pricing inventory that assumes that the first goods purchased are also the first goods sold and therefore the cost of each unit sold is the first cost recorded.

5.7.3 LIFO (last-in-first-out), FIFO (first-in-first-out)

Management in business that buys stock needs to decide what levels it should carry for greatest efficiency. At the end of the accounting period, financial management needs to determine the value of stock sold throughout the year as well as the value of remaining stock. These values assist with determining a business's gross profit. However, how does management calculate the value of the remaining stock — the inventory valuation — if the price of these goods changes during the accounting period? The main inventory valuation techniques include:

- **LIFO (last-in-first-out)**
- **FIFO (first-in-first-out)**.

FIGURE 5.14 The costs associated with holding inventory in warehouses can be as high as 30 per cent of its value.



Each of these will now be examined with reference to this example: Assume that a business buys and re-sells mobile phones. It purchases 1000 mobile phones in a batch for $100 each. Call this stock 'Batch A'. Assume half of Batch A stock is sold for $150 each. There are 500 mobile phones left in stock. A second batch, Batch B, of 1000 mobile phones is then purchased at a cost of $110 each. This takes the stock up to 1500 mobile phones. Another 900 mobile phones are sold, but this time at a price of $160. This leaves 600 phones in stock. A third batch, Batch C, of 500 phones is purchased at $120 each. The business sells 800 phones for $180 each, leaving stock of 300 phones at the end of the period.

Batch A

Purchase 1000 phones @ $100. Total cost is $100 000.

Batch B

Purchase 1000 phones @ $110. Total cost is $110 000.

Batch C

Purchase 500 phones @ $120. Total cost is $60 000.

Total sales = (500 × $150) + (900 × $160) + (800 × $180)

= $75 000 + $144 000 + 144 000 = $363 000

LIFO (last-in-first-out)

A total of 2200 items were sold. In businesses applying a LIFO approach, the business would apply cost on a last-in-first-out basis, meaning the stock bought last would assume to have been sold first. This would give the following cost:

The last group of 500 phones would be assumed to have sold first. Therefore, 500 of the phones would attract a cost of $120 each for a total cost of $60 000. The second last purchased cost would apply to the next 1000 phones sold. This gives the cost of that 1000 at $110 each, totalling $110 000. The first stock bought is assumed to have sold last, meaning the remaining 700 phones that sold would be given the first cost of $100 each for a total of $70 000.

Under this analysis, the total cost of goods sold is $60 000 + $110 000 + $70 000 = $240 000 and the unsold stock has a value of 300 units × $100 = $30 000.

BizFACT

The advantage of using LIFO is that the prices used to calculate the cost of sales, and therefore the gross profit, are more recent and therefore more closely reflect their economic value. However, in times of falling prices, LIFO overstates profits and maximises taxes.

FIFO (first-in-first-out)

A total of 2200 items were sold. In businesses that apply a FIFO approach, the business would apply cost on a first-in-first-out basis, meaning the stock bought first would assume to have been sold first. This would give the following cost:

The first group of 1000 phones would be assumed to have sold first. Therefore, 1000 of the phones would attract a cost of $100 each for a total cost of $100 000. The second purchased cost would apply to the next 1000 phones sold. This gives the cost of that 1000 at $110 each, totalling $110 000. The last stock bought is assumed to have sold last, meaning the remaining 200 phones that sold would be given the last cost of $120 each for a total of $24 000.

Under this analysis, the total cost of goods sold is $100 000 + 110 000 + $24 000 = $234 000 and the value of unsold stock 300 × $120 = $36 000.

BizFACT

In general, neither LIFO nor FIFO is necessarily better. The important point to remember is that during periods of price changes, two businesses (performing equally well in most respects) could legitimately report differing profit levels depending upon the inventory valuation method used. Because the inventory valuation method has such a powerful impact on gross profit, a business must state in the footnotes to its financial accounts which method is used.

Clearly, the method of valuation affects both the calculation of the value of the goods sold (which in turn affects gross profit) and also the value of the unsold stock. Operation managers can apply either of these methods or a weighted averaging approach as all are allowed under accounting standards. However, if LIFO is used, it may overstate cost and understate gross profit (especially when the cost of purchased goods rises over time). Moreover, it may undervalue stocks on hand at the end of the period. Alternatively, under a FIFO approach, stock costs may be understated and profits overstated. Moreover, stocks at the end of the period may be overvalued.

5.7.4 Just-in-time (JIT)

One means of managing stock is to apply a **just-in-time (JIT)** approach, which aims to overcome the problem of end-of-period stock valuation: a lean production method. This is because a JIT approach aims to have the business make only enough products to meet demand. Further, a JIT approach also allows retailers to display a wider range of products as they need to store less and can order in response to consumer demand. This, therefore, saves money as there are no expensive holding and insurance costs. Moreover, shrinkage costs and losses due to obsolescence are also minimised. However, a JIT approach requires a responsive operations function with flexible processing, an ability to respond quickly to changes in market demand and reliable supplier deliveries which must be received at the appropriate time.

just-in-time (JIT) an inventory management approach which ensures that the exact amount of material inputs will arrive only as they are needed in the operation process

Just-in-time is not an inventory valuation technique. It is a method of managing the flow and storage of stock. This means that the use of JIT is not separate from the valuation strategies — they are not alternatives. A business can use LIFO or FIFO and also be applying the JIT method of inventory management.

FIGURE 5.15 Inventory control software provides managers with precise knowledge of quantities and locations of stock, which is essential when using a just-in-time stock management system.



SNAPSHOT

Case study: A lean history

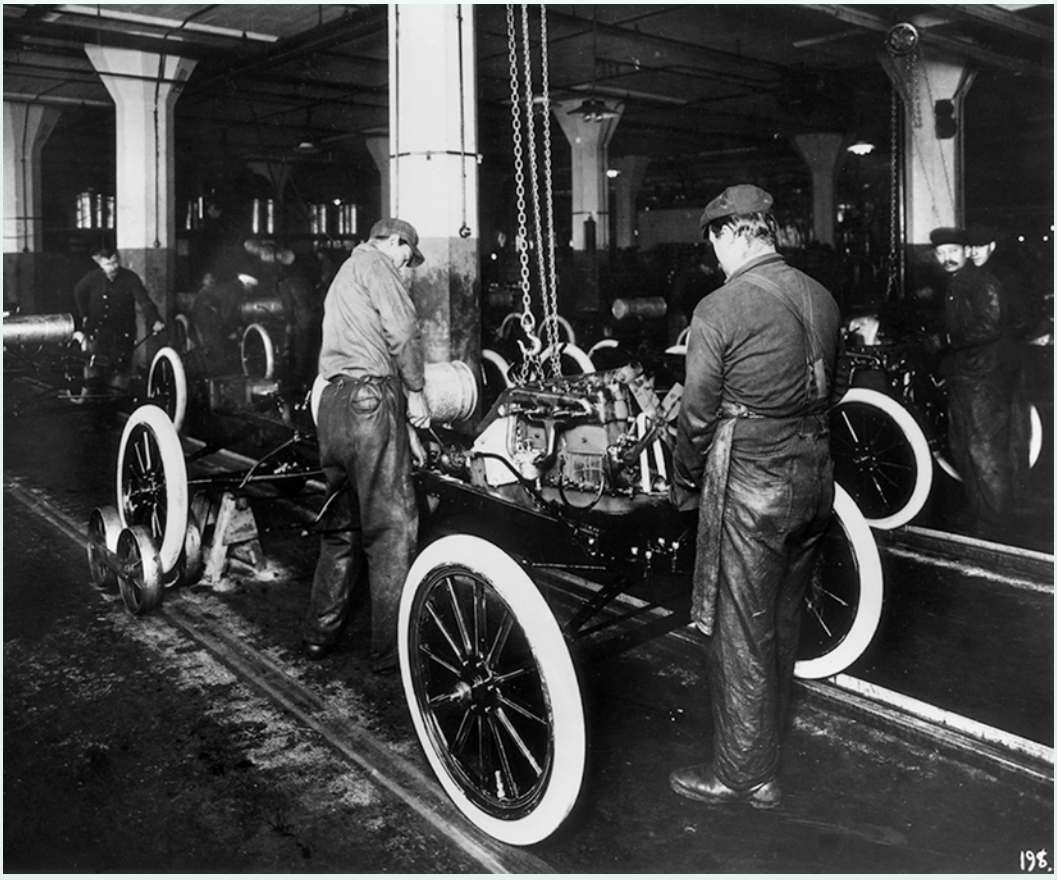
A good understanding of lean management can be gained by examining its history. Given that lean manufacturing has its origins in the automobile industry, it is necessary to consider the development of the car, which was invented in 1880.

Early in the twentieth century, mass production became an important focus for businesses. In 1910, Henry Ford developed an assembly line approach to automobile manufacturing that involved employees, components, machines and tools arranged along a production line called a conveyor belt system. This approach reduced the hours spent on the assembly of a car from 728 to just 1.5.

The assembly line approach to manufacturing emphasised efficiency. For the following 50 years it was assisted by developments in technology such as automation and computers. The United States became the largest producer of goods and services in the world, but after World War II, Japan began to compete with the Americans by developing a new manufacturing approach. This new approach arose out of necessity.

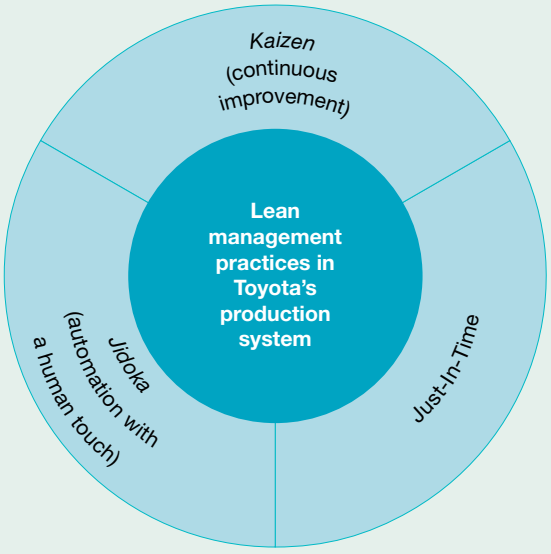
The development of lean manufacturing was based on the needs of Japan's economy. Demand was low and there was little point in focusing on economies of scale (mass production at the lowest cost per item). Toyota realised that production should be driven by actual sales of vehicles and that overproduction should be avoided. The company could not afford to have resources locked up in excess equipment or materials in production. Originally named just-in-time production (JIT), the Toyota production system was developed with the aim of minimising waste and fully utilising the capabilities of employees so that only minimal inventory was needed. Part of Toyota's philosophy of waste minimisation was the use of cellular manufacturing — efficiencies were gained through grouping machines and people into separate 'cells' that produce similar items or require a similar process of production.

Workers constructing a Model-T car on an assembly line in a Ford Motor Company factory, circa 1914



There are three main lean management practices involved in Toyota's production system:

1. *Kaizen* — a practice focused on making positive changes on a regular basis, often referred to as continuous improvement.
2. Just-in-time (JIT) — the right amounts of materials are delivered to the operations system just as they are needed for production, in the exact amount needed and where they are needed.
3. *Jidoka* — a Japanese word that means automation. However, Toyota interprets the word as meaning 'automation with a human touch'. This basically means that quality is embedded in the company's operations system. If, for example, a Toyota employee sees an abnormality such as a defect, they are able to intervene and bring production to a halt. This allows the defect to be corrected before more problems can occur, and can prevent further damage or even injury.



KEY IDEAS

- Inventory or stock refers to the amount of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time.
- Inventory management is a key operations strategy.
- There are advantages associated with holding stock, including being able to respond quickly to changes in demand and allowing development of new markets that can supply stock quickly.
- There are also disadvantages that come with carrying stock, including the costs and tying up of money that could be applied elsewhere.
- At the end of an accounting period, it is important that the value of sold and unsold stock is determined, to allow for the calculation of gross profit.
- There are alternative inventory valuation methods, including LIFO (last-in-first-out) and FIFO (first-in-first-out).
- Businesses are seeking to become 'lean', meaning they emphasise low cost.
- Lean businesses apply a just-in-time (JIT) approach to inventory management, which means to make to order.

5.7 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.7 Quick quiz on | **5.7 Exercise** | **5.7 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5, 10, 11, 13, 15	3, 6, 7, 8, 12, 14, 17	9, 16

5.7 Exercise

Revision

1. **What** is inventory management?
2. Provide an alternative name for inventory.
3. Select what you consider to be the three most important advantages of holding stock. **Justify** your selection.
4. **Summarise** three disadvantages of holding stock.
5. **What** do the acronyms LIFO and FIFO represent?
6. On 1 May Zegna Shoes orders 200 pairs of joggers at $30 apiece and sells 150 pairs for $50. Eight weeks later, Zegna Shoes orders 100 more pairs at a new price of $35 and sells 60 of these at $55. By the end of the accounting period 210 of the 300 pairs are sold. **Calculate** the total cost of sales (cost of stock), total sales and gross profit using the (i) LIFO and (ii) FIFO simplified cost analysis methods.
7. **Contrast** the use of LIFO and FIFO in terms of their effect on profitability and stock valuation.
8. **How** does the just-in-time approach to inventory management improve productivity and reduce costs?
9. **Determine** the potential problems that you can see with the just-in-time approach. Summarise your answer.

Read the case study 'A lean history' and answer questions 10 to 15.

10. **Summarise** the evolution of a lean management approach in the 19th and 20th centuries.
11. **Outline** the factors that gave rise to the use of lean manufacturing at Toyota.
12. **How** is just-in-time used in the manufacturing process at Toyota?
13. **Describe** the other lean management practices used within the Toyota production system.
14. **Explain** the relationship between lean management and quality as operations strategies.
15. Project into the role of an operations manager at Fine Cars (a hypothetical business). You are going to recommend operations strategies related to inventory and quality management based on your understanding of lean management. **List** the main talking points in your presentation.

Extension

16. Chan is the operations manager of a large clothing manufacturer. Recently the business has been in financial trouble as retail customers begin to recognise it is a very poor supplier. The clothes are rarely delivered on time, and always in the wrong quantities. The problem for Chan is that the materials for some clothing lines keep running out. Some lines won't sell and the storage areas are full of materials for those lines.
    a. **Determine** the costs of having too many materials in storage.
    b. **Predict** what problems can occur when there are not enough materials on hand.
    c. Suggest any other materials management approaches you think would help Chan to optimise the clothing operations. Justify your answer.
17. 'Management's goal is to minimise total inventory costs by balancing inventory carrying and ordering costs.' **Distinguish** between carrying costs and ordering costs. Provide examples of each in your answer.

5.7 Exam questions

Question 1 (4 marks)

Source: HSC 2020 Business Studies Exam, Section I, Q11

A manager is concerned about ongoing theft and the cost of storing raw materials.

Which inventory management strategy would best address the manager's concerns?

A. Just-in-time
B. First-in-last-out
C. Last-in-first-out
D. First-in-first-out

Question 2 (4 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q24a

A fruit shop has experienced strong growth in its sales of fresh organic fruit since it started to sell online. Discuss ONE possible method of inventory management for this business.

Question 3 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q8

Which of the following is the best method for managing the stock of fresh milk in a supermarket?

A. Just-in-time
B. First-in-last-out
C. Last-in-first-out
D. First-in-first-out

Question 4 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q7

A car assembly plant had to shut down operations for a day because tyres had not been delivered.

What inventory management strategy at the car assembly plant may have caused this situation?

A. Just-in-case
B. Just-in-time
C. First-in-first-out
D. Last-in-first-out

Question 5 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q18

A business is experiencing increasing costs for its stock over time. It is seeking to maximise its profit for the current financial period.

Which strategy should it adopt to value its inventory?

A. First-in-first-out
B. Just-in-case
C. Just-in-time
D. Last-in-first-out

More exam questions are available in your learnON title.

5.8 Quality management

SYLLABUS LINK In this subtopic you will learn about quality management as an operations strategy, including quality control, quality assurance and quality improvement.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

'Quality' is a term used to describe the degree of excellence of a product or service, and its fitness for a stated purpose. **Quality management** refers to those processes that a business undertakes to ensure consistency, reliability, safety and fitness of purpose of product. The more common contemporary approaches to quality as an operations strategy include:

- quality control — inspection, measurement and intervention
- quality assurance — application of international quality standards
- quality improvement — total quality management and continuous improvement.

5.8.1 Quality control (QC)

Quality control (QC) reduces problems and defects in the product by using inspections at various points in the production process.

FIGURE 5.16 Amazon, a world-leading online retailer, uses a quality management approach known as Six Sigma.



In the first instance, a business needs to have defined quality standards and parameters. These standards need to be broadly applied across the range of products and processes. Once the standards have been set, a range of tests needs to be designed to assess the quality of products and processes against the standards. Pre-determined quality targets would be set, and any failure to meet the targets would need to be assessed and appropriate action taken to correct any issue that has caused standards to fall below expectation. This reactive approach needs to be balanced against a more proactive approach that encourages a continuous improvement model.

Quality control management may require that labour is appropriately trained to apply quality standards throughout working processes.

quality management those processes that a business undertakes to ensure consistency, reliability, safety and fitness of purpose of product

quality control (QC) involves the use of inspections at various points in the production process to check for problems and defects

SNAPSHOT

Case study: Quality control — customer service



The salesperson was on her mobile phone when the customer arrived. The customer was looking for a pair of shoes for a job interview and was feeling a little anxious about choosing ones that would best reflect her prospective new workplace. As the customer browsed through the available shoes on display, the salesperson scrolled through her mobile phone, messaging and smiling to herself. The customer was trying to make eye contact in order to get some service. At one stage the salesperson looked up but only briefly and soon continued being distracted by her mobile phone.

The customer found a pair of shoes that were perfect for the interview. The shop, as it turned out, had a very unusual range and there were several pairs that the customer wanted to buy. However, the salesperson was still preoccupied on her mobile phone. The customer eventually walked to the counter and said, 'Hi. . . I think you have awesome stock here and I would love to buy three or four pairs of the shoes you sell. . .'

The salesperson looked up momentarily but her eyes flicked back to her mobile phone. The customer continued, 'However the quality of your service here is the worst I have ever experienced. I have watched you message and laugh while I am here with money ready and willing to buy. There is no-one else in this store to help me. The quality of the stock you sell is brilliant but I will never buy from a store with such hopeless customer service!'

Inspection and quality control

To ensure output meets required standards, many businesses carry out inspections of all or part of the total volume of production. When an inspection is conducted, the goods or services under inspection can be passed as 'okay' or 'defective'. This is an *attribute inspection*, which might answer questions such as: does an electric switch turn off and on? Does a hinge open and close? Does a water container have any leaks? In service businesses, an inspection of employee performance may be conducted. A bank may inspect teller accuracy, courtesy, speed and efficiency; and a supermarket may check operator scanning rates.

BizFACT

Yakult Australia Pty Ltd commenced local production in 1994. Its range of items includes Yakult Original and Yakult LIGHT, which are fermented milk beverages. It contains probiotic bacteria known as *Lactobacillus casei* Shirota strain, which assists people in maintaining a healthy digestive system.

Its quality management system complies with International Organisation for Standardisation's relevant Standard (ISO 9001:2015) which ensures that it meets the highest international food manufacturing standards. All company procedures are regularly audited. Further, all bottles are randomly inspected for incorrect printing and lid seals. Yakult samples are collected for sampling, quality assessment and taste in the company's onsite quality control area.

5.8.2 Quality assurance (QA)

Quality assurance (QA) involves the use of a system to ensure that set standards are achieved in production. This is done through taking a series of measurements standards. Quality assurance is a proactive approach to quality rather than a reactive one. This means that a business emphasises quality in the design of a product that provides a level of assurance to prospective buyers. Aspects of quality that are important to QA include:

- the notion of 'fitness for purpose' — how well a product does what it is designed to do
- the desire to achieve 'right first time' so that products do not need to be reworked, which wastes time, energy and other resources.

A series of quality assurance standards has been developed in response to the impact of globalisation and the international emphasis on quality. Such standards can be applied universally, which means that a component from Korea that meets the accepted international standard is theoretically of the same quality as a similar component from an Australian manufacturer. Given that different manufacturers throughout the world could produce components for a plasma television, such standards are an important quality control mechanism for 'global' companies.

A widely used international standard is the ISO 9001 series of quality certifications (see figure 5.17). 'ISO' stands for International Organization for Standardization. ISO standards are voluntary but many businesses comply with their requirements to enhance their domestic and international competitiveness.

FIGURE 5.17
Certification of the ISO 9001 Quality Management System series is easily recognised by the 'five ticks' Quality Endorsed Company Standards Mark.



SNAPSHOT

Case study: Coco & Lucas' Kitchen

Australian business Coco & Lucas' Kitchen was inspired by the need to create a range of healthy foods for children. The owners took advantage of an opportunity in the market for children aged 3 to 12 years and created a range of high-quality and well-packaged foods that have the following features:

- Gluten and lactose free
- All natural ingredients
- No preservatives
- No artificial flavours or colours
- Made in Australia
- Handmade
- 100% Aussie meat
- Truly recyclable packaging
- No GM (genetically modified) ingredients
- Frozen, fully locked-in goodness
- Contain more than 25% protein

Some of the foods made by the business include spaghetti bolognaise, cottage beef pie, honey soy chicken and penne pasta. The products are handmade from local ingredients, and are packaged in a way that makes them perfect for school lunches.

quality assurance (QA) involves the use of a system to ensure that set standards are achieved in production

The business concept was inspired by the owner's need to make food for her nephew who had lactose and gluten intolerance. Accordingly, Coco & Lucas' Kitchen created Australia's first 'junior foodies' range for children with specific food requirements.

The business focuses on using high-quality ingredients and handmade processing that is completed within Australia. Coco & Lucas' Kitchen supplies to Australian supermarkets and was recently recognised for quality and innovation at the World Food Innovation Awards, being nominated in each of the following categories:

- Best convenience food innovation
- Best children's food
- Best new brand or business (which it won)
- Best frozen food.

5.8.3 Quality improvement (QI)

Quality improvement (QI) emphasises continuous improvement and total quality management.

Continuous improvement

Continuous improvement is the belief that over time processes will be made more efficient and effective. Improvement may be a monumental breakthrough achieved through innovation all at once or it may occur gradually over time. Staff are integral to quality improvement; that is, all staff are encouraged to demonstrate initiative and to suggest areas where changes can be made. In this way, all processes can be enhanced simultaneously and 'ownership' for improvement extends to all.

continuous improvement an ongoing commitment to improving a business's goods or services

SNAPSHOT

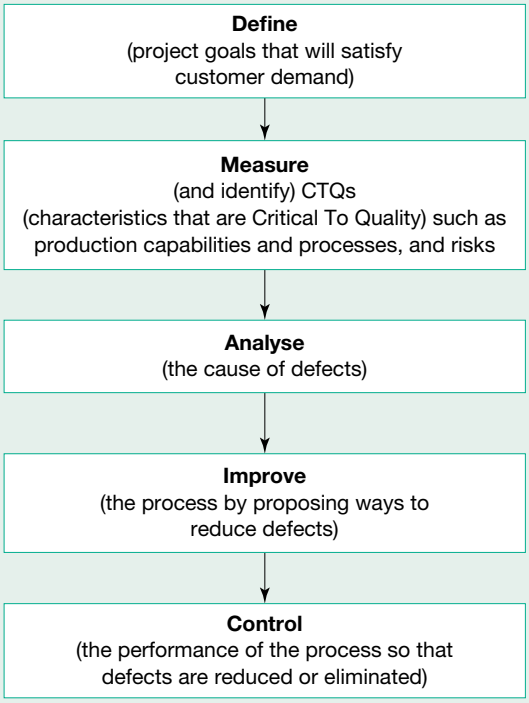
Case study: Six Sigma at Boral

Six Sigma is a measurement-based approach and methodology designed to achieve near perfection in the operations process through the elimination of defects. It was originally developed by former US telecommunications company Motorola Inc. in the mid-1980s. Six Sigma is used to identify and remove the causes of problems in the operations process, so that a business produces only 3.4 defective parts per million products. This translates to a perfection rate of 99.9997 per cent. It uses typical quality management methods, including statistical tools to measure variations in the operations process, empowerment of staff and training, a commitment to improving quality through the whole business and continuous improvement.

A special team of people within the business is established. This is composed of staff who have been given Six Sigma training, and are able to coordinate others in adopting methods to improve quality. A five-step process to problem solving applies to Six Sigma, commonly referred to as DMAIC. This is shown in the diagram at right.

Boral Limited produces and distributes construction materials and building products. With almost $5 billion worth of sales, Boral has more than 14 000 employees working across 700 operating sites. In 2007, Boral introduced Six Sigma throughout its construction materials division in Victoria, New South Wales, the ACT and Tasmania.

The Six Sigma DMAIC problem-solving process



Regional General Manager of Boral Australian Construction Materials (ACM) NSW/ACT, Tony Charnock, claimed that in its first year, Six Sigma helped the New South Wales business achieve a profit of $5 million. In 2009, Boral announced that the implementation of Six Sigma led to the construction materials division identifying $45 million of cost reduction initiatives and predicted that these would deliver three years of benefits. Boral continues to make use of Six Sigma, as well as lean management and continuous improvement.

Boral has a strong focus on continuous improvement, and Six Sigma gave it a structured way to make cost savings and improvements. Tony Charnock regarded Boral's improvement program as a never-ending process. 'Once you start making improvements, new ones keep presenting themselves. That is the experience of major companies elsewhere with Six Sigma.'

The fur seals and sea lions at the Great Southern Oceans exhibit at Taronga Zoo put on a spectacular show for up to 950 people in their new home. Boral supplied substantial quantities of concrete to the project. Boral is a company that has successfully implemented Six Sigma.



At Boral, Six Sigma training is available to staff. Staff trained as Six Sigma project leaders are known as 'black belts' and 'green belts'. Yellow-belt training provides workplace team leaders with basic problem-solving skills. For projects to succeed, staff with belts must have the support of managers ('project champions').

Boral's 'black belts' started to investigate the company's processes, looking for problems with or variations to the usual processes. This followed several months of compiling and validating data from the business. Then they came up with solutions to the problems.

One problem concerned unplanned stoppages because of products becoming trapped on conveyor systems and causing blockages. The team installed equipment, giving early warning of blockages. Maintenance and operational employees were trained in how to deal with the problem. The solution substantially cut the amount of down time caused by the unplanned stoppages.

On another project, Six Sigma's statistical analysis was applied to a problem that involved concrete being poured from trucks. By analysing variations in strengths of concrete after it was poured, changes were made to the process used in order to achieve more consistency.

John Worden, Boral ACM's Six Sigma champion in New South Wales, said, 'That is how Six Sigma works. We look for sources of variation and identify ways to eliminate them or, if that is not possible, bring them under control.'

In Six Sigma, people trained as project leaders are known as black belts and green belts. Some businesses use other belt colours as well, such as yellow belts for employees that have basic training in Six Sigma.



KEY IDEAS

- Quality management refers to those processes that a business undertakes to ensure consistency, reliability, safety and fitness of product purpose.
- The most common quality management approaches are:
  - quality controls — inspection, measurement and intervention
  - quality assurance — application of international quality standards such as the ISO 9001 series
  - quality improvements — continuous improvement and total quality management.
- A focus on continuous improvement is an ongoing commitment to improving a business's goods or services.
- Innovation, employee involvement and quality are closely aligned and indicate quality working processes.

5.8 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.8 Quick quiz on | **5.8 Exercise** | **5.8 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 6, 9, 13, 14, 15, 16, 17, 20	7, 8, 11, 12, 18, 21	10, 19, 22, 23

5.8 Exercise

Revision

1. **What** is 'quality management'?
2. **List** three different approaches to quality management.

Read the 'Quality control — customer service' case study and answer questions 3 and 4.

3. **Identify** the two distinct elements of service.
4. **What** is the link between product and quality of service?
5. **What** quality controls would a consumer make when purchasing clothing?
6. **Outline** the steps involved in the quality control approach.
7. **Why** is quality control important in the manufacture of pharmaceutical products?
8. **How** does the quality assurance system operate?

Read the 'Coco & Lucas' Kitchen' case study and answer questions 9 to 11.

9. **What** was the inspiration behind the business's range of food for children?
10. **Evaluate** the need for the type of food produced by the business.
11. **Explain** the significance of quality and innovation to the ongoing success of the business.
12. **Account** for the development of an international quality standard.
13. **Clarify** what the term ISO represents.
14. **Outline** the concept of continuous improvement.

Read the 'Six Sigma at Boral' case study and answer questions 15 to 19.

15. **What** is the Six Sigma approach to quality management?
16. **Identify** the characteristics of Six Sigma that make it a quality management approach.
17. **Describe** how Boral uses the Six Sigma approach to improve operations and in turn achieve business objectives.
18. **Explain** the role of the use of Six Sigma as a strategy to sustain a competitive advantage in operations.
19. Critics of the Six Sigma approach believe that it actually impedes business progress. **Evaluate** this assessment based upon your knowledge of the system.
20. **Recall** how continuous improvement can occur.

Extension

21. Imagine you are responsible for quality management within the school canteen. Identify which quality management approach you would adopt. **Justify** your decision.
22. **Analyse** the effectiveness of a focus on continuous improvement on work processes.
23. Use business magazines, newspapers and the internet to examine quality failures of Samsung, Volkswagen and Takata. **Create** a 300-word report on the issues faced by the chosen business. In your report, mention the impact on the business's reputation, revenue and profitability.

5.8 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q7

What is the most likely reason for an Australian clothing business choosing to manufacture locally?

A. To achieve cost leadership
B. To maintain quality control
C. To focus on other key business functions
D. To take advantage of lower overseas wages

Question 2 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q9

A business reduces product defects by using inspections in the production process.

This is an example of quality

A. control.
B. improvement.
C. innovation.
D. production.

Question 3 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q2

In which aspect of a business does continuous improvement occur?

A. Quality assurance
B. Legal compliance
C. Just-in-time management
D. Total quality management

Question 4 (1 mark)

French and Snape is a large bakery that makes and supplies cakes and pies throughout Australia. They have improved their operations processes by considering that each stage of operations has either an internal or external customer. The feedback from these customers is used to improve operations processes. Which operations strategy best describes the strategy employed at French and Snape?

A. Quality assurance
B. Quality control
C. Continuous improvement
D. Quality processes

Question 5 (6 marks)

The General Roberts Hotel has a new management team. They want the hotel's operations to be based on quality management principles. Recommend TWO quality management strategies and analyse their impact on the General Roberts Hotel.

Question 6 (3 marks)

Explain quality control as an operations strategy.

More exam questions are available in your learnON title.

5.9 Overcoming resistance to change

SYLLABUS LINK In this subtopic you will learn about overcoming resistance to change as an operations strategy, including financial costs, purchasing new equipment, redundancy payments, retraining, reorganising plant layout and inertia.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

A notable influence on operations strategy arises from the need to manage and be responsive to change. External changes are caused by legislation, the economy, society's expectations and new technology. Internal changes are brought on by staff initiative, use of available technology and innovation of goods or services.

BizFACT

Theories of human behaviour reveal that for most of us, personal change is achieved only with a great deal of effort. Over the last decade, management has realised that change also represents a serious obstacle for businesses.

When changes arise from external sources, a business must learn to adapt. This may require a significant internal realignment. Change can often be resisted as it can cause uncertainty and that can be stressful. In economic terms, uncertainty represents risk and most people are risk averse. Thus, a business needs to apply particular skills to help manage change processes.

Resistance to change arises from two principal sources within a business:

- financial
- psychological/emotional.

The most important step in overcoming resistance to change is to ensure that managers understand the main reasons why change is resisted. Once these factors have been identified, managers can put in place strategies to overcome the resistance.

BizFACT

According to change management consultant Tony McCulloch, it is essential managers ask one fundamental question when introducing changes: 'Am I giving as clear a picture as I can of the what, when, how and why of the changes?'

5.9.1 Financial costs

One major cause of a resistance to change from managers and business owners is that of financial costs, including costs associated with:

- purchasing new equipment
- redundancies
- retraining employees
- structural reorganisation of the business, including changes to plant and equipment layouts (plant layout).

Purchasing new equipment

The purchase of equipment such as machinery and technology is considered a capital cost. Such costs are usually quite high and are generally recouped through use (which adds value in transformation processes) and depreciation. Although the purchase of new equipment can be significant, there can be market advantages from

making such a capital investment and in doing so, a business may find some key operational goals are better achieved. These goals include:

- improved processing flexibility and speed, and reduced lead times
- consistency in production
- higher quality in processing
- reduced waste and loss from equipment failure.

Prior to making the investment in new equipment, it is highly likely that operations managers will assess the cost of purchase against leasing new equipment and technology. Leasing does not require a high upfront payment, but it can be more expensive as an ongoing operational cost.

Redundancy payments

Redundancy is defined as a loss of work arising from job skills that are no longer relevant to the workplace, which results in employees losing their jobs. This leaves those employees to seek jobs elsewhere in the same industry or to retrain and 'upskill' so that they have more relevant job skills in different industries. A significant cost associated with redundancies is the related payout. Typically, redundancy payouts are quite high because the value of the payout depends on factors related to the:

- length of time the employee has had with the business. Under legislation redundant workers are entitled to minimum payouts.
- worker's existing wage or salary
- amount of unused leave that the employee has accrued (including annual leave and long service leave)
- outstanding wages the employee is owed.

redundancy occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition

Redundancy costs can be substantial because the cumulative effect of the payments that must be made can be high. This is especially the case when many employees are made redundant and typically occurs when capital, in the form of machinery and technology, replaces labour in what is called 'capital–labour substitution'.

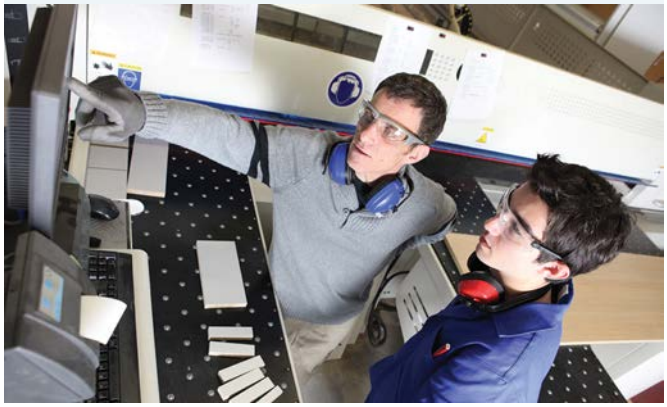
BizFACT

During 2017 the LEGO Group experienced a massive downturn in revenue arising from lower than forecast sales. The major concern for LEGO was that it had recently allocated increased investment expenditure to new factories in anticipation of increased demand. Following the unexpected downturn in sales, the business announced the loss of 1400 jobs from manufacturing plants globally.

Retraining

This cost arises from change that causes a reorganisation of the business's internal hierarchy or from the acquisition of technology. In the first instance, job roles may change, requiring employees to acquire different work skills. This can be achieved through training. In the second situation, the purchase of technology often requires training or retraining, either on or off the job.

FIGURE 5.18 To improve efficiency and productivity, the installation of new equipment may require reorganisation of the plant layout and often this will require that employees be retrained. The benefit from the introduction of new technology cannot be realised without expenditure on training and development.



Reorganising plant layout

Plant refers to the facilities where the machinery is arranged. Typically the plant layout is organised around the needs of the goods and the transformation processes required to create these goods. Major changes such as the complete re-engineering of systems often require extensive reorganisation of the layout within the facility and there can be high costs associated with reorganising the plant; for example when upgraded power generation is brought to the new plant. Additional costs are incurred in the downtime when transferring from the old to the new machinery and when testing its capacity. Further costs occur with losses in productivity, arising from staff orientating themselves with changed processes and systems.

5.9.2 Inertia

Another source of resistance to change arises from what is known as **inertia**. Inertia is a term that describes a psychological resistance to change. A feeling of uncertainty or fear of the unknown, when change is imminent or pressing, can lead people to resist. This feeling is common to most people. You may be familiar with the reaction of a parent who is in the car when their P-plate teenager is driving. The parent will often suggest a different route even if the one taken by the teenager is quicker. This is an everyday example of resistance to change. How much more resistance would be felt by people who feel like their job prospects may be threatened, who fear loss of career opportunities or who find new technology and equipment intimidating?

inertia a psychological resistance to change

KEY IDEAS

- Generally, sources of change are external and the business is responding to the threat that change can pose.
- Resistance to change can be a major obstacle to the realisation of operations goals. Overcoming the resistance to change is a necessary aspect of change management.
- There are two principal sources of resistance to change: financial and psychological (inertia).
- The financial costs of change include purchasing new equipment and technology, redundancies, retraining employees and structural reorganisation.
- Inertia can be due to a feeling of uncertainty or fear of the unknown.

5.9 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

5.9 Quick quiz on	5.9 Exercise	5.9 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5	3	6, 7, 8

5.9 Exercise

Revision

1. **What** are two sources of resistance to change?
2. Complete the following table to **summarise** the financial costs which create resistance to change. The first one has been completed for you.

Financial cost	Meaning
1. Purchasing new equipment	• Capital costs are usually quite high
2. Redundancy	
3. Retraining	
4. Reorganising plant layout	

3. Recall the kinds of resistance to change you have observed recently. **Propose** how they could have been overcome.
4. **What** is the effect of psychological uncertainty on change management processes?
5. **List** three factors that create constructive change.

Extension

6. Select a major change in your life and complete the following:
   a. **Determine** the reasons why you liked or disliked the change. Share your thoughts.
   b. Classify the reasons that were common among the group.
   c. Explain what this tells you about the strategy a manager could best use to help overcome resistance to change.
7. When the new CEO for Bradley Southport Limited attempted to make some major changes, she encountered resistance among some senior level managers. **Analyse** why these managers may have resisted the changes.
8. Assume you have been appointed managing director of an engineering business that is facing increased competition from products made overseas and needs, therefore, to improve productivity. **Create** a plan for overcoming employee resistance to the changes that are necessary to increase production.

5.9 Exam questions

Question 1 (4 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q21a

Explain why managers may be resistant to change.

Question 2 (1 mark)

Source: HSC 2010 Business Studies Exam, Section I, Q11

Which of the following is an example of a manager displaying inertia?

A. Accusing employees of disloyalty
B. Dismissing a person who requests maternity leave
C. Using inappropriate cut-off periods when recording sales
D. Continuing current practices when a new competitor emerges

Question 3 (1 mark)

Source: HSC 2009 Business Studies Exam, Section I, Q19

Which of the following reasons for resistance to change is a financial cost to a business?

A. Inertia of managers
B. Loss of career prospects
C. Re-organisation of plant layout
D. Cultural incompatibility in mergers

Question 4 (2 marks)

Source: HSC 2006 Business Studies Exam, Section II, Q24b

Home Gym Suppliers merged with Athletic Sports Company to improve profits. Explain a reason for resistance to change resulting from the merger of these two businesses.

Question 5 (2 marks)

Source: Adapted from HSC 2001 Business Studies Exam, Section II, Q21c

A business has decided to replace its labour-intensive manufacturing process with a new automated system. Discuss ONE reason for possible resistance to this change.

More exam questions are available in your learnON title.

5.10 Global factors

SYLLABUS LINK In this subtopic you will learn about global factors as an operations strategy, including global sourcing, economies of scale, scanning and learning and research and development. You will also learn to explain how any of the operations strategies can help the business to sustain its competitive advantage and recommend possible operations strategies for one hypothetical business.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Several global factors present opportunities when assessing the operations strategies in managing a business. These opportunities may be classified as:

- global sourcing
- economies of scale
- scanning and learning
- research and development (R&D).

Each of these factors facilitate a comprehensive examination of the impact of globalisation on operations strategy.

5.10.1 Global sourcing

Global sourcing is a broad term that refers to businesses purchasing supplies or services without being constrained by location. Although a key aspect of global sourcing involves procurement for the supply chain, the concept is much broader than simply a supply chain management strategy. Global sourcing as an operations strategy involves undertaking any business decision that leads to achieving cost advantages. Often, global sourcing will seek to obtain benefits that arise due to outsourcing.

Global sourcing ensures that the outsourcing decision is exposed to the global market so that the decision is made based on cost, efficiency, productivity, technical ability and an ability to operate over more hours of the day.

FIGURE 5.19 To remain competitive, businesses are forced to find ways to reduce costs of production and to improve their goods or services. One solution is global sourcing, which enables the business to find suppliers who have lower prices, higher quality products and more advanced technology.



Challenges arising with global sourcing include the relocation of aspects of operations, the increased cost of logistics, storage and distribution, managing different regulatory conditions between nations, and the increasing complexity of overall operations when sourcing from diverse locations. One of these complexities is financial and the other is contractual. Financial concerns arise from the risk associated with exchange rate fluctuations. Contractual concerns arise from language and cultural variations, and regulatory differences and misunderstanding created by poorly negotiated SLAs (service level agreements — the level of service expected by a customer from a supplier, including the metrics used to measure the service, and the remedies should service levels not be met).

5.10.2 Economies of scale

Economies of scale refers to cost advantages that can be gained by increasing the size, or scale, of production. This means that businesses can lower their per unit input costs. Economies of scale becomes a global factor when businesses respond to increases in demand and volume that necessitate making higher product volumes. Clearly, any individual nation has a limited population to sell to. When a business expands into global markets, the need to source globally becomes a strategic decision. Similarly, the need to sell to global markets becomes a decision based on scale advantages. As the scale of production increases, the costs per unit falls. This means that profitability can rise.

Economies of scale arise in several different areas of business. There are clear production advantages of producing high volumes. However economies of scale can also be derived on capital investment and the improved use of technologies. For multinational corporations (MNC), economies of scale can arise in marketing, with branding and advertising saving costs on duplication. as seen with homogenised advertising and branding in companies like Nike or McDonalds. Further economies of scale can be created in the field of human resources through the application of training and development and the range of strategies globally.

FIGURE 5.20 Assisted by improvements in communication, transport and technology, large businesses are able to achieve economics of scale, which are the savings resulting from mass production.



5.10.3 Scanning and learning

All businesses can benefit from scanning the global environment and it is an effective global operations strategy when identifying and more importantly learning from the best practice of businesses around the world. Much of contemporary business practice is influenced by the post-WWII industrial success of Japanese businesses, which emphasised quality, care and continuous improvement (**kaizen**). Management journals, industry and business associations, conferences and other forums act as opportunities for businesspeople to learn from one another. Another source of learning comes from staff members and managers who have worked in other businesses sometimes internationally. Diversity of experience helps businesses learn how to develop flexibility and insight.

SNAPSHOT

Case study: Scanning and learning — supermarket wars

Also called 'environmental scanning', the processes of scanning and learning occur when businesses watch what other businesses are doing and then adapt in order to compete more effectively. This can involve watching other businesses within the same or different industries.



Scanning and learning has been a feature of the supermarket wars in Australia. From how businesses create their supply chains through to the investment in self-scan checkout technologies, the major supermarkets are continually using environmental scanning to improve the customer experience.

When Coles invested in self-scan technology, Woolworths followed with an improved iteration. When Aldi created strong supplier relationships that threatened both Coles and Woolworths, it forced the larger supermarket chains to re-evaluate their supply chain management practices. Aldi brought its success from operating in different markets overseas to the Australian market.

In this way, scanning and learning helps to change and improve business practices.

These is some suggestion that the arrival of Amazon may have affected supermarkets but this has been largely dismissed by industry observers. Amazon's increasing popularity has had a greater effect on Australian goods retailers than on the supermarket industry. Nevertheless, all of the main supermarket retailers are increasing their investment in online selling as a defensive response to a possible threat.

kaizen Japanese for 'improvement'. It emphasises continuous improvement in all areas of a business, from the way the CEO manages to the way assembly line workers perform their jobs.

5.10.4 Research and development (R&D)

Proactive companies allocate resources to research and development (R&D). R&D helps businesses to create leading edge technologies, and to create innovative products and solutions. Government encourages R&D, and may offer taxation incentives and grants as an inducement for business to invest in R&D. Companies such as CSL Ltd and 3M spend huge amounts of money on R&D, developing innovative products to better meet the needs of consumers. A central aspect of R&D is ascertaining what consumers want and assisting to create products that meet their needs.

As an operations strategy R&D must contribute more to business decision making in Australia then it presently does.

The Australian government R&D incentive aims to provide business support through taxation concessions. Recent cuts to the funding of this scheme are cause for concern as Australia fell to 107th place globally in terms of R&D investment according to the Organisation of Economic Co-operation and Development (OECD) index. Moreover, Australia's overall investment is below that of Europe, China, the United States of America, South Korea and Japan.

BizFACT

The Research and Development Tax Incentive scheme sponsored by the Australian government has had a number of success stories including:

- Vaxxas — Needle-free delivery of vaccines through the less invasive Nanopatch
- RayGen Resources — Solar-based technology involved in the design and development of new solar power technology that is more efficient and cheaper to produce than conventional solar panels.

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KEY IDEAS

- Four key global factors affect operations strategy and provide opportunities for operations managers: global sourcing, economies of scale, scanning and listening, and research and development (R&D).
- Global sourcing is a broad reference to sourcing business supplies or services without being constrained by location and it therefore includes all outsourcing.
- Economies of scale can lead to significant cost saving in various aspects of the business enterprise.
- Scanning and listening can be a very valuable operations management tool as it can help managers adapt best practice to the business operations.
- R&D can make a very big difference to the level of innovation, quality and competitive advantage of a business.

5.10 Activities

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5.10 Quick quiz on	5.10 Exercise	5.10 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 6, 8, 9, 10	3, 4, 5, 7, 11	12 ,13 ,14

5.10 Exercise

Revision

1. **What** are four global factors that affect operations strategy and provide opportunities for operations managers?

Read the 'Scanning and learning — supermarket wars' case study and answer questions 2 to 4.

2. **Identify** an alternative term for 'scanning and learning'.
3. **How** does scanning and learning affect business practice?
4. **Investigate** the changes that have occurred in retail shops due to the introduction of scanning and learning.
5. **Why** do businesses source globally?
6. **State** the benefits and challenges associated with global sourcing.
7. **Distinguish** between financial and contractual concerns associated with global sourcing.
8. **Define** the term 'economies of scale'.
9. **What** is the relationship between economies of scale and profitability?
10. **Clarify** why an effective manager should continuously scan the business environment.
11. **Detail** the importance of R&D as an operations strategy.

Extension

12. Examine the concept of economies of scale. Contrast this with economies of scope. **Determine** why many large businesses adopt both of these operational strategies.
13. 'A global supply chain strategy reduces costs of production by creating a network of cost-effective facilities located around the globe all contributing to the final product. Its benefits outweigh its costs.' (Adzumi Saito, Operations & Logistics Manager, ZenTech Industries) **Assess** the accuracy of this statement. Make reference to how a global approach assists a business in reducing production costs.
14. **Evaluate** the importance of research and development to CSL Limited.

5.10 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q6

The main advantage of economies of scale is that a business can achieve

A. economic objectives.
B. industry benchmarks.
C. lower per unit input costs.
D. simplified supply chain management.

Question 2 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q13

In order to achieve best practice, a mobile phone company examines global trends in phone technology before designing and producing their phones. What operations strategy is this business using?

A. Standardisation
B. Global sourcing
C. Scanning and learning
D. Inventory management

Question 3 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q3

Phil goes overseas to a photographic equipment trade fair where he sees other businesses using more efficient methods of taking passport photos.

What is this an example of?

A. Process layout
B. Economies of scale
C. Scanning and learning
D. Inventory management

Question 4 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q6

A cake manufacturer buys more sugar as its production output increases. This enables it to buy the sugar at a lower price per kilogram.

What is this an example of?

A. Logistics
B. Just-in-time
C. Global sourcing
D. Economies of scale

Question 5 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q6

A global business has adopted a strategy which aims to lower the average cost of its product by increasing output.

What is this strategy called?

A. Outsourcing
B. Global pricing
C. Global sourcing
D. Economies of scale

Question 6 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q15

What is the most likely result of a business achieving economies of scale?

A. Greater flexibility
B. Higher sales price per unit
C. Greater efficiencies in production
D. Higher average costs of production

More exam questions are available in your learnON title.

5.11 Review

5.11.1 Summary

Performance objectives

- Operations strategies are based around the need to achieve performance objectives.
- Performance objectives are goals that relate to particular aspects of the transformation function and can be allocated to particular key performance indicators (KPIs) in the following areas.
  - Quality, including:
    - design: how well a good is made or a service is delivered
    - conformance: how well the good or service meets a prescribed design with a certain specification
    - service: how reliable, suitable and timely the service delivery is.
  - Speed: the time it takes for the production and the operations processes to respond to changes in market demand
  - Dependability: how consistent and reliable a business's goods or services are
  - Flexibility: how quickly operations processes can adjust to changes in the market
  - Customisation: the creation of individualised goods or services to meet the specific needs of the customers
  - Cost: the minimisation of expenses so that operations processes are conducted as cheaply as possible
- Each of the performance objectives will be allocated targets or goals.

New product or service design and development

- A business needs to design and develop new products and services.
- Two different approaches determine product design and development:
  - consumer preferences
  - changes and innovations in technology.
- Important factors in new product design and development include quality, supply chain management, output capacity and cost.
- Service design and development differs from the design and development of products as services are intangible and 'consumed' as they are produced.
- A service can be:
  - explicit — the application of time, expertise, skill and effort
  - implicit — the feeling of being looked after.

Supply chain management

- Supply chain management (SCM) involves the management and flow of supplies throughout all inputs, transformations processes and outputs.
- There are three key aspects to SCM: logistics, e-commerce (including e-procurement) and sourcing (including global sourcing).
- Logistics refers to the physical distribution and transportation of products. The use of warehouses and distribution centres is crucial to the successful management and movement of inventories.
- E-commerce enables businesses to source through online links to suppliers through business-to-business (B2B) processes and also enables customers direct access to products through business-to-consumer (B2C) processes.
- Sourcing, in the context of SCM, involves the purchasing of inputs for transformations processes.
- Global sourcing involves the use of global markets for the purchasing of any supplies; however, in the context of SCM, global sourcing refers to where and how supplies are sourced within the limitation of geography.

Outsourcing

- Outsourcing involves taking to market those internal business processes and activities that can be done better and at lower cost when given to external vendors.
- The term 'outsourcing' is often called business process outsourcing (BPO) and captures a range of outsourced business processes including:
  - finance and accounting outsourcing (FAO)
  - knowledge process outsourcing (KPO)
  - legal process outsourcing (LPO).
- The outsourcing decision should consider several factors and can involve the use of different options.
- Numerous advantages are associated with outsourcing:
  - simplification
  - efficiency and cost savings
  - increased process capability
  - increased accountability
  - access to skill/resources lacking within the business
  - provides a capacity to focus on core competencies, thus improving in-house performance and several strategic benefits.
- The disadvantages associated with outsourcing include:
  - the cost and uncertainty associated with payback
  - issues with communication and language
  - loss of control of standards and information security
  - loss of corporate memory and costs associated with IT, organisational change, redesign and management of hierarchies.

Technology: leading edge, established

- The thoughtful application of technology helps a business create a competitive advantage.
- Leading edge technology — the most advanced or innovative at any point in time — can help businesses to:
  - create more products quickly and to higher standards
  - reduce waste
  - operate more effectively.
- Established technology — that is widely accepted and used — helps to establish basic standards for productivity and speed.
- Both forms of technology give businesses efficiencies, productivity gains and a capacity to improve operations processes.

Inventory management

- Inventory or stock refers to the amount of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time.
- Inventory management is a key operations strategy.
- There are advantages associated with holding stock, including being able to respond quickly to changes in demand and allowing development of new markets that can supply stock quickly.
- There are also disadvantages that come with carrying stock, including the costs and tying up of money that could be applied elsewhere.
- At the end of an accounting period, it is important that the value of sold and unsold stock is determined to allow for the calculation of gross profit.
- There are alternative inventory valuation methods, including LIFO (last-in-first-out) and FIFO (first-in-first-out).
- Businesses are seeking to become 'lean', meaning they emphasise low cost.
- Lean businesses apply a just-in-time (JIT) approach to inventory management, which means to make to order.

Quality management

- Quality management refers to those processes that a business undertakes to ensure consistency, reliability, safety and fitness of product purpose.
- The most common quality management approaches are:
  - quality controls — inspection, measurement and intervention
  - quality assurance — application of international quality standards such as the ISO 9000 series
  - quality improvements — continuous improvement and total quality management.
- A focus on continuous improvement is an ongoing commitment to improving a business's goods or services.
- Innovation, employee involvement and quality are closely aligned and indicate quality working processes.

Overcoming resistance to change

- Generally, sources of change are external and the business is responding to the threat that change can pose.
- Resistance to change can be a major obstacle to the realisation of operations goals. Overcoming the resistance to change is a necessary aspect of change management.
- There are two principal sources of resistance to change: financial and psychological (inertia).
- The financial costs of change include purchasing new equipment and technology, redundancies, retraining employees and structural reorganisation.
- Inertia can be due to a feeling of uncertainty or fear of the unknown.

Global factors

- Four key global factors affect operations strategy and provide opportunities for operations managers: global sourcing, economies of scale, scanning and listening, and research and development (R&D).
- Global sourcing is a broad reference to sourcing business supplies or services without being constrained by location and it therefore includes all outsourcing.
- Economies of scale can lead to significant cost saving in various aspects of the business enterprise.
- Scanning and listening can be a very valuable operations management tool as it can help managers adapt best practice to the business operations.
- R&D can make a very big difference to the level of innovation, quality and competitive advantage of a business.

5.11.2 Key terms

B2B direct access from one business (the supplier) to another (the buyer), allowing the supplier to assess the needs of the buyer and meet them in a timely manner
B2C the selling of goods and services to consumers over the internet, with payment usually by credit card
continuous improvement an ongoing commitment to improving a business's goods or services
cost as a performance objective, refers to the minimisation of expenses so that operations processes are conducted as cheaply as possible
customisation refers to creation of individualised products to meet the specific needs of the customers
dependability as a performance objective, refers to how consistent and reliable a business's products are
distribution the ways of getting the goods or services to the customer
e-commerce the buying and selling of goods and services via the internet
e-procurement the use of online systems to manage supply, which allows suppliers direct access to the business's level of supplies
established technology technology that has been developed and is widely used and simply accepted without question
explicit service the tangible aspect of the service being provided, such as the application of time, expertise, skill and effort
FIFO (first-in-first-out) a method of pricing inventory that assumes that the first goods purchased are also the first goods sold and therefore the cost of each unit sold is the first cost recorded.
flexibility how quickly operations processes can adjust to changes in the market

global sourcing a broad term that refers to businesses purchasing supplies or services without being constrained by location. In the supply chain management activity, global sourcing means buying or sourcing from wherever the suppliers are that best meet the sourcing requirements.
implicit service is based on a feeling and is therefore intangible. The implicit aspects of a service are the psychological wellbeing — the feeling of being looked after — that comes with the provision of the service.
inertia a psychological resistance to change
inventory or **stock** the amount of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time
just-in-time (JIT) an inventory management approach which ensures that the exact amount of material inputs will arrive only as they are needed in the operation process
kaizen Japanese for 'improvement'. It emphasises continuous improvement in all areas of a business, from the way the CEO manages to the way assembly line workers perform their jobs.
leading edge technology the technology that is the most advanced or innovative at any point in time
LIFO (last-in-first-out) a method of pricing inventory that assumes that the last goods purchased are also the first goods sold and therefore the cost of each unit sold is the last cost recorded
logistics a term broadly referring to distribution but includes transportation (including transportation modes), the use of storage, warehousing and distribution centres, materials handling and packaging
mass customisation a process that allows a standard, mass-produced item to be personally modified to specific customer requirements
performance objectives goals that relate to particular aspects of the transformation processes
product utility the usefulness and value that a product has from the consumer's point of view
quality assurance (QA) involves the use of a system to ensure that set standards are achieved in production
quality control (QC) involves the use of inspections at various points in the production process to check for problems and defects
quality of conformance the focus on how well the product meets the standard of a prescribed design with certain specifications
quality management those processes that a business undertakes to ensure consistency, reliability, safety and fitness of purpose of product
redundancy occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition
sourcing the purchasing of inputs for the transformation process
speed refers the time it takes for the production and the operations process to respond to changes in market demand
storage involves finding a secure place to hold stock until it is required
supply chain management (SCM) involves integrating and managing the flow of supplies throughout the inputs, transformation processes (throughput and value adding) and outputs in order to best meet the needs of customers
warehousing the use of warehouses for the storage, protection and, later, distribution of stock

on Resources

Digital documents	Key terms glossary (doc-35662) Chapter crossword (doc-36213)
Interactivity	Chapter crossword (int-7155)
Exam question booklet	Chapter 5 Exam question booklet (eqb-0027)

5.11 Activities

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Exercise 1: Multiple choice questions

1. A process that allows a standard massproduced item to be personally modified to individual requirements is an example of which of the following?
   - **A.** Flexibility
   - **B.** Conformance
   - **C.** Customisation
   - **D.** Service

2. A successful restaurant could address the needs for both explicit and implicit service through which of the following?
   - **A.** The menu and the script followed by wait staff
   - **B.** Lighting and music
   - **C.** Waste management and table linen
   - **D.** Food quality and delivery time

3. E-commerce involves buying and selling goods and services via the internet. B2B refers to which of the following?
   - **A.** Business suppliers having direct access to the buyer
   - **B.** Business suppliers having direct access to other suppliers
   - **C.** Business consumers having access to businesses
   - **D.** Business suppliers having direct access to specialist sites to sell or auction to customers

4. Logistics includes which of the following?
   - **A.** Transportation
   - **B.** Use of storage, warehouse and distribution centres
   - **C.** Materials handling and packaging
   - **D.** All of the above

5. You need to send 1500 umbrellas to the MCG for a test cricket match. Each umbrella weighs 0.5 kilograms. Which of the following would be the cheapest mode of transport for this delivery?
   - **A.** Van
   - **B.** Truck
   - **C.** Train
   - **D.** Aeroplane

6. Which of the following may be a disadvantage of outsourcing?
   - **A.** Corporate memory reduction and vulnerability
   - **B.** Lost capacity to focus on core business
   - **C.** Efficiency and cost reductions
   - **D.** Simplification

7. LIFO as an inventory management tool may do which of the following?
   - **A.** Overstate cost and understate gross profit.
   - **B.** Undervalue stocks on hand at the end of the period.
   - **C.** Overvalue stocks at the end of the period.
   - **D.** A and B

8. Which of the following is a disadvantage of holding stock?
   - **A.** Product lines may run out.
   - **B.** Lead times between order and delivery are reduced.
   - **C.** Costs associated with economies of scale are reduced.
   - **D.** There is a cost of obsolescence if stock remains unsold.

9. Build-Up Construction wishes to achieve total quality management objectives. These should include which of the following?
   - **A.** Benchmarking, employee empowerment, customer focus and continuous improvement
   - **B.** Benchmarking, employee training, customer focus and continuous improvement
   - **C.** Reduction in waste, employee empowerment, customer focus, continuous improvement
   - **D.** Reduction in waste, employee training, employee empowerment, customer focus

10. Global opportunities for managers of operations strategies include which of the following?
   - **A.** Global sourcing, diseconomies of scale, scanning and learning, regulatory differences
   - **B.** Economies of scale, regulatory differences, research and development, scanning and learning
   - **C.** Greater profitability per unit, economies of scale, kaizen, scanning and learning
   - **D.** Global sourcing, economies of scale, scanning and learning, research and development

Exercise 2: Exam practice questions

Question 1 (6 marks)

a. **What** are performance objectives? **(2 marks)**

b. **Identify** TWO performance objectives and explain how they can be used to assess business performance. **(4 marks)**

Question 2 (6 marks)

Analyse the significance of supply chain management as a business operations strategy.

Question 3 (4 marks)

Discuss the use of outsourcing as an operations strategy that can assist a business in achieving a sustainable competitive advantage.

Question 4 (8 marks)

a. **What** is inventory management? **(2 marks)**

b. **Evaluate** the importance of holding stock as an operations strategy. **(6 marks)**

Question 5 (6 marks)

Examine the impact of globalisation on operations strategy.

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Topic 1 Operations review

Operations: Practice examination

Section I — Multiple choice questions (10 marks)

1. Which of the following is a list of performance objectives?
   - **A.** Quality, speed, dependability and cost
   - **B.** Quality, flexibility, customisation and profit
   - **C.** Speed, cost, flexibility and choice
   - **D.** Dependability, customisation, profit and choice
2. Which is not an important aspect of quality?
   - **A.** Control
   - **B.** Assurance
   - **C.** Process
   - **D.** Improvement
3. What is the correct order of steps in the product design and development process?
   - **A.** Market research, product design and prototype, prototype testing, product distribution and product refinement
   - **B.** Market research, product design and prototype, prototype testing and assessment, product and production processes refined, product distribution and launch
   - **C.** Market research, product refinement, prototype testing and assessment, product development, product launch and product line extension
   - **D.** Product design and prototype, prototype testing and assessment, product refinement, market research and production, distribution and specification development
4. Which is *not* a trend in supply chain management (SCM)?
   - **A.** Cost minimisation
   - **B.** Supplier rationalisation
   - **C.** Responsive supply chain processes
   - **D.** Forward vertical integration
5. Which is an essential aspect of logistics?
   - **A.** Creating a budget for new machinery
   - **B.** Materials handling and packaging
   - **C.** Checking the quality of outputs
   - **D.** Undertaking a skills audit
6. What is a cost associated with warehousing?
   - **A.** Costs of new machinery
   - **B.** The expenses associated with borrowing
   - **C.** Insurance and security of the stock held
   - **D.** The time saving in distribution
7. Which is *not* a form of outsourcing?
   - **A.** Business process outsourcing (BPO)
   - **B.** Finance and accounting outsourcing (FAO)
   - **C.** Knowledge process outsourcing (KPO)
   - **D.** Marketing processes outsourcing (MPO)
8. Which is an example of established technology?
   - **A.** Laptop computers
   - **B.** Nano particle technology
   - **C.** Bluetooth technology that can cross the globe
   - **D.** None of the above

9. What is a disadvantage of carrying stocks of unsold inventory?
   - **A.** If a particular product line runs out, an alternative can be offered thereby generating income for the business instead of a lost sale.
   - **B.** It reduces lead times between order and delivery.
   - **C.** Stocks give the opportunity for a business to generate immediate revenue. It is very hard to generate revenue from partially transformed inputs.
   - **D.** The cost of obsolescence
10. Which of the following is *not* a financial cost associated with change?
   - **A.** Redundancies
   - **B.** Inertia
   - **C.** Purchase of new equipment
   - **D.** Retraining

Section II — Short answer questions (32 marks)

1. **a.** **Define** the term 'operations'. **2 marks**
   b. **Distinguish** between inputs, transformations processes and outputs in operations processes. **6 marks**
2. **a.** **What** is meant by total quality management? **2 marks**
   b. **Distinguish** between quality control and quality assurance. **4 marks**
3. **a.** **Identify** two advantages and two disadvantages of holding stock. **2 marks**
   b. **Outline** the role of inventory management. **2 marks**
   c. **Recommend** which inventory management system is preferable for a medium-sized manufacturing business: LIFO (last-in-first-out) or FIFO (first-in-first-out). **3 marks**
4. **Analyse** three examples of ethically and socially responsible issues that may arise in operations management. **6 marks**
5. **Discuss** the factors that an operations manager needs to consider when selecting the optimum facilities design and layout. **5 marks**

Section III — Extended response questions

1. **Discuss** the balance between cost and quality in operations strategy.
2. Intense competition in the internet service provider (ISP) industry has forced WireFree Technology, a Sydney-based ISP serving the metropolitan areas of Sydney and Wollongong, to evaluate its operational management systems. Prepare a report that could be given to WireFree Technology's management team. In your report, you should:
   - **a.** **Outline** the concepts of cost leadership and product differentiation.
   - **b.** **Propose** operations management strategies WireFree Technology could implement to improve its competitive position.
3. **Evaluate** the various operations management strategies that can be implemented.
4. **Recommend** possible operations strategies for a business that you have studied.
5. **Assess** the relationship between operations and other key business functions.

Operations: Practice business report — 20 marks

Your answer will be assessed on how well you:

- demonstrate knowledge and understanding relevant to the question
- apply the hypothetical business situation
- communicate using relevant business terminology and concepts
- present a sustained, logical and cohesive response in the form of a business report.

The Wider Brim sells a range of quality headwear in Australia and overseas. Its range of headwear includes the very popular 'urban sombrero', a wide-brimmed hat that protects people from the harsh Australian sun. The Wider Brim's owners have manufactured its urban sombrero in regional NSW for 10 years however a number of customers have recently reported issues with its quality and in particular that, when wet, the urban sombrero breaks into pieces.

The urban sombrero was also the subject of a recent news report that described its production process as being environmentally unsound because it involves sourcing cotton from farms where excessive use of water has caused disruptions to local water supplies and also widespread soil erosion.

Due to a number of production issues the owners are considering whether the company should continue to produce the urban sombrero locally or engage an overseas manufacturer. If The Wider Brim continues to make its headwear locally, new production facilities and material suppliers will be required. If The Wider Brim's owners decide to produce overseas, they are concerned that quality and supply may be difficult to manage.

To address these concerns, you have been hired as a consultant by The Wider Brim to write a report to its management and owner.

In your report:

- explain why corporate social responsibility is a key concern
- evaluate the operations process used by the business
- recommend possible operations strategies.

on Resources

Digital document Sample HSC Business Report (doc-14150)

TOPIC

2 Marketing

FOCUS AREA

The focus of this topic is the main elements involved in the development and implementation of successful marketing strategies.

OUTCOMES CHECKLIST

Students should be able to:

- ☐ critically analyse the role of business in Australia and globally
- ☐ evaluate management strategies in response to changes in internal and external influences
- ☐ discuss the social and ethical responsibilities of management
- ☐ analyse business functions and processes in large and global businesses
- ☐ explain management strategies and their impact on businesses
- ☐ evaluate the effectiveness of management in the performance of businesses
- ☐ plan and conduct investigations into contemporary business issues
- ☐ organise and evaluate information for actual and hypothetical business situations
- ☐ communicate business information, issues and concepts in appropriate formats
- ☐ apply mathematical concepts appropriately in business situations.

CHAPTER SEQUENCE





SNAPSHOT

Case study: How Airbnb brought a new twist into the market



Have you heard of Airbnb? Of course you have! Not only have they revolutionised the travel industry, they've become the market leader for travel accommodation. This was achieved through the implementation of a mix of innovative marketing strategies that have all played a part in driving the company's rapid growth.

Airbnb is a booking engine that offers travellers unique accommodation around the world. Some have argued that their popularity is due to their price: Airbnbs tend to be cheaper than hotels. However, there are still many properties on the platform that are more expensive than hotels, proving that price cannot be the only factor contributing to their success.

Airbnb's strongly customer-oriented marketing is a key driver of their success. Airbnb understand what their customers want and then provide a product that matches those needs.

Airbnb have positioned themselves to stand out from the competition. By listing the properties of ordinary people, they have set themselves apart by offering travellers the opportunity to experience a destination as a local would.

Airbnb continuously update their website, which is very visual, user-friendly and personalised, to produce more relevant pages for users. They also invest in paid search, with approximately 12 per cent of their total website traffic generated from this.

Email marketing is another important part of their marketing plan. They use email marketing to communicate with existing and prospective customers to encourage new as well as repeat usage.

Social media also plays an integral role in their promotional mix. They use Facebook, Instagram and Twitter to make use of social influencers and celebrities, paying for their stay in return for some publicity.

While the COVID-19 pandemic has taken a huge toll on the travel industry, Airbnb is starting to make a comeback, due to their clever marketing tactics, with data showing bookings are already up in countries much harder hit by the virus than Australia.

online only

6 Kathmandu case study: Marketing

This case study provides detailed information on the marketing of outdoor apparel and equipment retailer Kathmandu, including case study content and exercises.

on Resources

Digital documents	Kathmandu case study: Marketing (doc-35664) Answers for case study (doc-35665)
Weblink	Kathmandu

6 Kathmandu case study: Marketing

LEARNING SEQUENCE

6.1 Role of marketing
6.2 Influences on marketing
6.3 Marketing process
6.4 Marketing strategies
6.5 Review

6.1 Role of marketing

The desire to be both a technical product and a fashion-based brand has enabled Kathmandu to broaden its market appeal. However, this also makes it more vulnerable to competition. Other businesses with a presence in Australia such as Rebel, Lorna Jane and more recently Decathlon, along with traditional competitors such as Macpac, Paddy Pallin and The North Face, also operate in the same retail space, which ensures that to survive Kathmandu must continue to evolve.

Despite the challenges posed by the current competitive retail environment, the business recently recorded an increase in sales, same-store sales growth, online sales and loyalty club members.

FIGURE 6.1 Brand distinctiveness is an important aspect of marketing.



Marketing is an important focus of the overall sustainability of retail businesses generally and Kathmandu is no different in this regard. In the most recent financial report, its chief executive officer identified the importance of a range of strategic marketing initiatives that drive the company.

These include:

- brand distinctiveness through product design and innovation
- inspiring customer engagement through its loyalty program Summit Club
- increasingly devoting resources to social media and its digital channels
- refining promotions to increase foot traffic and basket size (number of purchases per visit) during important trading periods
- making the entire range of its products available both in store and online — a so-called 'channel agnostic' approach to distribution
- developing existing stores through more effective visual merchandising, product presentation and an improved customer experience
- developing global sales opportunities.

These initiatives are designed to continue engaging customers and, when aligned with distinctive, sustainable and superior quality products, create greater brand authenticity (reliability and confidence in the company's products). This will consolidate and grow core markets as well as allowing the exploration of global marketing opportunities.

6.1.1 Interdependence of marketing with other key business functions

The use of an effective marketing approach will also require an interaction with the other key functional areas to ensure the operations function meets customer expectations through new and innovative products, cost control and automation. The finance function will need to use management strategies that ensure adequate funding for any marketing initiatives and human resources needs to foster a team-driven approach that encourages workers who embody the spirit, culture and attitude of the brand to generate innovative and competitive products.

Kathmandu employs a consumer-led marketing approach that targets specific market segments and focuses on how to maximise the return from each of these segments. This approach (where customer requirements are a priority) is reflected strongly in its desire to establish sustainable (ongoing, long-term) relationships that reward loyalty. The adventure travel focus (for example, trekking, camping and cycling) of the business can also be considered a niche that offers substantial opportunities for growth.

on Resources

Sample responses Chapter 6 Exercise questions – sample responses (sar-0181)

Weblink Kathmandu

6.2 Influences on marketing

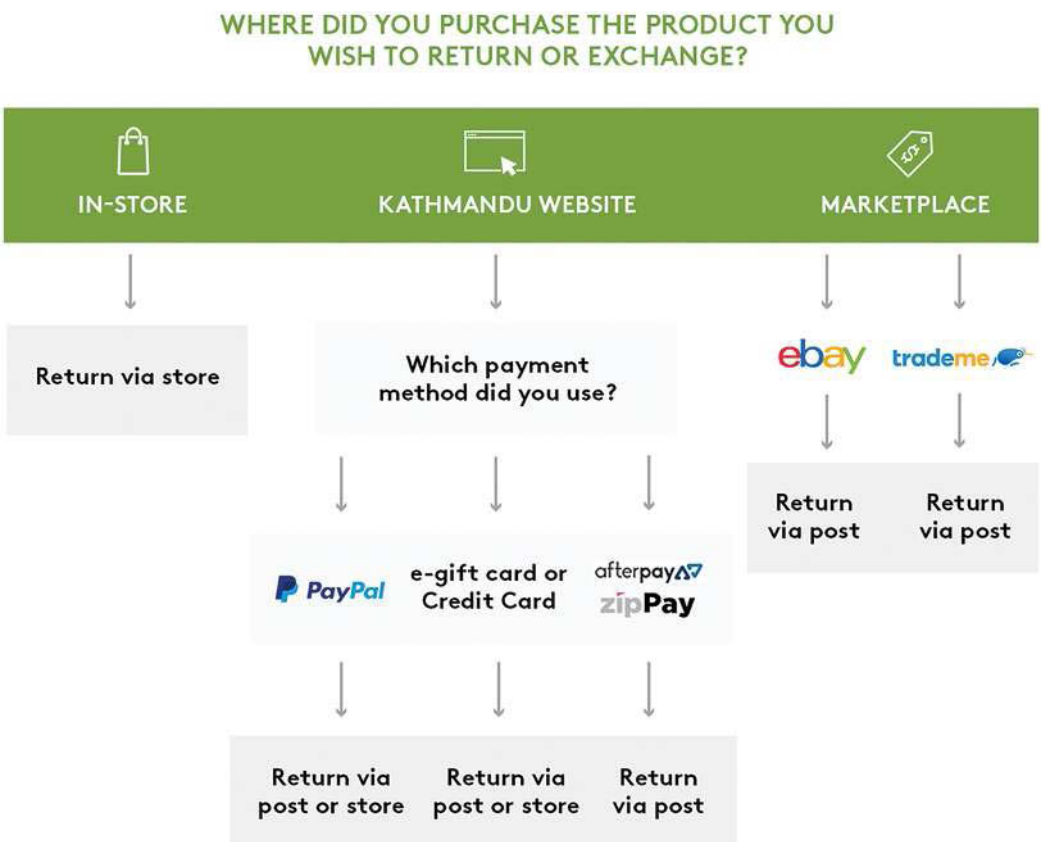
A well-developed understanding of its customers and their sociocultural characteristics (age, income, education, lifestyle) and other influences such as the prevailing economic conditions (four successive quarters of same-store sales growth despite current difficult trading conditions and when several apparel retailers have closed) have an impact on management decision-making across the business.

Kathmandu abides by the relevant federal consumer laws especially in respect to warranties. Its extensive returns and exchanges policy reflects this:

> Kathmandu provides quality outdoor gear for travel and adventure that is built to last. We believe you will be fully satisfied with your Kathmandu product.
>
> We are committed to complying with all obligations under consumer law. Any rights you have under this policy in relation to your Kathmandu product are additional to any rights you may have under consumer laws.

The process for seeking redress to assist consumers according to their purchase method is illustrated in figure 6.2.

FIGURE 6.2 Return and exchange process at Kathmandu

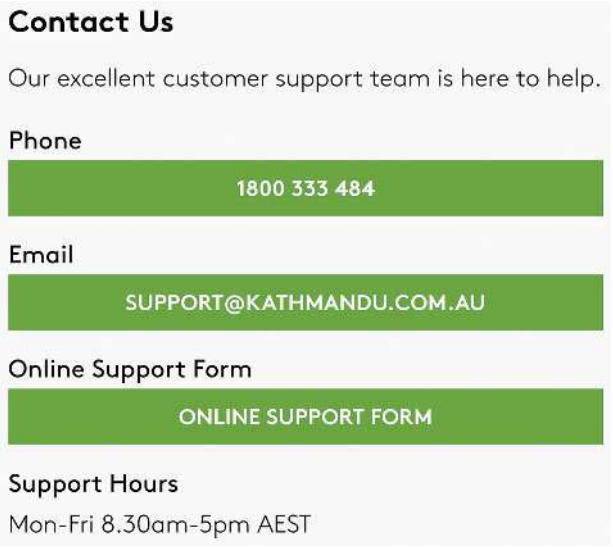


Further, the website provides a number of opportunities for customer contact to further enhance the customer experience as shown in figure 6.3.

Its ethical approach to marketing extends to truth, accuracy, good taste in advertising and ensuring its products are safe while engaging fairly with its competitors.

For example, all products must meet compliance requirements under the 2010 Australian Consumer Law (ACL) and consumer guarantees in respect to acceptable quality of goods including that they match any descriptions or samples, meet extra promises about performance and have satisfactory repair facilities available should purchased goods require it.

FIGURE 6.3 Contact details to assist Kathmandu customers



on Resources

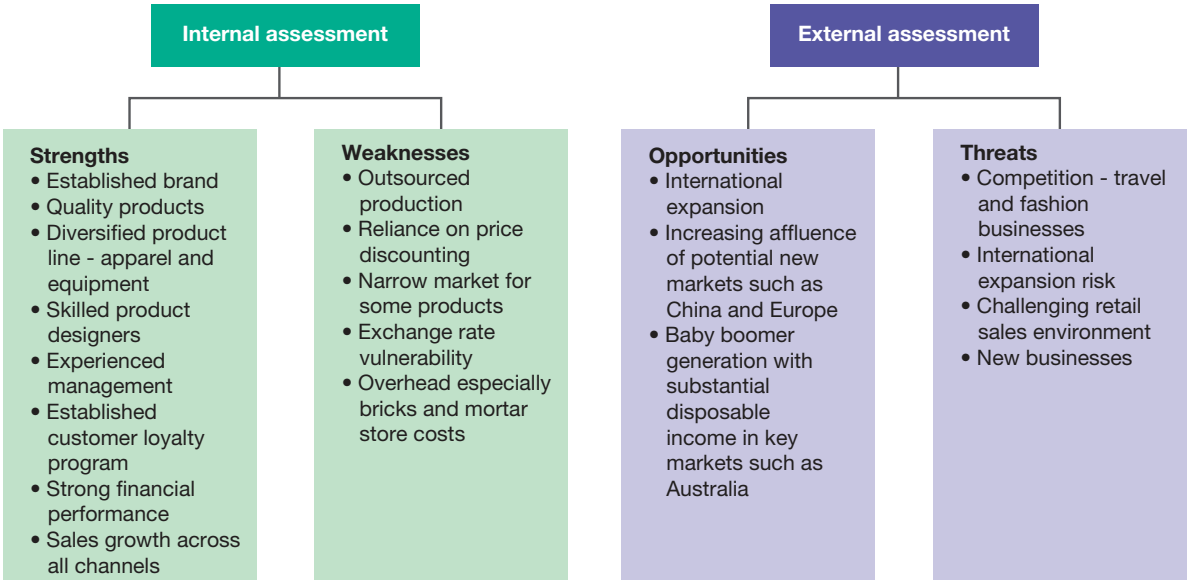
Sample responses Chapter 6 Exercise questions – sample responses (sar-0181)

Weblink Kathmandu

6.3 Marketing process

6.3.1 Situational analysis

FIGURE 6.4 SWOT analysis. Kathmandu is in the mature stage of the product lifecycle for much of its products. This phase has involved the business investing heavily in marketing strategies and adapting products to sustain its competitive advantage.



6.3.2 Market research

The market research process provides insight into customer requirements with respect to their product expectations. Kathmandu uses its loyalty program, the Summit Club, to provide metrics that can be used to both improve existing products and drive new lines. In particular the Summit Club database gives insight into:

- who is buying the active products
- when they made the purchase
- the most popular stores
- other products purchased at the same time.

This allows the marketing team to create focus groups to better understand the areas that it needs to improve. Recent insight gained from such discussions led to a new business strategy for the active range to encourage sales to young customers. This has resulted in a more contemporary range with an emphasis on trail running. Further, Kathmandu consolidated this newly acquired knowledge with a targeted sponsorship of New Zealand's most iconic adventure race and engaged known trail runners as ambassadors for the new range. Consequently, product awareness and sales in these product categories have grown.

6.3.3 Market objectives

More specific marketing objectives comprise increased brand awareness, new product development, pricing and promotion strategies, increased Summit Club membership, enhanced use of social media and digital channels, new store openings, improved in-store customer experience and global expansion. A strong environmental position that focuses on sustainable products is also a prominent feature.

6.3.4 Target markets

Kathmandu's target market is broad and is reflected in its diversity of products. Kathmandu has categorised its market into the following groups:

- young and serious (aspirational achievers)
- young and casual (fun seekers)
- middle aged and serious (experienced enthusiasts)
- middle aged and casual (family adventurers)
- older and serious (rediscovers)
- older and casual (appreciators).

The range of marketing strategies used by Kathmandu is varied and influenced by factors such as the time of year. For example, there are traditional Christmas sales in major cities like Sydney and Melbourne and it has diversified into a summer range of clothing (it is often thought of as a predominantly winter brand).

Kathmandu attempts to differentiate its products through contemporary style, functionality and quality and this has proven effective as demonstrated by growing sales. Its product differentiation is exemplified in its current range of clothing by a 5-in-1 rain jacket that has a number of layers, and removable sleeves and hood (see figure 6.5). Another example is a highly adaptable backpack (see figure 6.6).

FIGURE 6.5 Jardin Women's GORE-TEX 3 Layer Waterproof Jacket v2



- GORE-TEX® 3-layer fabric: rugged, durably waterproof and windproof
- Fully waterproof and seam-sealed with a Durable Water Repellent (DWR) finish – which encourages water to roll off the surface
- Fully windproof, breathable and abrasion resistant
- Backpack-friendly, water-resistant front check pockets
- Two-way adjustable hood with wired hood peak allows free movements even when cinched
- Hood rolls away into collar
- Fleece-lined collar and chin guard for added comfort
- Water-resistant, two-way centre-front zip with internal storm guard
- Water-resistant, two-way pit-zips for ventilation
- Articulated fit for full range of movement with adjustable hem, waist and cuffs
- Internal check pocket with cord port for media device

FIGURE 6.6 Entrada 65L Backpack v2



The 65L Entrada Backpack is an ideal lightweight pack for travellers. From the handy, detachable 15L Gluon Ora daypack to the luggage-style opening, the Entrada is designed for your overseas experience. It has a comfortable, easily adjustable harness, lockable zips and a storm flap over the main zip to protect you from the weather.

- Detachable 15L Gluon™ Ora day-pack
- Luggage-style opening
- Easily adjustable RS2 harness
- Lockable zips & storm flap over the main zip for extra weather protection
- Duffle style carry straps
- Bottle pocket & mesh pocket interior

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Sample responses Chapter 6 Exercise questions – sample responses (sar-0181)

Weblink Kathmandu

6.4 Marketing strategies

6.4.1 Product differentiation and positioning

A brand-driven approach (the consumer associates the brand with quality) has been the focus of recent marketing strategies including its most recent winter campaign. The theme of 'gear that adapts' was consistent with its overall 'adaptive gear for inspired travel and adventure' approach, which was supported by a strong narrative of how its products were highly adaptable to different landscapes, climates and individuals no matter the circumstances. It reached 2.7 million people, attracted 1.8 million views and had 35 000 website visits — easily meeting brand key performance indicators.

Its products have a heavy ecological emphasis, particularly in relation to the finite nature of resources used in the manufacturing process. For example, materials to be used in apparel are considered according to the impact their manufacturing process may have on the environment and most products are made of 'preferred fibres and materials'. This strategy has three pillars: lead (driving innovation), connection (building supplier and industry partnerships) and inform (transparency with customers), as reflected in the *2017 Sustainability Report*:

> Down is preferred because of its warmth and that it is a natural product — it is a waste product from goose farming. Often synthetic alternatives require the use of petrochemicals, however, Kathmandu recycles 33% of its synthetic insulation. This process allows manufacturing in a more environmentally safe process.

6.4.2 Importance of packaging

Packaging is also a consideration for any business in the retail space. An emphasis on visually appealing packaging at Kathmandu has taken second place behind eliminating waste, including zero-waste to landfill by 2018. Figure 6.7 shows the breakdown of in-store packaging waste.

Kathmandu has introduced biodegradable polybags that can be recycled. The Sydney and Melbourne stores have employed the plastic upcycling service RedGROUP that collects soft plastics to be reused as raw material for recycled plastic products such as outdoor furniture, bollards and decking.

FIGURE 6.7 Store waste breakdown



50 % Paper/ Cardboard

30 % Polybags and shrink wrap

10 % Co-mingled recycling

10 % Non-recycled material

GREENER, MORE EFFICIENT PACKAGING

Kathmandu produces a staggering 8 million hangtags per year. These had been produced by 120 different suppliers. This year we undertook a major overhaul of our packaging that started with an audit of all our packaging requirements. Once we had a complete picture, we could approach one supplier to take over the production. We chose Avery Dennison because they have a global network that will allow printing to be done close to garment factories and because they understand global packaging compliance requirements. Avery Dennison is also a leader in sustainability.Their Greenprint packaging audit looks at six factors — fossil material, trees, water, energy, CO2 and waste. Greenprint tools help assess the footprint of packaging options and compare them to other options. Across our vast packaging requirements, even small improvements can make a huge difference to the overall impact.

PACKAGING WINS

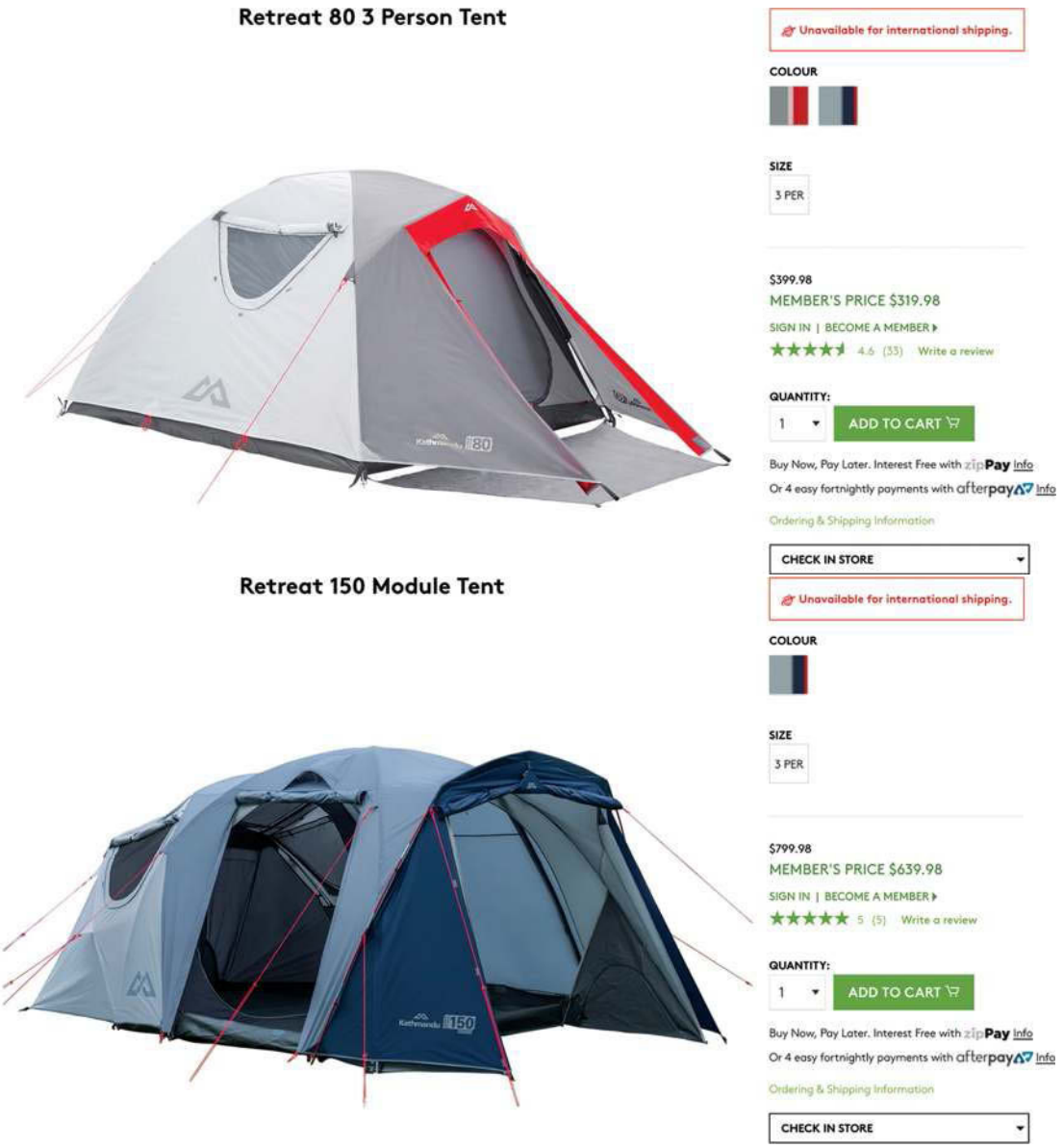
As members of the Australian Packaging Covenant, we are scored every year. The industry average is 3.2 out of 5. This year we scored 4.7 (up from 4.5 last year) and won two awards, which reflect our work on waste management and consolidating our product packaging

Kathmandu, Sustainability Report 2017, p. 49

6.4.3 Price

Pricing strategies used by Kathmandu are heavily influenced by those offered by competitors. They are also driven by a cost-based approach as reflected in the desire to establish cost-effective relationships with suppliers. It offers similar products at varying price points often with minor price differences to reflect additional qualities for those that require it. For example, in its quest to cater for all aspects of its market, the Retreat 80 three-person tent is a basic tent designed for the occasional camper, offered in contrast to the Retreat 150 Module Tent, which offers more for the seasoned camper.

FIGURE 6.8 Different price points for tents



Kathmandu emphasises a strong association between price and quality in its marketing. In practice, this is implemented in all of its products through such things as inspections of distribution centres and investigations should a customer raise quality concerns. The values of brand authenticity and distinctive, sustainable products are strongly adhered to.

6.4.4 Promotion

Promotion such as advertising on television has a role in developing product association and in turn generating increased sales, especially during traditional retail sales periods such as mid-year and after Christmas.

In an interesting decision, Kathmandu recently engaged in some product tie-in with the television show *The Amazing Race Australia*. The local version of the international reality show follows teams of two around the country as they face a range of challenges that will eventually eliminate participants so that only one team remains. (COVID-19 restrictions limited the format of the show — contestants would usually travel by various forms of transport to exotic global destinations.)

The diversity of landscapes and physical nature of many of the activities was a good fit with the outdoor, active and healthy image conveyed by Kathmandu in its promotional material. Contestants were seen wearing apparel and carrying backpacks with the company logo prominently displayed as they travelled between destinations and throughout the challenges.

Personal selling is a focus of the company and Kathmandu ensures staff have a mix of relevant skills when employing people as customer service representatives in store. This is supplemented by extensive staff training such as practical in-store programs involving group and individual selling techniques. This has led to retail store teams being more capable of identifying customer traits and being able to adjust their selling techniques accordingly.

Other examples of relationship marketing include online-only deals that are exclusive to registered customers, are offered for a limited time and do not apply in store. Promotional codes for exclusive deals can only be applied to online purchases.

6.4.5 The Summit Club

The Summit Club is perhaps the company's main method of establishing effective customer relationships. Over 1.7 million members have joined and the program is currently free for students and those aged over 60. It encourages customers who love travel and the outdoors to become members. Membership offers the opportunity to participate in local and international adventures such as Himalayan treks and community volunteer opportunities. In addition, members get discounts up to 20 per cent for all full-priced gear and 10 per cent for other gear. They also earn points with every purchase, have exclusive access to Summit Club days, VIP offers and promotions, and are supported by an online help centre.

Kathmandu uses the membership of the Summit Club as a database for the company to better align its products and marketing to its customers' needs, and it is acknowledged by management as an opportunity to better engage with customers.

6.4.6 Publicity and public relations

Kathmandu seeks to gain publicity through a number of channels. It sponsors Summit Club members who seek outdoor clothing and equipment that will assist them with an adventure or project that is consistent with the company's values. These projects include inspirational adventures, culturally engaging projects and outcome-oriented projects that contribute to environmental conservatism.

The Summit Club events seek to get customers moving outdoors. Its range of sponsored activities include:

- Run Club program — involves free weekly meet ups and provides professional trail-running coaches

- Hike Club — provides a series of events that incorporate trail running, hiking, navigation, wilderness skills and photography tips
- Workplace Giving — the company matches donations made to charities by staff
- Neverest Challenge (Australia) and Himalayan Trust New Zealand Summit Challenge (New Zealand) — participants walk or run the equivalent height of Mt Everest to raise money for the people of Nepal.

Kathmandu's *Summit* magazine is also an important way of communicating seasonal products every quarter. It charts the travels of adventurists (often opinion leaders), recommends gear and assorted travel tips as well as tracking personal journeys all aimed at the lifestyle traveller at that particular time of the year.

6.4.7 E-marketing

Kathmandu is exploring more effective ways to take advantage of social media and digital technologies, shifting to more of an e-marketing based approach. It has modelled its plan on that used by similar retailers and is mostly targeting younger age groups who are more willing to engage with such digital platforms. Early indications are positive that its strategy is working and has potential for continued success, as identified in the recent growth of online sales. Kathmandu is also keen to use its website to gauge the potential of overseas interest in its products and the opportunity for access to bigger markets and sales.

While Kathmandu has invested heavily in its in-store presence and continues to upgrade where necessary to maximise the customer experience, it has also expressed the desire to complement this with its expanded online capacity. The effects of COVID-19 meant that customers resorted to online shopping during the initial stages of the lockdown. An ongoing effort in expanding technology infrastructure meant that Kathmandu was able to quickly scale up to meet surging online demand. Most recent sales indicate a 81 per cent (retail store) to 19 per cent (online) ratio.

Inspired by its customer-centred focus and innovation, Kathmandu aligned with Uber to launch same day delivery in Sydney and Melbourne in response to COVID-19 postage delays. If a customer placed an order by 3 pm, they would receive their goods the same day.

The scheme was so successful that it was soon rolled out in other capital cities (within a 10-kilometre radius). The additional benefit for Kathmandu was that it could make use of under-utilised bricks-and-mortar stores and ease pressure on distribution centre staff as sales grew.

A longer term view is being taken of the Uber deliveries, as the potential for fewer in-store visits becomes a reality and as contactless service and online demand continue to remain popular.

6.4.8 Place and distribution

In respect to the distribution of its product Kathmandu has employed an omnichannel approach that it hopes enables it to better meet customer expectations both online and in-store. This has included an upgrade in the website's capacity to deal in multiple currencies, international shipping on many products and a click-and-collect trial in the United Kingdom. It also continues in its desire to engage with customers both in Australia and internationally through its app, ratings and reviews of products and now has a team devoted to online marketing.

Inventory management also extends to Kathmandu's Outlet store. Out-of-season stock, products with minor faults and discontinued products are offered at heavily discounted prices in locations such as factory outlet centres.

It seeks to target a somewhat selective market, driven by its understanding of the factors influencing purchases — although as previously mentioned it breaks this market down further into age and personality groups.

The other aspects of marketing strategies relate to the importance of recently recorded in-store sales growth due to improving visual merchandising and its focused and efficient sales team.

6.4.9 Global marketing

From its origins in New Zealand, Kathmandu has always had a global perspective. Its continued successful expansion into overseas markets will be based on a sound global marketing strategy. It has arranged distribution with large outdoor retail and wholesale networks in Europe and expanded online sales into China. Much of this expansion has been due to its capacity to leverage its successful brand and online presence developed in Australia and New Zealand, which has encouraged a so-called 'soft' expansion into locations where it sees market potential. Despite its strength in traditional brick-and-mortar stores, Kathmandu sees its online sales potential as its main entry into global markets and is building its IT infrastructure around a hassle-free experience for customers regardless of their location.

Products are identical in different markets with scope for differentiation at this stage of its global expansion difficult. Pricing is comparable, however, as the northern and southern hemispheres experience different seasons at any one time an in-season product here in Australia that is sold for a premium may be at the end of the season in the UK, thus requiring a discounted price to allow for new stock. This may account for slight price differences as seen in the following example. The product on the left is available on the UK site for between approximately $60–130 and in Australia the discounted member's price is $99.98.

Kathmandu has started selling its brand-name products through two overseas outdoor retailers, SportScheck, the leading outdoors retailer in Germany, and GO Outdoors in Britain.

The vertically integrated retailer has also launched a global website, kathmanduoutdoor.com to complement its Australian, New Zealand and UK e-commerce sites, and in early 2018 was setting up shop on Alibaba's TMall Global, a cross-border marketplace that enables international brands to sell directly to Chinese consumers and is seen as way of entering the competitive global travel and adventure apparel and equipment retail market in China.

FIGURE 6.9 Price differences between southern and northern hemispheres



on Resources

Sample responses Chapter 6 Exercise questions – sample responses (sar-0181)

Weblink Kathmandu

6.5 Review

6.5 Activities

learnON

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Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2	3, 4, 6, 8	5, 7

6.5 Exercise

1. **Identify** Kathmandu's main competitors in Australia.
2. **Outline** the strategic marketing initiatives used.
3. **Explain** the role of ethical behaviour and government regulation in marketing.
4. **Explain** why the equipment and apparel are central to marketing and operations at the business.
5. **Evaluate** the marketing strategies used by Kathmandu.
6. **How** is a mix of promotional marketing strategies used?
7. **Analyse** the marketing plan used.
8. **How** can global marketing be used to expand the market?

on Resources

Sample responses Chapter 6 Exercise questions – sample responses (sar-0181)

Weblink Kathmandu

7 Role of marketing

7.1 Overview

LEARNING SEQUENCE

7.1 Overview
7.2 Role of marketing
7.3 Production, selling, marketing approaches
7.4 Types of markets
7.5 Review

7.1.1 Introduction

Some Year 12 students decided they wanted to help those affected by the devastating Australian bushfires in 2020 so they approached their principal about their fundraising ideas. Once their idea was approved, they got word out via social media, morning announcements and posters around the school informing students about the dress-up day as well as explaining how the small contributions they make can help the wider community and make an impact. These students were involved in marketing, whether they realised it or not.

FIGURE 7.1 Uber created a cohesive brand that is instantly recognisable and easily adapts to the 660+ cities worldwide where Uber operates. The clean visual change from Uber's previous brand identity broke ties with their former CEO and toxic culture and helped move the company forward into a new era. This illustrates the powerful influence marketing can have on consumers' perceptions.



Meanwhile Uber introduced one of the biggest changes to their marketing **strategy**. The company decided to rebrand themselves due to the negative publicity that had been generated which was undermining their marketing efforts. While Uber's former CEO built a hugely successful business, their increasingly toxic culture tarnished the business's reputation. The old Uber logo with an all-caps and hyper-masculine appeal emphasised consumer's perceptions of this hostility. In order to persuade customers that this culture was gone when their former CEO was replaced, Uber decided on a complete redesign to overhaul the brand from the ground up. They began this by updating their logo to one that incorporates a sense of accessibility and friendliness. Uber's promotional strategies showcased how the company was using their new logo in the real world. This rebrand is an example of how marketing can influence consumers' opinions.

strategy long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

Both of these examples show that marketing is undertaken by businesses — regardless of size — with the intention of generating sales by satisfying customers' needs and wants.

Everywhere you look, you are constantly exposed to all aspects of the marketing process. For example, as you were travelling to school today, you probably didn't realise you were exposed to many different forms of marketing. But just how many advertisements do we see in a day? Back in the 1970s, it was reported that the average person saw between 500 and 1600 ads each day. Since there was no online marketing back then, most ads were found on TV, in newspapers and on billboards. A few decades later and these figures have grown exponentially. In 2020, it is estimated that the average person encounters between 6000 and 10 000 ads every single day. Like the students at the beginning of this section, you have therefore been participating in the process of marketing, whether or not you were aware of it.

BizFACT

The average consumer is exposed to an estimated 3000 advertising messages every day.

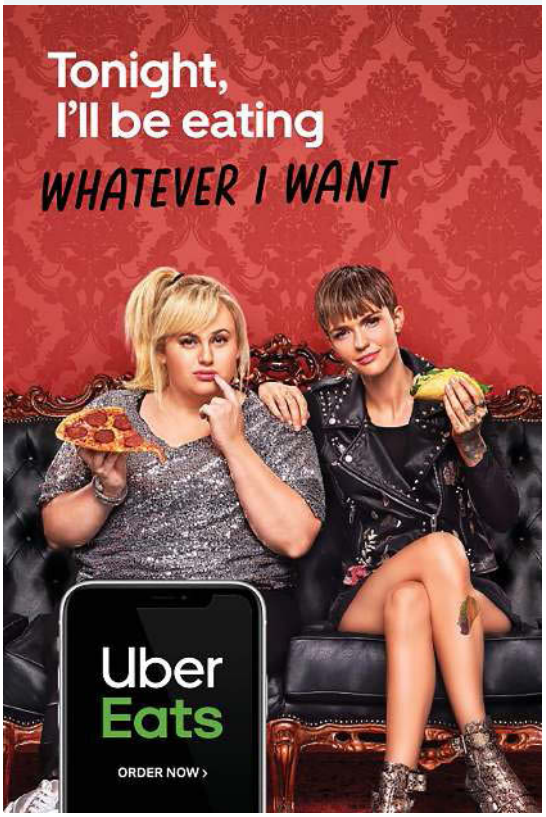
Certain aspects of the marketing process are easily identifiable, and our culture has become immersed in product promotion, especially advertising (see figure 7.2).

Marketing is vital to the existence of a business. Just because someone invents a new product or improves an existing one does not guarantee customers will buy it. Without some form of marketing, customers may not even be aware of a product's existence regardless of how 'record breaking', 'new and improved' or 'revolutionary' it may be.

Statistics reveal that more than 80 per cent of new products launched on the market fail in the first year of operation, mainly as a result of poor marketing. Businesses make few sales if they do not market their products successfully, eventually ending in failure. At the same time, many products that would seem insignificant and unimportant have become best-selling 'essential' items as a result of a well-managed and professional marketing plan. Who would have ever thought that brown, sugary, fizzy water with addictive qualities would become the global product it is today.

The following chapter will outline the strategic role of marketing, how marketing is interdependent with other key business functions, the various approaches to marketing that exist as well as the different types of markets.

FIGURE 7.2 Which current advertisement has most impressed you? What product is it advertising? You can probably answer these questions easily. This is because you have been influenced by advertising. Everywhere you look businesses are using advertising to influence consumer buying behaviour.



on Resources

Digital document Key terms glossary (doc-35573)
Exam question booklet Chapter 7 Exam question booklet (eqb-0029)

7.2 Role of marketing

SYLLABUS LINK In this subtopic you will learn about the strategic role of marketing.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

7.2.1 Introduction

There are many definitions used to describe **marketing**. The most commonly accepted definition comes from the American Marketing Association: 'Marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives.'

A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers. At the heart of these activities is the most fundamental question all businesses should continually ask: 'What do customers want to buy — now and in the future?' This is the essence of marketing — finding out what the customers want then attempting to satisfy their needs.

These definitions reveal the four main features of marketing. Marketing:

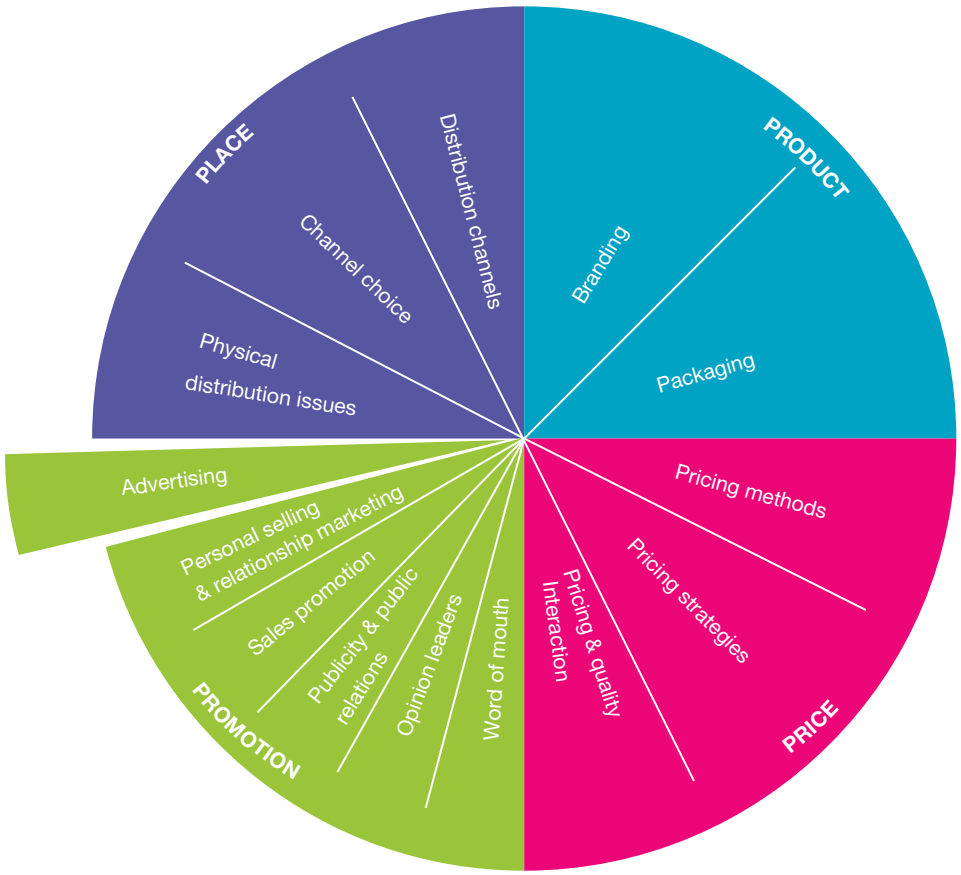
- involves a wide range of activities
- is directed at a wide range of goods, services and ideas
- stresses the importance of satisfying exchanges — that is, something in return
- is not limited to the activities of businesses.

Many people when asked which word they associate with the term 'marketing' respond with 'selling'. They think that marketing is just a fancy name for selling. However, the two words have different meanings. Selling involves a set of activities that salespeople undertake to assist the customer's buying decisions. In this sense, selling is part of the marketing process, but marketing takes a much broader view and is more involved than selling. Actually, the current view of marketing is such that it does not even have to involve the selling of a good or service — for example, not-for-profit organisations such as community activist groups and charities attempt to market certain ideas or causes.

Many people also mistakenly believe that marketing is the same as advertising. This is because advertising is highly visible and everywhere, which makes it easy to associate the two. The definitions reveal, however, marketing to be a far more multifaceted activity. As you will discover in chapter 10, advertising, though highly influential, is just one part of the promotion strategy, which in itself is one of a number of marketing strategies. While in the past businesses adopted a sales-oriented approach to marketing, the current marketing approach places the customer at the centre of all marketing activities. This current approach focuses on satisfying the consumer's needs and wants, being socially responsible and building long-term and cost-effective relationships with customers.

marketing the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives (American Marketing Association). A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.

FIGURE 7.3 A good way to distinguish between advertising and marketing is to think of marketing as a pie. Inside that pie you have four slices for each of the four marketing strategies: product, price, promotion and place. Advertising is only one piece of the promotional slice in the strategy. All of these strategies must work together toward achieving the business's objectives.



SNAPSHOT

Case study: Apple sets the benchmark in marketing



Apple's success has been a direct result of their marketing, which is why they were voted the overall winner of the CMO Survey Award for Marketing Excellence for eleven consecutive years. Their marketing has become a benchmark for other companies who aspire to reach similar heights of recognition, revenue and market share. So why is Apple a great marketer?

Apple's marketing strategies are not complex and are kept as simple as possible. Their advertisements don't include feature lists, price, information on where to buy their products, voice-overs or special effects. Instead, they are very straightforward, using simple language and graphics to translate their message. Apple doesn't overwhelm customers with jargon, choices and options, their products are sleek and minimal and their product names are short and easy to remember. Apple studies their customers and speaks to them in their own language.

One of Apple's best marketing tactics is their ability to create mystery around new product launches. They withhold information, leak rumours and keep what they are doing under wraps, which generates even more excitement and mystique until the big unveiling. Their 'fanboys' and 'fangirls' camp out for days on end to be

the first in line for their latest product. Apple has built one of the most hardcore fan bases of any brand and of any time. They created a brand personality and culture that inspires devotion among millions of customers around the world.

Apple has created this loyal following because they have been able to reach their customers at an emotional level. Their advertisements show happy people having a great time with their products rather than focusing on product details and features. They create advertisements that make their customers believe their products will make their life better, easier, more fun and cooler.

Another effective marketing strategy Apple pursues is product placement. Since the mid-1990s, Apple products have been featured in hundreds of movies and TV shows each year. One of the best examples of product integration was in the *Modern Family* episode 'Connection Lost' where the entire episode is told through Claire Dunphy's Macbook Pro as well as the other apps she uses to communicate with her family such as FaceTime, Messaging, iTunes, iPhoto and iCloud. The result is an episode that's incredibly funny and effective without ever actually seeming like an ad.

Apple engineers their products to be so unique that people view their product name to be the product itself; for example, people don't buy a tablet, they buy an iPad. Very few brands have become so ingrained in the vocabulary that they're synonymous with the products themselves. These are only some of the marketing strategies that have turned the company from near bankruptcy to an industry leader.

7.2.2 Strategic role of marketing goods and services

As outlined previously, each of the key business functions has a **strategic** component. Generally, the overarching goal of business is **profit maximisation**. Therefore, the strategic role of marketing is to develop a combination of strategies that can be used to maximise sales, increase brand awareness and improve customer satisfaction so that the business can translate this goal of profit maximisation into reality. For example, through its sophisticated marketing plan, Coca-Cola has built on its highly recognisable brand name. In its first year, about 10 servings of Coke were sold per day. Today, Coca-Cola is sold in over 200 countries with 1.9 billion servings consumed every day. Marketing is therefore a powerful strategy available to help achieve a business's goals.

strategic refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

profit maximisation occurs when there is maximum difference between the total revenue coming into the business and total costs being paid out

marketing plan a document that lists activities aimed at achieving particular marketing outcomes in relation to goods or services. The plan provides a template for future action aimed at reaching business goals, such as profit maximisation.

Without a marketing strategy, financial disaster is inevitable. Many new inventions become commercial failures because they have not been marketed adequately. To develop customer awareness and demand, and thus form a customer base, an organised marketing campaign is necessary, starting with the development of a marketing plan.

When new products are developed, often the business can become too product focused. If businesses want to achieve their financial goal of making a profit, their product needs to generate sales. This requires them to develop a **marketing plan** detailing the strategies they will need to put into place to sell their products.

To achieve the goal of profit maximisation, the marketing plan should be the focus of both short-term and long-term planning for three reasons:

1. The marketing plan outlines the strategies to be used to bring the buyer and seller together. The business needs to be able to identify:
   - where the market is
   - who will buy the product
   - why they will buy the product
   - how often they will buy the product.
2. The core of marketing is satisfying existing customer wants, which should lead to repeat sales.
3. Marketing is the revenue-generating activity of any business. Nothing is achieved until a sale is made.

A successful business develops a marketing plan based on careful research and design. The customer should always be the central focus of the marketing plan. Any business that does not develop and maintain a customer base soon goes out of business. It is the role of the marketing plan to make sure a customer base is created and maintained.

The marketing plan, therefore, plays a crucial strategic role in the overall success of the business. If the business plan is the 'road map', then the marketing plan contains the signposts showing which direction to take (see figure 7.4).

FIGURE 7.4 The strategic role of marketing is to increase sales and market share, which should hopefully lead to greater profitability.



7.2.3 Interdependence with other key business functions

Interdependence refers to the mutual dependence that the key business functions have on one another. Marketing therefore does not occur in isolation, but relies on the other functions for its success.

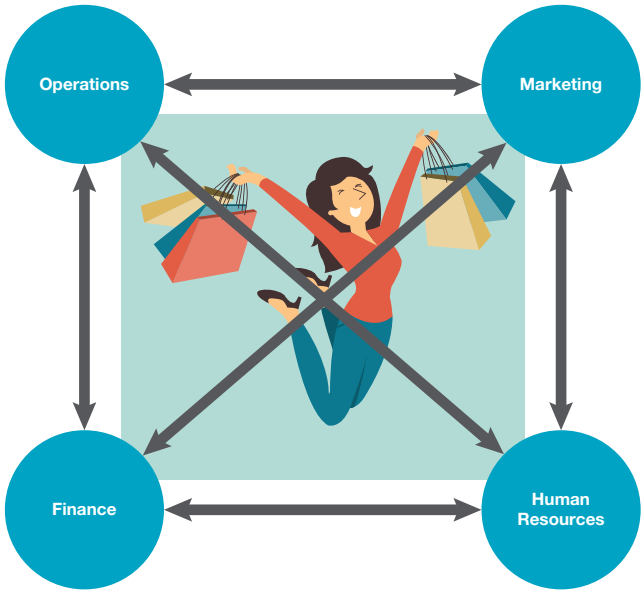
During the 1950s, businesses began to slowly accept that they were not solely producers or sellers, but in the business of satisfying customers' wants. This shift in focus to a customer-oriented approach brought about significant changes to marketing, especially the need to undertake market research and develop a marketing concept.

The **marketing concept** is a philosophy that states all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals. The business should direct all its policies, plans and operations towards achieving customer satisfaction. The marketing plan, therefore, needs to become integrated into all aspects of the business (see figure 7.5), with marketing strategies playing a major role in all business activities.

interdependence the mutual dependence that the key business functions have on one another

marketing concept a business philosophy that states that all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals

FIGURE 7.5 At every level of the business, employees should have as their primary focus the satisfaction of the customer. This requires the integration of the marketing plan in the four key business functions — operations, finance, human resources and marketing — in order to achieve the business's main goal of profit maximisation.



To be effective, therefore, the marketing concept must be embraced by all employees of the business, not only by those involved in marketing activities.

The marketing manager cannot work in isolation and often has to work with other managers in the business to ensure the success of the marketing plan. For example, if the success of the marketing plan means having a good or service ready by a certain date, the operations plan will need to be in place to make sure that happens. If, for example, a business makes Christmas puddings, it is no good delivering the puddings after 25 December! Financial planning must also 'connect' with the marketing plan. It is important to remember that marketing costs money; and finances must be available if, for example, the business wishes to embark on an expensive advertising campaign. The marketing manager will also have to work with the human resource manager to ensure that the right staff are employed to create the good or service that is desirable to customers.

on Resources

Weblinks PepsiCo
Coca-Cola

KEY IDEAS

- Marketing is undertaken by businesses with the intention of generating sales by satisfying customers' needs and wants.
- As consumers, we are constantly exposed to all aspects of the marketing process.
- Statistics reveal that more than 80 per cent of new products launched on the market fail in the first year of operation, mainly as a result of poor marketing.
- Marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives.
- A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.
- Marketing is a multifaceted activity involving much more than merely selling or advertising.
- The strategic role of marketing is to implement strategies to maximise sales, increase brand awareness and improve customer satisfaction so that the business can translate this goal into reality.

- Marketing today places a strong emphasis on viewing the business through the customers' eyes, or customer-oriented marketing.
- To develop customer awareness and demand, and thus form a customer base, an organised marketing campaign is necessary, starting with the development of a marketing plan.
- The marketing plan is a document that lists activities aimed at achieving particular marketing outcomes in relation to a good or service.
- Marketing does not occur in isolation; it is interdependent with the other key business functions.
- The marketing concept is a philosophy that states all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals.
- The marketing plan needs to become integrated into all aspects of the business, with marketing strategies playing a major role in all business activities.

7.2 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

7.2 Quick quiz on	7.2 Exercise	7.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 8, 10, 14, 17	6, 7, 9, 11, 12, 13, 15, 16, 21	18, 19, 20

7.2 Exercise

Revision

1. **Recall** the intention of the marketing undertaken by the Year 12 students and Coca-Cola.
2. **Identify** three marketing strategies that may have influenced you to purchase a good or service.
3. **Clarify** what the main reason is for approximately 80 per cent of all new products failing shortly after their launch.
4. **Define** the term 'marketing'.
5. **State** the four main features of marketing.
6. **Distinguish** between 'selling', 'advertising' and 'marketing'.
7. **How** has the definition of marketing provided in this chapter been different to your previous understanding of the term?
8. **Identify** a common financial business goal.
9. **Explain** the role marketing plays in achieving this goal.
10. **State** the main role of the marketing plan.
11. 'Businesses that neglect the importance of marketing will experience diminished sales and reduced profits.' **Discuss**.
12. 'The marketing manager cannot work in isolation and often has to work with other managers in the business to ensure the success of the marketing plan.' **Discuss**.
13. **Demonstrate** how marketing is interdependent with one other key business function.

Read the Airbnb case study in the topic 2 opener and answer questions 14 to 16.

14. **Summarise** the main marketing strategies used by Airbnb.
15. **How** does Airbnb demonstrate a customer-oriented approach to marketing?
16. **How** have Airbnb positioned themselves in the accommodation market?

Read the 'Apple sets the benchmark in marketing' case study and answer questions 17 and 18.

17. **Describe** the role of marketing at Apple.
18. **Evaluate** the effectiveness of three of Apple's most successful marketing strategies.

Extension

19. Use the library and the internet to examine and **create** a 300-word report on the marketing of PepsiCo. Mention similarities and differences between the marketing of PepsiCo and that of its main rival, Coca-Cola.
20. 'Selling is merely getting rid of existing stock, whereas marketing takes a much broader view. Successful marketing involves bringing the buyer and seller together and making a sale.' **Assess** the accuracy of this statement.
21. **Investigate** how the role of marketing has changed over time.

7.2 Exam questions

Question 1 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q8

A business plans to increase its stock to be ready for the grand opening of five new stores. This shows the interdependence between which business functions?

A. Operations and finance
B. Operations and marketing
C. Finance and human resources
D. Human resources and marketing

Question 2 (6 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q23c

XYZ Ltd produces sports shoes which are worn by elite athletes and the general public in North America. XYZ Ltd is keen to expand into Europe and Asia. The management team of XYZ Ltd is deciding whether to use customisation or standardisation as its marketing strategy for the expansion.

Analyse how marketing and finance would be linked in XYZ Ltd's decision to customise or standardise.

Question 3 (1 mark)

The CEO of a large business has called a meeting with the senior management of the marketing team to develop a global marketing plan as a part of the business's expansion strategies. Which of the following best describes the role of marketing in this business's goals?

A. Tactical
B. Operational
C. Financial
D. Strategic

Question 4 (1 mark)

Which of the following activities is the responsibility of the marketing team?

A. Setting budgets for sales teams
B. After-sales service
C. Inventory control
D. Building prototypes

Question 5 (3 marks)

Explain how marketing affects operations in a business.

More exam questions are available in your learnON title.

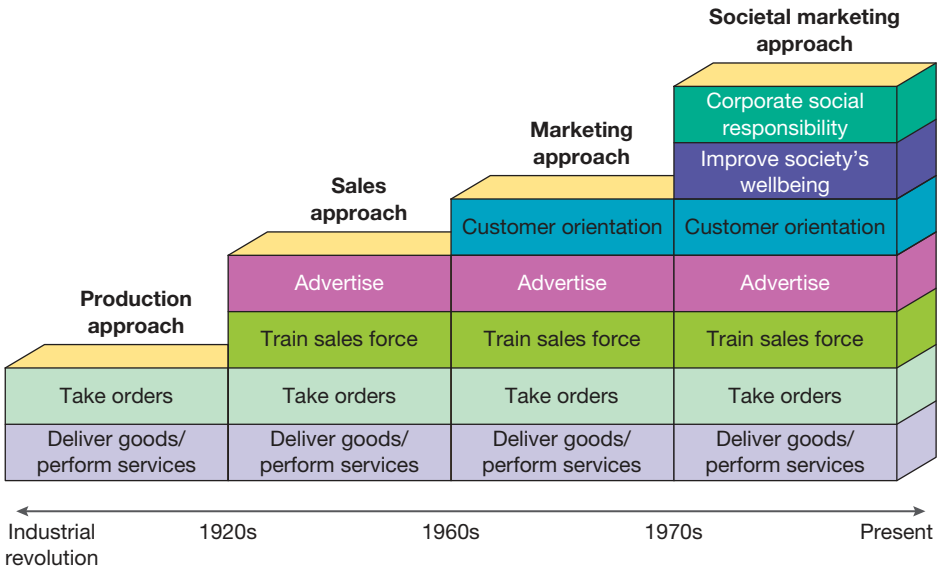
7.3 Production, selling, marketing approaches

SYLLABUS LINK In this subtopic you will learn about production, selling and marketing approaches.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The focus of businesses today is to develop a marketing plan based on the marketing concept — that is, an emphasis placed on customer satisfaction. However, marketing did not always have this as its main aim. As figure 7.6 shows, the focus of marketing strategies has changed dramatically over the years.

FIGURE 7.6 The evolution of marketing. Marketing has changed dramatically, evolving from the old-fashioned concept of simply producing goods and performing services and making them available for customers, to today's highly sophisticated and competitive marketing strategies, which involve aggressively seeking specific markets and customer needs to fill.



The idea of the marketing concept evolved in the early 1960s. Prior to this, there were two different approaches to marketing: production and sales.

7.3.1 The production approach — 1820s to 1920s

The **production approach** focused businesses on the production of goods and services. Consequently, until the 1920s, most businesses considered marketing simply as a spin-off of production. The attitude towards marketing is best explained by a catchphrase common during this time: 'If we make it, they will buy it'.

The Industrial Revolution created a tremendous burst of industrial output, which saw demand for goods (and some services) exceed the production capabilities of many businesses. Up until World War I, businesses concentrated their efforts on the production of goods and services. Businesses were usually able to sell all their output. Production design was based more on the demands of mass production techniques than on customer needs and wants. Business was production-oriented. Henry Ford, for example, focused on ways to produce motor vehicles more quickly and cheaply, confident that the people would buy them. Marketing consisted of simply taking orders and delivering the products.

production approach a marketing approach that focuses on the production of goods and services

FIGURE 7.7 Henry Ford is quoted as saying 'If I had asked people what they wanted, they would have said faster horses.' According to legend, Henry Ford ignored customer needs and instead manufactured innovation based solely on his vision for a better future.



7.3.2 The selling approach — 1920s to 1960s

After World War I, production became more efficient and productivity increased. Slowly the output of businesses started to catch up with demand. High-quality, mass-produced products came on to the market, and competition between businesses increased. No longer could a business rely on selling all it produced. Because customers' basic needs were satisfied, businesses had to develop a new marketing approach — one that was sales-oriented in an attempt to beat the competition and gain new customers.

The **sales approach** emphasised selling because of increased competition. To stimulate demand for their goods and services, businesses increased their spending on advertising, making use of newly developed electronic communications systems such as radio and film. Businesses faced the challenge of persuading customers to buy a specific brand. Sales representatives were hired and trained. Salespeople personally reached thousands of people and, in some instances, used high-pressure tactics to convince consumers to buy products. However, marketing still continued to play a secondary role to other functional areas such as production and finance.

Even though marketing was becoming more refined, most businesses were still neglecting the needs of the customer. Instead of researching what the customer wanted, they were producing what the company could make and getting their sales representatives to create demand. It was not until about the 1960s that businesses started to consider the customers' needs.

sales approach a marketing approach that emphasises selling because of increased competition

FIGURE 7.8 A sales-oriented business isn't concerned with the wants and needs of its target market; their logic is that making a superior product or service at the right price, combined with aggressive sales tactics, will enable them to persuade people to buy whatever they're selling. Car dealerships are based on a sales orientation approach because they are generally known to use aggressive sales tactics and promotions to persuade customers to buy their car instead of that of a competitor.



BizFACT

Throughout the sales approach era, the manager of the marketing department was usually given the title of sales manager.

7.3.3 The marketing approach — 1960s to present

The marketing approach began with the economic boom after World War II, as businesses began to practise marketing in its current form. The method of achieving business success changed from focusing on production or pushing goods and services on customers, to placing the customer at the centre of all marketing activities. The **marketing approach** focuses on finding out what customers want — through market research — and then satisfying that need.

marketing approach focuses on finding out what customers want — through market research — and then satisfying that need

For the first time, most Australian families had **discretionary income**, more income than what was needed to obtain the necessities of life. They used this extra income to satisfy their needs and wants with different kinds of goods and services. For example, consumers started spending more on travel and recreation. Producers now had to learn how to satisfy wants as well as needs; something else was needed if products were to sell as well as previously. The emphasis shifted to the development of a marketing concept.

The marketing concept is based on the following principles. It must be:

- customer-oriented
- aimed at satisfying customers
- integrated into the business plan so as to achieve the business's goals
- aimed to develop long-term relationships with customers.

As a result, the marketing approach is characterised by the importance placed on identifying and satisfying customer needs and wants *prior* to producing the goods or services — the motivation being that the business would produce what the customer desired, and the customer would then buy the good or service. Marketing now became central to all aspects of a business, and satisfying customer needs became the responsibility of all employees, regardless of whether employees were financial controllers, operations specialists, human resource officers or sales representatives/consultants.

FIGURE 7.9 For many years, Nike adopted a production-oriented approach to marketing and believed the way ahead was through product innovation. In the mid-1980s when competition intensified, Nike realised that the only way forward was to put the consumer in the spotlight as they are the ones who should drive innovation. They therefore changed their approach to first finding out exactly what customers want and then innovating and creating products to meet those needs.



If you purchased a digital television today, there is a one-in-three chance it was made in South Korea and a 25 per cent chance it was made by Samsung. The secret to Samsung's phenomenal success is that it is a business with a strong **customer orientation**: collecting information from customers and basing marketing decisions and practices on customers' wants and interests (see figure 7.9).

As mentioned previously, a key principle of the marketing approach is customer orientation. For businesses that adopt a customer-orientation approach, the customer relationship does not end with the sale; it begins there. Companies such as Samsung will strive continuously to not only simply meet but also exceed customer expectations. Samsung, similar to many other businesses, constantly strives towards achieving and maintaining high levels of **customer satisfaction**.

A customer-oriented business will want to create goods and services that customers want to buy. Everything they do will be directed towards putting the customer at the centre of their thinking. Since customers are the lifeblood of any business, they must be encouraged to stay loyal to the business. This means that, at every level of the business, all employees will work towards customer satisfaction by establishing positive relationships with customers.

discretionary income disposable income that is available for spending and saving after an individual has purchased the basic necessities of food, clothing and shelter

customer orientation the process of collecting information from customers and basing marketing decisions and practices on customers' wants and interests

customer satisfaction measures how goods and services supplied by a business meet or exceed customer expectation

SNAPSHOT

Case study: Slack's customer orientation and marketing approach



Have you ever accidentally written a reply-all email to dozens of people? Have you ever forgotten to attach a file? Have you ever been overwhelmed by the number of emails you receive each day? Messaging service, Slack, was created to address these common complaints made by people regarding emails. It was created to make people's lives easier and was developed based on customer feedback and concerns.

Slack has changed the way teams and businesses communicate with its app for centralising communications and information. The company began in 2013 and is today worth over $20 billion and has more than 8 million daily users. The success of the app can be attributed to the fact that it was built with obsessive attention paid to customer feedback.

Slack demonstrates extreme customer centricity by understanding what customers want and need. Today's workforce is increasingly mobile and want more flexibility. Slack responded to this change by designing a product to meet society's needs and make communication easier. Slack is easy to use and is also very quick — much quicker than sending an email.

Slack has incorporated customer feedback from day one. In fact, many of the app's greatest features have come from customers' opinions. Prior to releasing the first version, the company listened to customers and tested their app for seven months. They then released the app to just ten companies. As soon as users told them something wasn't working, they immediately fixed it. The company then progressively shared Slack with larger groups, received even more feedback and made even more modifications.

Slack is therefore focused on continuous improvement and they use real-time data and feedback to achieve this aim. This emphasises how Slack puts customers at the heart of their strategy, basing every update on feedback and consumer needs.

Slack aims to build long-term relationships with their users. Their customer support teams make themselves available for all kinds of feedback. The effectiveness of these teams is measured by their ability to respond to enquiries in a human way, rather than based on the number of issues resolved. This is done so that people don't feel like a number on a queue, but rather a valued customer. Their marketing is personal and engaging and helps build a connection between customers and the brand.

Slack approaches everything they do with a customer-oriented mindset and their primary consideration is what is best for customers. Their goal has never been about profits, but rather about improving the lives of customers. As opposed to financial or sales figures, Slack analyses customer-facing indicators like daily active users and Net Promoter Score (NPS), which measures the loyalty of customers to a company. This assists the company to get an idea of how customers perceive the brand. Their goal is to create loyal, satisfied customers who will then recommend the app to others. Instead of short-term financial objectives, their focus is on long-term customer satisfaction. A great product can only go so far. Slack is proof that businesses that focus on delivering quality customer experiences will grow and succeed.

Another key feature of the marketing approach is relationship marketing.

It is no longer sufficient for a business to just market its goods and services in the hope of attracting new customers. What is also required is a business to keep its existing customers satisfied. **Relationship marketing** is the type of marketing that does this. It places a high priority on customer retention and continual satisfaction. The core of relationship marketing is customer loyalty — so as to generate repeat sales — which can be achieved through reward programs, customer care or good after-sales service. If, for example, you purchased a mobile phone plan and the telecommunications provider gave you excellent pre- and after-sales service, and also a customer reward program, you would probably continue purchasing the service from the provider. You may even recommend the service provider to your friends.

relationship marketing the development of long-term and cost-effective relationships with individual customers

Relationship marketing will be discussed in more detail in chapter 10.

7.3.4 The societal marketing approach — 1970s to present

In the 1960s and 70s the unethical practices of many companies became public. With growing public concern over environmental pollution and resource depletion came a shift in the emphasis of marketing plans. The concept of social marketing surfaced in 1972; a more socially responsible, moral and ethical model of marketing. The societal marketing approach is closely related to corporate social responsibility and sustainable development, and was implemented by several companies to improve their public image.

The **societal marketing approach** emphasises social responsibilities and suggests that to sustain long-term success, a business should develop a marketing strategy to maintain and improve the wellbeing of both customers and society. The societal marketing approach holds that a business should make good marketing decisions by balancing three considerations: consumers' wants, business profits and society's long-term interests.

societal marketing approach
a marketing approach that emphasises social responsibilities, as well as the importance of maintaining and improving the wellbeing of customers and society

SNAPSHOT

Case study: Nestlé 'Good Food, Good Life'



Nestlé is an excellent example of a business that adopts a societal marketing approach. Since the beginning their aim has been to enhance lives. Their mission, 'Good Food, Good Life', represents the company's commitment to enhancing life by providing customers with the best tasting, most nutritious food and beverages.

In order to be successful in the long-term and create value for shareholders, Nestlé believes they must also create value for the communities where they operate and for their consumers. They call this 'creating shared value'.

Nestlé have developed three bold ambitions to help them achieve their mission of unlocking the power of food to enhance quality of life for everyone. These three 2030 ambitions are:

1. **To help 50 million children lead healthier lives**: In order to help address global public health issues and to meet changing consumer preferences for healthier foods, Nestlé introduced more nutritious foods and beverages, simplified their ingredient lists and removed artificial colours. They have further decreased the proportion of sugars, sodium and saturated fat in their products and increased vegetables and wholegrains.
2. **To improve 30 million livelihoods in communities directly connected to their business activities**: Nestlé work with suppliers, partners and farmers globally to develop a range of initiatives to support rural development, promote and respect human rights and guarantee decent employment and diversity to help build stronger communities.
3. **To strive for zero environmental impact in their operations**: In order to achieve this aim, Nestlé use responsibly sourced ingredients and renewable resources. They have implemented strategies to allow them to operate more efficiently, eliminate waste, manage water more responsibly and reduce their greenhouse gas emissions. Nestlé have also researched and attempted to develop the most sustainable packaging for their products.

In relation to marketing, Nestlé has been an advocate for responsible marketing to children for quite some time. They have developed a Nestlé Policy on Marketing Communication to Children which mandates that all communication to children follows responsible marketing principles. Part of this policy states that any form of promotion to children is limited only to products that meet a specific nutritional profile. The company has leveraged their marketing efforts to promote healthy cooking, eating and lifestyles.

Together these goals will help Nestlé improve value for their shareholders and will have a long-term positive impact on every stakeholder connected with the company.

KEY IDEAS

- The production approach (1820s–1920s) focused businesses on the production of goods and services.
- The sales approach (1920s–1960s) emphasised selling because of increased competition.
- To stimulate demand for their goods and services, businesses increased their spending on advertising and training sales representatives.
- The marketing approach (1960s to present) focuses on finding out what customers want — through market research — and then satisfying that need.
- The marketing concept is based on the following principles. It must be:
  - customer-oriented
  - aimed at satisfying customers
  - integrated into the business plan so as to achieve the business's goals
  - aimed to develop long-term.
- In the 1960s and 70s thegrowing public concern over environmental pollution and resource depletion led to the concept of social marketing.
- The societal marketing approach emphasises social responsibilities and suggests that to sustain long-term success, a business should develop a marketing strategy to maintain and improve both customers' and society's wellbeing.

7.3 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

7.3 Quick quiz on	7.3 Exercise	7.3 Exam questions

Select your pathway

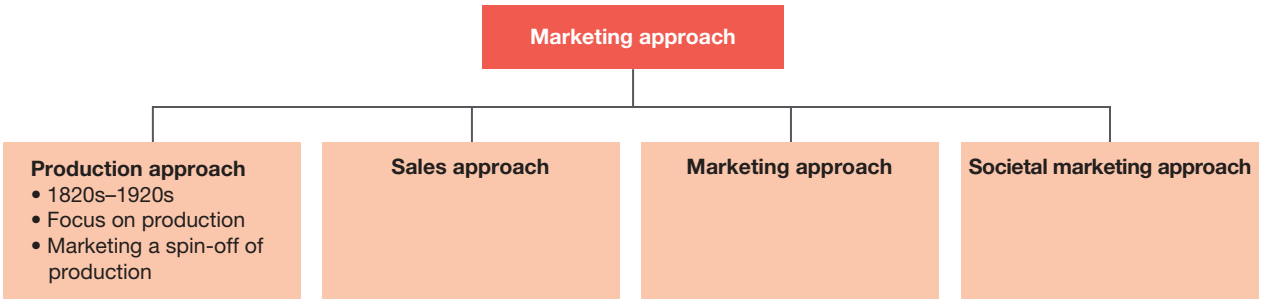
LEVEL 1	LEVEL 2	LEVEL 3
1, 7, 9, 10, 12, 13, 14	2, 3, 5, 6, 15	4, 8, 11, 16, 17

7.3 Exercise

Revision

1. **Define** the term 'marketing concept'.
2. The marketing concept is a business philosophy adopted by many modern businesses. Read the following three pairs of statements and write into your notebook the statement that represents the business that has adopted the marketing concept philosophy. **Justify** your selection.
   - **a.** Business A: 'Perhaps we should start stocking Clear View Mineral Water again. A lot of customers are asking for it.' Business B: 'We will only stock Clear View Mineral Water when it decides to give us a better deal than Natural Springs.'
   - **b.** Business A: 'Our sales are falling. We will have to think about laying off someone.' Business B: 'Our sales are falling. We will have to undertake some market research to find out why.'
   - **c.** Business A: 'Please give generously with your donations, no matter how small. You never know when you or your children may need some help.' Business B: 'Please help with your donations. Our charity is short of money.'

3. **Construct** a concept map (started below) summarising the four marketing approaches.



4. 'To disregard the "quality of life" issues when developing a marketing plan could lead to a customer backlash.' In small groups, use the brainstorm technique to **analyse** this statement. Share your group's answer with the rest of the class.
5. **Distinguish** between the terms 'customer orientation' and 'customer satisfaction'.
6. **Account** for why a business would want to adopt a societal marketing approach.
7. **Recall** the aim of relationship marketing.
8. Conduct a class survey to establish the number of loyalty programs that class members belong to. Discuss their effectiveness from the customers' viewpoint. **Create** a 100-word report of the discussion.

Read the Nestlé 'Good Food, Good Life' case study and answer questions 9 to 11.

9. **Outline** two ways in which Nestlé demonstrates corporate social responsibility.
10. Select one of their 2030 ambitions and then research Nestlé and **describe** one strategy the company has implemented in order to achieve that goal.
11. **Assess** whether Nestlé have been living up to their mission of 'Good Food, Good Life'.

Read the 'Slack's customer orientation and marketing approach' case study and answer questions 12 to 14.

12. **Identify** the external influences in the business environment that have had an impact on Slack.
13. **Outline** some of the strategies Slack has adopted that illustrate it has adopted a marketing approach.
14. **Describe** how Slack undertakes market research.

Extension

15. **Determine** why the marketing concept is difficult for some businesses to implement.
16. 'Marketing is not the sole responsibility of the marketing manager, but all managers.' **Assess** the accuracy of this statement using examples.
17. 'Relationship marketing is only successful if the business has access to detailed information about its customers.' **Evaluate** this statement.

7.3 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q10

Which approach is being used when a business creates a focus group to evaluate a product?

A. Marketing
B. Production
C. Selling
D. Standardisation

Question 2 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q15

Company XYZ allocates most of its marketing budget to advertising.

What approach has XYZ adopted?

A. Selling approach
B. Market approach
C. Customer approach
D. Production approach

Question 3 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q6

A business develops a shirt made from fabric which never stains or looks crushed. It then runs an advertising campaign to inform people about this product.

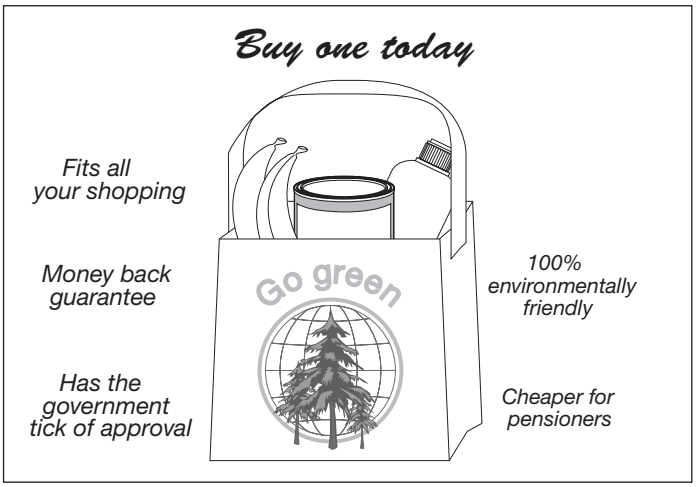
What type of approach is this?

A. Industrial
B. Marketing
C. Production
D. Selling

Question 4 (2 marks)

Source: HSC 2009 Business Studies Exam, Section II, Q25a

A customer-oriented business sells environmentally friendly shopping bags. The business is considering using the following advertisement to market its product. One business objective is to improve its reputation as a provider of environmentally friendly products.



Define *customer orientation*.

Question 5 (1 mark)

Source: Adapted from HSC 2005 Business Studies Exam, Section I, Q7

Which of the following best describes the selling approach to marketing?

A. Using aggressive advertising to persuade customers to purchase products
B. Satisfying the current and future preferences of customers to ensure long-term success
C. Pursuing production efficiencies to deliver quality products at prices that attract consumers
D. Enhancing the quality of working life to motivate staff to deliver high-quality goods and services

More exam questions are available in your learnON title.

7.4 Types of markets

SYLLABUS LINK In this subtopic you will learn about different types of markets, including: resource, industrial, intermediate, consumer, mass and niche.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

7.4.1 Introduction

For the purposes of this topic, a **market** is defined as a group of individuals, organisations or both that:

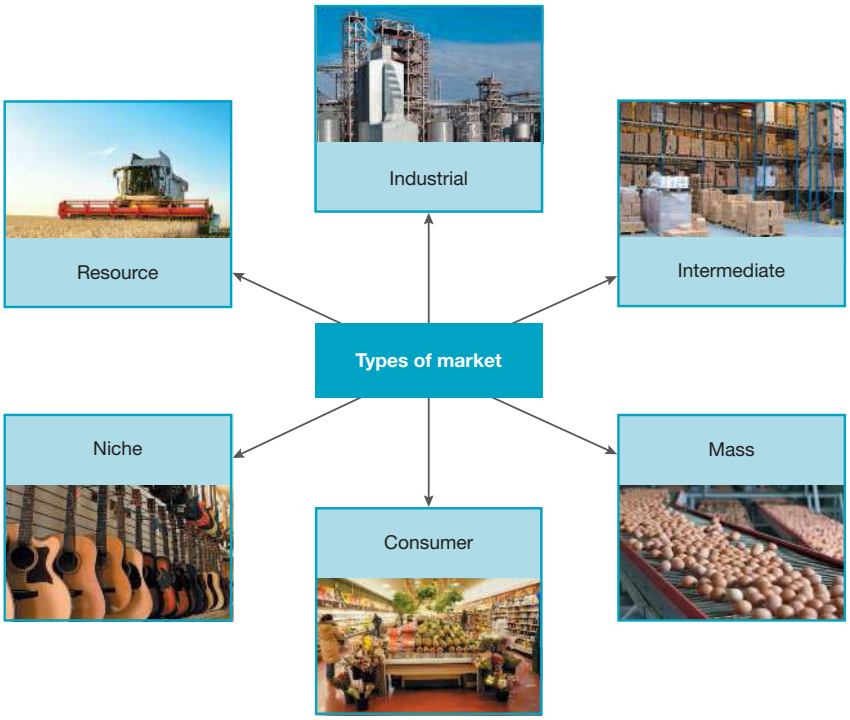
- need or want a product (goods or service)
- have the money (purchasing power) to purchase the product
- are willing to spend their money to obtain the product
- are socially and legally authorised to purchase the product.

market a group of individuals, organisations or both that: need or want products (goods or services), have the money (purchasing power) to purchase the product, are willing to spend their money to obtain the product, are socially and legally authorised to purchase the product

A group that does not have these four features is not considered to be a market.

In general use, the term 'market' usually refers to the total population, or mass market, that purchases products. Our definition is more specific and refers to individuals or groups who wish to buy *specific* products. There are many markets in an economy. Based on the characteristics of the individuals and groups that make up a specific market, it is possible to divide markets into six main types of markets: resource, industrial, intermediate, consumer, mass and niche (see figure 7.10).

FIGURE 7.10 The six different types of markets



Because marketing plans and strategies vary depending on the intended market, marketing managers need to understand the main characteristics of these six different types of markets.

7.4.2 Resource market

The **resource market** consists of those individuals or groups that are engaged in all forms of primary production, including mining, agriculture, forestry and fishing. The resource market makes up over 8 per cent of Australia's economy and generates over $264 billion in exports, accounting for more than 60 per cent of Australia's exports. As a group, this market in Australia is made up of over 180 000 enterprises or customers and has a large purchasing power. Farmers, for example, purchase machinery, seed and fertiliser.

resource market consists of those individuals or groups that are engaged in all forms of primary production, including mining, agriculture, forestry and fishing

industrial market includes industries and businesses that purchase products to use in the production of other products or in their daily operations

intermediate market consists of wholesalers and retailers who purchase finished products and resell them to make a profit

consumer market a market that consists of individuals — that is, members of a household who plan to use or consume the products they buy

7.4.3 Industrial market

An **industrial market** includes industries and businesses that purchase products to use in the production of other products or in their daily operations. Tip Top Bakery, for example, buys flour to make bread, and Sony buys plastics and metals to produce televisions. There are more than 481 000 businesses in the manufacturing and construction industries.

7.4.4 Intermediate market

The **intermediate market** consists of wholesalers and retailers who purchase finished products and sell them again to make a profit. The vast majority of goods sold to consumer markets are first sold to an intermediate market. Resellers are an intermediate market. Subway, for example, is a retailer that buys goods to make into sandwiches and salads for sale to consumers.

In Australia, the total intermediate market is made up of approximately over 132 000 retailers and over 79 000 wholesaling intermediaries. These figures however were prior to COVID-19 which resulted in decreased consumer confidence, an increase in job losses as well as a reduction in household spending. Australian retailers are now experiencing many hardships due to predictions that the retail market will decrease by 3.2 per cent in 2020.

FIGURE 7.11 The COVID-19 pandemic has had a devastating impact on the intermediate market. A significantly high number of big-name brands collapsed in 2020, which resulted in the closure of many retail shopfronts.



7.4.5 Consumer market

Consumer markets are the markets with which we are most familiar. Each time we go shopping at the local supermarket, we are part of the consumer market. **Consumer markets** consist of individuals — that is, members of a household who plan to use or consume the products they buy. Consumers do not intend to use the products to make other goods and services. Each of us is part of numerous consumer markets for products such as housing, clothing, food, entertainment, appliances, music recordings, cars and personal services.

Marketing managers examine closely the behaviour of consumers so they can better understand what motivates an individual to purchase a particular product. They also try to influence consumer buying behaviour by developing a mix of marketing strategies.

7.4.6 Mass market

mass markets in mass markets, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers

niche market a narrowly selected target market segment (also known as a concentrated or micro market)

Fifty years ago, marketing managers commonly spoke about the 'mass market'. In other words, there was a large demand for a standard product. In **mass markets**, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers. The business does not target its products to a specific group of buyers. The assumption is that all customers in the market have similar needs and wants.

The Model T Ford was the first motor vehicle to be mass-produced and sold to the mass market. When the Model T Ford was first released onto the American market in 1908, production could not keep up with demand. Henry Ford changed the production methods so that the assembly process was cut from 12.5 hours to 93 minutes. Henry Ford's 'famous' marketing slogan was that the customer could have the car in any colour he or she wished, 'as long as it was black'. This meant customers' wishes were not considered. A business could adopt this attitude in the early periods of industrialisation because consumers' wants could not be fulfilled; most items that were produced could easily be sold. (The production approach philosophy was dominant at this time.)

Very few products today are marketed to the mass market. Basic food items, electricity and water are three current examples. Due to greater choice, higher personal incomes and customers seeking more individualised products, the mass market has been replaced by segmented or niche markets.

The main benefits of serving the mass market are the scope and cost efficiency of doing business on such a large scale. Advertising messages broadcast over mass media give a business the ability to achieve economies of scale and appeal to a very large audience in a single showing. However, the advantages of mass marketing can only be achieved if the product in question is a commodity or is beneficial to people across a wide range of demographics.

FIGURE 7.12 Shoes of Prey began in 2009 enabling shoppers to customise shoes online. The business was quite successful targeting a niche audience for a number of years, but began to struggle when they attempted to scale into the mass market. In 2019 Shoes of Prey collapsed into liquidation. They learnt that mass market customers don't want to create; they want to be inspired and shown what to wear. They want to wear the latest trends and what influencers are wearing.



7.4.7 Niche market

At the other end of the spectrum to the mass market is a **niche market**, also known as a concentrated or micro market. The mass market is divided into smaller market segments consisting of buyers who have specific needs or lifestyles. This smaller group of consumers becomes the 'target' market, towards which marketing managers 'aim' their marketing efforts. For example, in any newsagent you will see row upon row of magazines, each appealing to a specific niche market — male, female, young, old, high income, low income, urban, rural, outdoor lifestyle, indoor lifestyle and so on (see figure 7.13). Market segmentation is discussed in more detail in chapter 9.

FIGURE 7.13 Niche magazines target highly specialised interests. They target extremely narrow audiences and appeal to the specific values of limited segments of people. For example, Meredith publishes a wide range of specialist publications that cater to women. While they publish more popular magazines such as *Better Homes & Gardens* and *Fitness*, they also publish special interest titles such as *Beautiful Kitchens & Baths, Do It Yourself, Country Gardens, Quilting and Diabetic Living.*



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KEY IDEAS

- A market is a group of individuals, organisations or both that:
  - need or want a product
  - have the money to purchase the product
  - are willing to spend their money to obtain the product
  - are socially and legally authorised to purchase the product.
- Marketing plans and strategies vary depending on the intended market.
- Marketing managers need to understand the main characteristics of these six different types of markets.
- There are six main types of markets.
  - Resource market: individuals or groups that are engaged in all forms of primary production
  - Industrial market: businesses that purchase products to use in the production of other products or in their daily operations
  - Intermediate market: wholesalers and retailers who purchase finished products and resell them to make a profit.
  - Consumer market: individuals who plan to use or consume the products they buy
  - Mass market: where the seller mass-produces, mass-distributes and mass-promotes one product to all buyers
  - Niche market: a narrowly selected target market segment

7.4 Activities

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7.4 Quick quiz on | **7.4 Exercise** | **7.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 6	2, 4, 5, 7, 8, 9, 10	11

7.4 Exercise

Revision

1. **Define** the term ‘market’.
2. **How** does this definition of market differ from the general use of the term?
3. **Outline** the six different types of markets.
4. **Distinguish** between the resource and industrial markets.
5. **Why** is Subway considered to be part of the intermediate market?
6. **Recall** the correct word to complete the following sentences. The words can be found by reading the ‘7.4.5 Consumer market’ section.
   a. Each time we go shopping at the local _____, we are part of the _____ market.
   b. Consumer markets consist of _____ that is, _____ of a household who plan to use or _____ the products they buy.
   c. Marketing managers examine closely the _____ of consumers so they can better understand what _____ an individual to purchase a particular product.
   d. Marketing managers also try to _____ consumer buying _____ by developing a mix of marketing _____.
7. **Distinguish** between the mass market and a niche market.

8. Indicate, using an 'M' or 'N', whether the following products are sold in a mass or niche market. **Justify** your selection.
   - **a.** Rolls Royce cars
   - **b.** Mount Franklin water
   - **c.** *BRW* magazine
   - **d.** Fruit and vegetables
   - **e.** BP petrol
   - **f.** Billabong wetsuits
   - **g.** PlayStation games
   - **h.** Sunbeam shearing combs

Extension

9. Research the Resource and Industrial markets. **Explain** some of the recent trends in these markets.
10. **Compare** and **contrast** the main features of a mass market and a niche market.
11. Refer to figure 7.11 and **assess** the impact COVID-19 has had on the retail market.

7.4 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q1

Sam runs a business that designs and sells custom-made, high fashion clothes.

In which type of market is Sam's business operating?

A. Intermediate
B. Mass
C. Niche
D. Resource

Question 2 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q14

In which type of market would a large scale manufacturer of pasta purchase flour for its products?

A. Consumer
B. Industrial
C. Mass
D. Resource

Question 3 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q15

A confectionery company used to sell its chocolate bars direct to the public. Now its products will only be available in supermarkets.

How has the market for the product changed?

A. From a resource market to an industrial market
B. From a consumer market to an industrial market
C. From a consumer market to an intermediate market
D. From an intermediate market to a consumer market

Question 4 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q1

In what type of market do wheat farmers sell their products?

A. Industrial
B. Intermediate
C. Niche
D. Resource

Question 5 (1 mark)

Source: HSC 2013 Business Studies Exam, Section II, Q25b

Robin and Pat are planning to establish a sporting goods business. They have decided to adopt a niche market approach to maximise profits. Evaluate their decision to adopt a niche market approach.

More exam questions are available in your learnON title.

7.5 Review

7.5.1 Summary

Role of marketing

- Marketing is undertaken by businesses with the intention of generating sales by satisfying customers' needs and wants.
- As consumers, we are constantly exposed to all aspects of the marketing process.
- Statistics reveal that more than 80 per cent of new products launched on the market fail in the first year of operation, mainly as a result of poor marketing.
- Marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives.
- A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.
- Marketing is a multifaceted activity involving much more than merely selling or advertising.
- The strategic role of marketing is to implement strategies to maximise sales, increase brand awareness and improve customer satisfaction so that the business can translate this goal into reality.
- Marketing today places a strong emphasis on viewing the business through the customers' eyes, or customer-oriented marketing.
- To develop customer awareness and demand, and thus form a customer base, an organised marketing campaign is necessary, starting with the development of a marketing plan.
- The marketing plan is a document that lists activities aimed at achieving particular marketing outcomes in relation to a good or service.
- Marketing does not occur in isolation; it is interdependent with the other key business functions.
- The marketing concept is a philosophy that states all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals.
- The marketing plan needs to become integrated into all aspects of the business, with marketing strategies playing a major role in all business activities.

Production, selling, marketing approaches

- The production approach (1820s–1920s) focused businesses on the production of goods and services.
- The sales approach (1920s–1960s) emphasised selling because of increased competition.
- To stimulate demand for their goods and services, businesses increased their spending on advertising and training sales representatives.
- The marketing approach (1960s to present) focuses on finding out what customers want — through market research — and then satisfying that need.
- The marketing concept is based on the following principles. It must be:
  - customer-oriented
  - aimed at satisfying customers
  - integrated into the business plan so as to achieve the business's goals
  - aimed to develop long-term.
- In the 1960s and 70s the growing public concern over environmental pollution and resource depletion led to the concept of social marketing.
- The societal marketing approach emphasises social responsibilities and suggests that to sustain long-term success, a business should develop a marketing strategy to maintain and improve both customers' and society's wellbeing.

Types of markets

- A market is a group of individuals, organisations or both that:
  - need or want a product
  - have the money to purchase the product
  - are willing to spend their money to obtain the product
  - are socially and legally authorised to purchase the product.
- Marketing plans and strategies vary depending on the intended market.

- Marketing managers need to understand the main characteristics of these six different types of markets.
- There are six main types of markets.
  - Resource market: individuals or groups that are engaged in all forms of primary production
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  - Intermediate market: wholesalers and retailers who purchase finished products and resell them to make a profit
  - Consumer market: individuals who plan to use or consume the products they buy
  - Mass market: where the seller mass-produces, mass-distributes and mass-promotes one product to all buyers
  - Niche market: a narrowly selected target market segment

7.5.2 Key terms

consumer market a market that consists of individuals — that is, members of a household who plan to use or consume the products they buy
customer orientation the process of collecting information from customers and basing marketing decisions and practices on customers' wants and interests
customer satisfaction measures how goods and services supplied by a business meet or exceed customer expectation
discretionary income disposable income that is available for spending and saving after an individual has purchased the basic necessities of food, clothing and shelter
industrial market includes industries and businesses that purchase products to use in the production of other products or in their daily operations
interdependence the mutual dependence that the key business functions have on one another
intermediate market consists of wholesalers and retailers who purchase finished products and resell them to make a profit
market a group of individuals, organisations or both that: need or want products (goods or services), have the money (purchasing power) to purchase the product, are willing to spend their money to obtain the product, are socially and legally authorised to purchase the product
marketing the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives (American Marketing Association). A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.
marketing approach focuses on finding out what customers want — through market research — and then satisfying that need
marketing concept a business philosophy that states that all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals
marketing plan a document that lists activities aimed at achieving particular marketing outcomes in relation to goods or services. The plan provides a template for future action aimed at reaching business goals, such as profit maximisation.
mass markets in mass markets, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers
niche market a narrowly selected target market segment (also known as a concentrated or micro market)
production approach a marketing approach that focuses on the production of goods and services
profit maximisation occurs when there is maximum difference between the total revenue coming into the business and total costs being paid out
relationship marketing the development of long-term and cost-effective relationships with individual customers
resource market consists of those individuals or groups that are engaged in all forms of primary production, including mining, agriculture, forestry and fishing
sales approach a marketing approach that emphasises selling because of increased competition
societal marketing approach a marketing approach that emphasises social responsibilities, as well as the importance of maintaining and improving the wellbeing of customers and society
strategic refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

strategy long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

Resources

Digital documents	Key terms glossary (doc-35573) Chapter crossword (doc-36214)
Interactivity	Chapter crossword (int-7157)
Exam question booklet	Chapter 7 Exam question booklet (eqb-0029)

7.5 Activities

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Exercise 1: Multiple choice questions

1. Which three key business functions is marketing interdependent with?
   - **A.** Operations, promotion and human resources
   - **B.** Promotion, human resources and finance
   - **C.** Human resources, finance and operations
   - **D.** Finance, operations and sales
2. Which of the following activities make up the four elements of the marketing mix?
   - **A.** Distribution, price, product and place
   - **B.** Promotion, price, packaging, product
   - **C.** Price, product, promotion, distribution
   - **D.** Product, publicity, price and promotion
3. A farmer grows vegetables to sell.
   In what type of market does this farmer operate?
   - **A.** Niche market
   - **B.** Resource market
   - **C.** Industrial market
   - **D.** Intermediate market
4. Which of the following best describes the selling approach to marketing?
   - **A.** Investing in more ecologically sustainable practices
   - **B.** Purchasing new machinery to assist the business in increasing production
   - **C.** Using extensive advertising methods to persuade customers to purchase products
   - **D.** Attempting to build long-term relationships with customers through superior customer service
5. Which of the following would be an example of a strategic goal?
   - **A.** To increase sales by 2 per cent in 6 months
   - **B.** To increase net profit by 10 per cent in 5 years
   - **C.** To launch a new product in the next three months
   - **D.** To hire two more employees to work in the marketing department in the next month
6. A-one Turf supplies rolls of grass to companies. Their motto is 'If we make it, they'll buy it'. Which marketing approach does this represent?
   - **A.** Marketing approach
   - **B.** Sales approach
   - **C.** Production approach
   - **D.** Customer orientation approach
7. Blissful Bedding buys springs and foam underlays to make beds. In which of the following does this company operate?
   - **A.** Intermediate market
   - **B.** Industrial market
   - **C.** Resource market
   - **D.** Niche market

8. Daring Dos is a hairdressing salon specialising in dreadlocks and hair extensions. Its market is considered to be which of the following?
   - **A.** Consumer market
   - **B.** Industrial market
   - **C.** Resource market
   - **D.** Niche market
9. What type of market is electricity an example of?
   - **A.** Niche market product
   - **B.** Consumer market product
   - **C.** Mass market product
   - **D.** Intermediate market product
10. Smokin' Salmon is a Tasmanian wholesaler selling smoked salmon in global markets. It packages the salmon with fine cheese and quality crackers, which it then sells to upmarket global retailers. It is operating in what type of market?
    - **A.** Consumer market
    - **B.** Industrial market
    - **C.** Resource market
    - **D.** Intermediate market

Exercise 2: Exam practice questions

Question 1 (3 marks)
Describe the strategic role of marketing goods and services.

Question 2 (2 marks)
Outline why very few products today are marketed to the mass market.

Question 3 (5 marks)
Explain how marketing is interdependent with operations. Use an example to support your answer.

Question 4 (4 marks)
Distinguish between the production and selling approaches to marketing.

Question 5 (5 marks)
Assess how a customer-oriented approach to marketing can provide a business with a competitive advantage.

Question 6 (6 marks)
Analyse the impact the COVID-19 pandemic has had on the intermediate market.

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Teacher-led video Chapter 7 Exam practice solutions (tlvd-1871)

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8 Influences on marketing

8.1 Overview

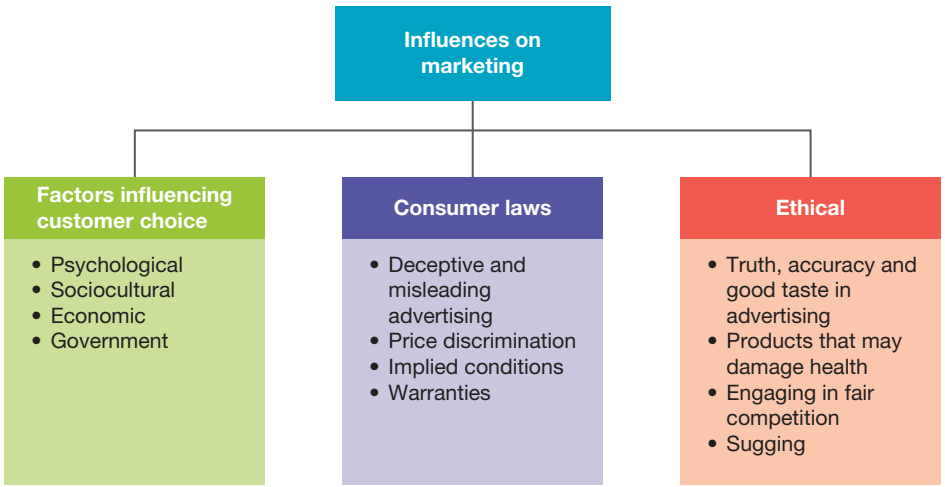
LEARNING SEQUENCE

8.1 Overview
8.2 Factors influencing customer choice
8.3 Consumer laws
8.4 Ethical influences
8.5 Review

8.1.1 Introduction

Marketing is a key business function that impacts on business success. To successfully manage the marketing function, managers must deal with a range of influences that could affect the success of a marketing campaign. Some industries differ from others, but most of the factors that influence marketing are the same across the board. These factors, and changes in them, present both threats and opportunities for businesses and require modifications to marketing plans. Marketers must continually monitor these influences and make changes accordingly, as these factors play a big role in the success of a business's marketing plan, as well as the overall success of the business. These influences are shown in figure 8.1.

FIGURE 8.1 Influences on marketing



on Resources

Digital document Key terms glossary (doc-35575)
Exam question booklet Chapter 8 Exam question booklet (eqb-0030)

8.2 Factors influencing customer choice

SYLLABUS LINK In this subtopic you will learn about factors influencing customer choice — psychological, sociocultural, economic, government.

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Marketers closely examine the behaviour of customers (consumers) to understand what motivates an individual to purchase a particular product — **customer choice (buying behaviour)**. They want to know why the customer selects one product and rejects another. As well, businesses try to influence customer choice by modifying their marketing strategies to appeal to the customer's motives.

Market research asks questions such as 'Who are our customers?', 'What do they buy?', 'When do they buy?' and 'How often do they buy?'; customer behaviour asks 'Why do they buy?'.

If businesses are aware of the factors that influence customer choice, they can predict customer trends and how they may react to particular marketing strategies.

customer choice (buying behaviour) the decisions and actions of customers when they search for, evaluate, select and purchase goods and services

SNAPSHOT

Case study: Coronavirus shifts consumer behaviour and helps some businesses boom

Social distancing measures and shutdowns introduced in response to the coronavirus pandemic have forced everyone to rethink their everyday interactions.

It may permanently change the way we live and work, according to Australian business leaders.

Teleconferencing services like Zoom and Skype, food delivery services like Uber Eats and Deliveroo, and bricks and mortar businesses like Bunnings now see the future differently.

They are a few of the fortunate businesses that have not just survived the biggest health and economic catastrophe of the century, but are booming.

However, the crisis has also raised new questions about privacy and security.

If more of us are online and using apps to do everything from birthday parties, weddings and funerals to high-level business board meetings and cabinet discussions, what responsibilities do companies have to protect our information?

Demand for videoconferencing will be 'exponential'

Zoom's head of APAC, Michael Chetner, says … videoconferencing has never been accessed as it is now.

Technology is now a requirement, not a wish list.

He noted recent cases of Italians using Zoom to conduct a wedding, New Zealand's Prime Minister Jacinda Ardern using the platform to pull together a cabinet meeting, and even senators in Brazil using it to vote on legislation.

…

In Australia there has been more demand for services in rural and regional areas and around education and health.

Mr Chetner says once there is more widespread use — with educators teaching their students and health professionals using the medium to deliver e-health services — "the increase will be exponential".

"It's still very early to tell whether that free user growth is going to turn into paying customers", he said, but noted in time that could happen.

"As of the end of December last year, the maximum number of daily meeting participants, both free and paid, conducted on Zoom was about 10 million.

"In March this year, we reached more than 200 million daily meeting participants, both free and paid."

Online food delivery soars and car sharing holds up



The introduction of social distancing measures and related closures of businesses has hit the café and restaurant sector especially hard.

But companies like UberEats and Deliveroo — which for some time have faced heavy opposition from bricks and mortar businesses for not paying the industry enough of a cut — are now seeing droves of temporarily shut-down restaurants move onto their platform.

Deliveroo chief executive Ed McManus said in the week after bans were introduced, the company saw an additional 1700 restaurants come onto their platform.

This includes higher-end restaurants, and those which in the non-coronavirus-period typically had long lines of customers waiting outside their doors, such as Melbourne's Chin Chin.

Mr McManus says there has also been growth in the number of new consumers ordering through the app, as well as in the volume of deliveries.

"We have seen steady growth over past few weeks particularly in lunchtime demand."

He says coronavirus does raise interesting questions about whether consumer behaviour is now forever changed across industries, especially in retailing.

"It depends how long this lasts," he said, but added Australians loved dining out with friends and family, and that would likely always be the case.

Uber Eats regional general manager Jodie Auster says the platform already has more than 20,000 restaurant partners to choose from.

"Since the start of the coronavirus pandemic we have witnessed an influx of new restaurants … looking for ways to increase their digital business," she said.

Uber Eats has deployed staff from other parts of its business, including New Zealand, to meet this increased demand.

'Leave at door' contactless delivery is now available in all Australian cities.

But while this is an "unprecedented time for businesses across the world", according to Ms Auster, once the crisis ends she expects Australians will return to dining out.

Chapel Street Precinct Association general manager Chrissie Maus said businesses have been forced to pivot to home delivery to survive this pandemic period, but were reluctantly using the online delivery platforms which charged "sky-high commissions".

Mr McManus said, "we do hear that message, but we're not in a position to reduce commissioners because if we did, we'd have to pay delivery riders less".

Will Davies, chief executive and co-founder of car sharing platform Car Next Door, said at one point last month their service was up 70 per cent compared to the same time last year.

While demand has since dropped off, he says Australians are still using car sharing, especially people in the healthcare industry who are still travelling to and from work but don't have a car and don't want to use public transport.

Retail sector in a state of flux, but it will adapt

The retail sector, however, may have permanently changed.

Bunnings managing director Mike Schneider says the retailer has seen unprecedented demand for goods as more Australians work and spend time at home.

Mr Schneider says there has been a huge wave of people purchasing supplies to build home offices and home classrooms.

But there has also been steady strong demand for cleaning products, seedlings and general garden supplies including seedlings.

The company's online marketplace has also been booming, with people purchasing gym equipment and various home fittings and furnishings.

Mr Schneider said in March there were about 30 million visits to the Bunnings website.

"That's started to flow through to increased products purchased through the website," he said.

The percentage of customers opting for online delivery also increased.

"Our patterns of living are going to change, and if that changes then what you buy and how you buy it changes. That presents a challenge for business to adapt. There's no doubt that the online retailing space will."

Demand for online goods from beauty to books

Businesses that have already been operating online have been unexpected winners in this crisis.

Kate Morris, founder of adorebeauty.com.au, says her Melbourne-based business has never seen such a leap in demand for online beauty and skincare products.

She expects they will hit over the budget target of $100 million turnover this year, thanks to a huge spike in demand for products including handwash, hand sanitiser and soap and skincare.

"Premium handwash sales are up 342 per cent," she said.

Since beauty salons closed and people stopped going to hairdressers because of stricter social distancing measures, Ms Morris says sales of shampoo and conditioners as well as "feel-good" items like face masks have also soared.

"There's a big uplift in new customers shopping with us for the first time. It's possible that they were shopping online somewhere else before or they are first-time online shoppers."

It's not just the beauty industry benefiting.

Australian online bookstore Booktopia's deputy CEO and CTO Wayne Baskin says they are hitting their budget targets because demand for some books has gone up.

"A lot of the universities have delayed their courses as international students aren't coming in anymore."

Online auctions make an entrance

Since mid-March, following a ban on open home inspections and on-site auctions, there's been some growth in online auctions and livestreaming of auctions.

…

Australians find new ways to survive, interact

Brendan Condon, chief executive of Melbourne-based urban farming company Biofilta, has already seen people's living habits change.

His business offers a "Foodcube" that allows communities to produce large volumes of fresh food in small city spaces including backyards, carparks and rooftops.

Mr Condon said since coronavirus, Biofilta had more than doubled the number of Foodcubes it sells each month from 150 to 300.

He says each module grows around 25 kilograms of fresh produce annually and the average order is between five to 10 food cubes with soil.

"That's enough for 125 kilograms to 250 kilograms of fresh produce," he said.

But it is not just consumer habits changing. Small businesses are also adapting.

Suzi Jamil is the owner and director of Think Inc, an events touring company that has in the past brought international speakers including Jane Goodall and Richard Dawkins to Australia.

She said the company used to charge about $70 to $80 a ticket for people to see live events at places like the Sydney Opera House.

Now, she's moved the events online and charges about $10 to $20 a ticket.

Online audiences can still engage with the star of the show in real-time, with a live Q&A, and chance to do online networking after the event.

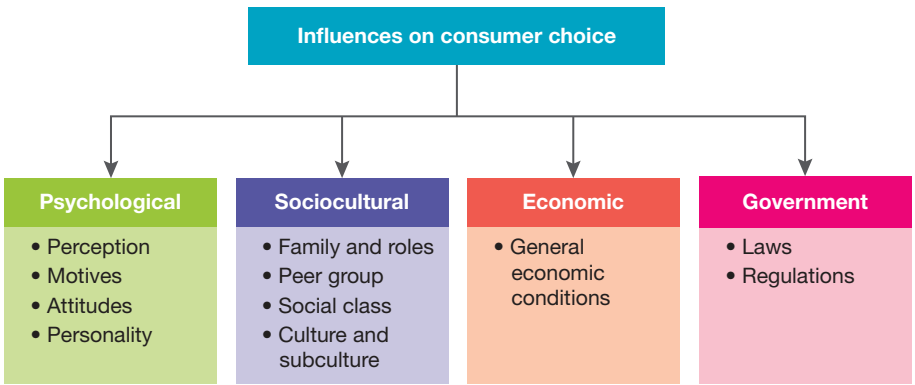
"This is a major shift [in how people behave]," she said.

"It is teaching people to link up online. And as a small business owner based in Sydney, I can reach a global demographic."

Source: Nassim Khadem, 'Coronavirus shifts consumer behaviour and helps some businesses boom', ABC.net.au, 6 April 2020.

Have you ever stopped to consider what influences your buying decisions? Why do you purchase certain products and not others? Over the years, marketers have suggested numerous theories to explain what it is that persuades individuals to buy products. One of the most common ways is by examining the four main factors which influence customer choice (see figure 8.2).

FIGURE 8.2 The four main factors influencing customer choice



BizFACT

Successful marketing begins with understanding why and how customers behave as they do.

8.2.1 Psychological influences

Psychological factors are influences within an individual that affect his or her buying behaviour. Five main psychological factors influence customer choice. These are perception, motives, attitudes, personality and self-image, and learning.

Even though these psychological factors operate internally, they are also very much affected by sociocultural forces outside the individual.

Perception

What an individual perceives may be very different from reality; people see and hear the same things differently. For example, one person sees a Ferrari motor vehicle as a sign of achievement; another sees it as ostentatious. This is the result of perception. **Perception** is the process through which people select, organise and interpret information to create meaning. Usually there is a range of perceptions across different individuals.

As individuals we often act on our perceptions of reality rather than reality itself. Consequently, marketing managers are extremely aware that they must create a positive or favourable perception about their product in the mind of the customer. Customers will not normally purchase a product that they perceive as inferior. The perception customers have of a product is often the result of some type of advertising that attempted to create a certain 'image' of the product — images such as trendy, luxurious, classy, fun and rebellious. In reality, the product may not necessarily have such qualities. It may be more to do with how consumers perceive the product.

Motives

A **motive** is an individual's reason for doing something. The main motives that influence customer choice include comfort, health, safety, ambition, taste, pleasure, fear, amusement, cleanliness and the approval of others. As with the customer's perception of the product, advertising also attempts to influence an individual's motives (for instance, the desire to emulate a sporting hero). That is, advertising attempts to motivate the customer to buy the product.

Attitudes

An **attitude** is a person's overall feeling about an object or activity. Customer attitudes to a business and its products generally influence the success or failure of the business's marketing strategy. Negative attitudes to a business or its products often force the business to change its strategies.

Personality and self-image

An individual's **personality** is the collection of all the behaviours and characteristics that make up that person. To some extent, personality will influence the types and brands of product a person buys. For example, the style of car, clothing or jewellery that a person buys may reflect their personality.

Coupled with personality is an individual's **self-image**: how a person views himself or herself. Self-image is a major determinant of what products we buy. We all have an image of who we are, and we reinforce this image through our purchases. The tendency to believe 'you are what you buy' is widespread among certain types of individuals, especially young people. Marketers will make the most of an individual's desire to express their identity through what they buy by highlighting the image value of their products. This is why celebrities and sportspeople are regularly used to endorse a product; people want their self-image to be a reflection of those who they regard as important and influential (see figure 8.3).

psychological factors influences within an individual that affect his or her buying behaviour

perception the process through which people select, organise and interpret information to create meaning

motive an individual's reason for doing something

attitude a person's overall feeling about an object or activity

personality the collection of all the behaviours and characteristics that make up an individual

self-image how a person views himself or herself

Learning

Customers have direct experience of many new products. When they do, they are also learning. Consequently, much of customer behaviour is learned. **Learning** refers to changes in an individual's behaviour caused by information and experiences. For example, learning occurred the first time a customer tasted Coca-Cola! Learning may also be based on indirect experiences. If a customer sees an advertisement for Coca-Cola that shows other people enjoying a new flavour, the customer might assume that they would like it also.

FIGURE 8.3 Celebrities and sportspeople are often used to endorse products because people aspire to be like them. If a consumer idolises a certain celebrity who supports a particular brand or is seen in advertisements promoting a new product, that consumer will associate it with their success, beauty and skill and will subconsciously believe that using that product will give them the same traits they admire.



To market products successfully, a business must help customers learn about them. Successful marketing strategies may assist customer learning that encourages **brand loyalty** Therefore, marketers can successfully use positive learned experiences to build brand loyalty. Behaviour that results in a satisfying outcome will tend to be repeated. For example, when a customer buys a packet of chips and likes them, he or she is more likely to buy that same packet of chips again. This experience (learning) relates to habit formation. There is a close link between habits and brand loyalty; customers will continue purchasing particular brands because of positive reinforcement of previous actions.

8.2.2 Sociocultural influences

Whereas psychological influences are internal forces, **sociocultural influences** are forces exerted by other people and groups that affect customer behaviour. There are four main sociocultural factors. They are social class, culture and subculture, family and roles, and reference (peer) group.

Social class

In our society, the factors generally used to determine a person's **social class** — often referred to as **socioeconomic status** — are education, occupation and income. Social class influences the type, quality and quantity of products a customer buys. People from a high socioeconomic status background, for example, are usually willing to buy products that are perceived to be prestigious. Higher income earners may purchase luxury cars that symbolise their status, and are more likely to shop in upmarket retail stores.

Culture and subculture

Culture is all the learned values, beliefs, behaviours and traditions shared by a society. Culture influences buying behaviour because it infiltrates all that we do in our everyday life. It determines what people wear, what and how they eat, and where and how they live. For example, in response to the greater desire for nutritious and healthy foods, many low-fat, sugar-free and fibre-enriched processed food products are now marketed.

learning changes in an individual's behaviour caused by information and experiences

brand loyalty when a favourable attitude towards a single brand results in repeat sales over time

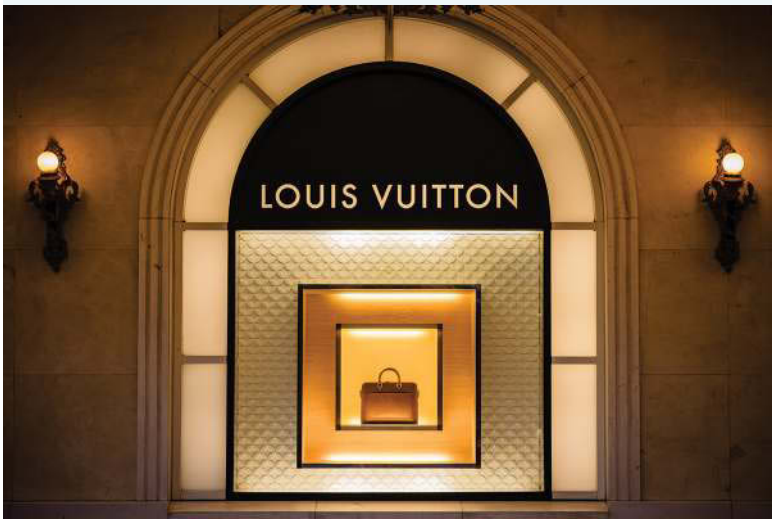
sociocultural influences forces exerted by other people and groups that affect an individual's buying behaviour

social class or **socioeconomic status** a person's relative rank in society, based on his or her education, income or occupation

Family and roles

All of us occupy different roles within the family and groups within the wider community. These roles influence buying behaviour. For example, although women's roles are changing, market research shows that most women still make buying decisions related to healthcare products, food and laundry supplies. Studies have shown that teens are a household's chief influencer and their opinion on purchases is often sought by parents worldwide. The main categories in which teens wield the most influence are clothes, shoes, music, books, food and beverages, household goods, travel and spending on family excursions. Around three-quarters of teens said they influenced how their parents spent on these categories.

FIGURE 8.4 Marketers realise that socioeconomic status plays a significant role in customer behaviour. These days, many women are prepared to spend more on a handbag than on a holiday or even a car! Why are luxurious handbags so desirable? It's partly because they've become symbolic of a woman's status and earning power.



BizFACT

Pester power is the ability children have to make their parents buy something, by asking for it many times until they get it. Seventy-one per cent of parents believe their kids exert influence over how much they spend on products.

Reference (peer) groups

A **reference** or **peer group** is a group of people with whom a person closely identifies, adopting their attitudes, values and beliefs. A customer's buying behaviour may change to match the rest of the group's beliefs and attitudes. For example, if a close friend tells you of a bad experience at a particular shop, you will probably change your buying behaviour based on this information. Alternatively, if your peer group wears distinctive clothing, you probably make clothing purchases based on this influence.

8.2.3 Economic influences

Economic forces have an enormous impact both on businesses and customers. They influence a business's capacity to compete and a customer's willingness and ability to spend. Economies do not always experience constant growth. Rather, the level of economic activity fluctuates from boom to recession. Each of these two distinct phases influences the marketing environment in a number of ways (see figure 8.5).

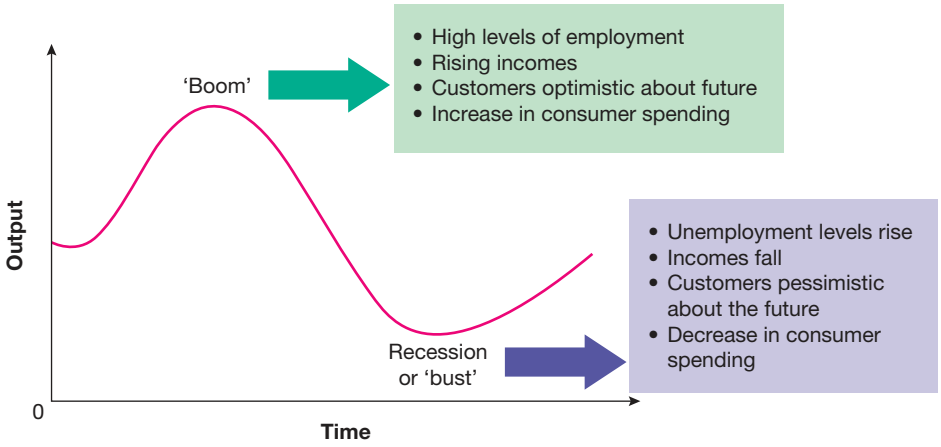
Boom

A boom is a period of low unemployment and rising incomes. Businesses and customers are optimistic about the future. Businesses increase their production lines, and attempt to increase their market share by intensifying their promotional efforts. Customers are willing to spend because they feel secure about their jobs and source of income.

reference or **peer group** a group of people with whom a person closely identifies, adopting their attitudes, values and beliefs

The marketing potential during such a phase is large, with sales responding to all forms of promotion.

FIGURE 8.5 Economic influences on customer choice



Recession

A recession sees unemployment reach high levels and incomes fall dramatically. Customers and businesses lack confidence in the economy and if this phase lasts for a long time, a mood of deep pessimism persists. Customer and business spending reach very low levels. Such caution and pessimism result in customers reducing their spending. Customers become more price-conscious. They look for value and products that are functional and long-lasting (see the following case study). Marketing plans should, therefore, stress the value and usefulness of a product. As well, marketing plans during this time should concentrate on maintaining existing market share. Survival becomes the main business goal.

SNAPSHOT

Case study: How the coronacession influenced customer choice

Australia's current recession is the deepest since the Great Depression of the early 1930s. The economy shrank 7 per cent in the three months from April to June 2020, which is the biggest collapse since the Australian Bureau of Statistics began collecting records. This pandemic has illustrated how much economic disruption can influence and change spending behaviour.

At the beginning of the pandemic, advisers to the government predicted the economy would collapse by 20 per cent; however, the unprecedented government support that was provided helped Australia avoid such a large fall. The government spent more than $100 billion on JobKeeper and JobSeeker payments alone. This stimulus helped lift household incomes while 643 000 Australians lost their jobs and many others lost hours.

Household consumption suffered a 12.1 per cent drop in the June quarter 2020. This can be attributed in part to the lockdowns as well as caution due to the fact that the pandemic provided fewer opportunities for consumers to spend.



Obviously, the downturn in the economy impacted industries differently. For instance, industries that were hit hardest by the pandemic were transport services (which includes everything from flights to public transport), accommodation, and recreational and cultural services, which fell 88 per cent, 55.7 per cent and 54.5 per cent respectively.

Another influence of the recession on customer choice was that, during the pandemic, many Australians switched to discount brands like Aldi and Costco. Discount department stores such as Big W and Kmart also experienced an increase in market share.

Australian spending habits also changed markedly in 2020. Some spending habits that emerged during the downturn are predicted to permanently reshape consumer behaviour and choice. For instance, food delivery has seen the biggest per capita increase, with spending 351 per cent higher by the end of August than the pre-pandemic norm. Subscription television was 11 per cent higher than normal and the purchase of streamed music, video games and apps were also 53 per cent above normal. COVID-19 also turbocharged the shift to online shopping. Online sales increased 55 per cent in July 2020 compared with July 2019. Even as social-distancing rules ease, many physical stores are predicted to close as a result.

Purchases on furniture and office equipment were 77 per cent higher than normal by the end of August, home improvement spending was up 38 per cent and pet care spending was 14 per cent higher than normal. In addition, spending on online gambling and alcohol were 71 and 35 per cent higher than normal respectively.

8.2.4 Government influences

Governments use a number of economic policy measures to influence the level of economic activity. Depending on the prevailing economic conditions, the government will put in place policies that expand or contract the level of economic activity. These policies directly or indirectly influence business activity and customers' spending habits, and therefore will influence the marketing plan.

The influence of government regulations has a more direct and immediate impact on the marketing plans of a business. Regulatory forces consist of laws (statutes) and regulatory bodies that can influence business behaviour. Such regulatory forces exert a significant influence over the marketing activities of businesses because the breaking of these laws or regulations may result in financial penalties.

A number of laws, such as the *Competition and Consumer Act 2010* (Cwlth) (formerly the *Trade Practices Act 1974*), *Sale of Goods Act 1923* (NSW) and the *Fair Trading Act 1987* (NSW), have been passed that influence marketing decisions.

In March 2020, the federal government released three stimulus payments that had a very big influence on consumer spending: the $550 Coronavirus Supplement, which people received if they were on JobSeeker; the one-off $750 Economic Support Payment; and the $1500 JobKeeper wage subsidy.

JobKeeper was a wage subsidy scheme that provided payments of $1500 per fortnight to millions of eligible Australians. Payment was made via businesses impacted by COVID-19. These businesses were able to access a subsidy from the government to enable them to continue paying their employees.

JobSeeker is a social security payment for people who are looking for work. It can also be paid if a person is sick or injured and can't do their usual work for a short time. The JobSeeker Payment was introduced to replace other payments in response to COVID-19. In March 2020, the government began paying a supplement of $550 per fortnight, effectively doubling the current payment, for new and existing social security recipients.

In relation to consumer confidence and spending, these payments kept up to six million people employed, thus avoiding what could have been an even bigger increase in the unemployment rate and an even bigger fall in spending.

on Resources

Weblink NSW Fair Trading 1

KEY IDEAS

- Marketers examine the behaviour of customers (consumers) to understand what influences customer choice.
- Customer choice is influenced by four main factors.
  1. Psychological:
     - influences within an individual that affect his or her buying behaviour
     - psychological factors include the buyer's perceptions, motives, attitudes, personality and self-image, and learning.
  2. Sociocultural:
     - influences exerted by other people and groups that affect an individual's buying behaviour
     - sociocultural factors include the buyer's social class, culture and subculture, family role and peer groups.
  3. Economic:
     - economic forces that influence a business's capacity to compete, and a customer's willingness and ability to spend
     - the level of economic activity fluctuates from boom to recession.
  4. Government:
     - policies that directly or indirectly influence business activity and customers' spending habits
     - laws such as the *Competition and Consumer Act 2010* (Cwlth), *Sale of Goods Act 1923* (NSW) and the *Fair Trading Act 1987* (NSW) that influence marketing decisions.

8.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. **A downloadable solutions** file is also available in the Resources tab.

8.2 Quick quiz on	8.2 Exercise	8.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 11, 13, 14, 15, 17, 20, 22	2, 3, 4, 5, 6, 7, 8, 9, 10, 12, 16, 18, 19, 21, 23, 24	25, 26, 27

8.2 Exercise

Revision

1. **Define** the term 'customer choice'.
2. Of the four factors influencing customer choice, **identify** which factor you think influences you most. **Justify** your answer.
3. **How** does an individual's perception of a product influence their buying behaviour?
4. **How** and why do marketing managers attempt to alter consumer perception?
5. 'The tendency to believe "you are what you buy" is widespread among certain types of individuals, especially young people.' **Interpret** what is meant by this statement.
6. **How** might an understanding of customers' learning processes affect a marketing plan? Use an example to support your answer.
7. **Explain** the relationship between positive learned experiences, habits and brand loyalty.
8. **Identify** a brand that you are loyal to and **justify** why you are loyal to this brand.
9. **Distinguish** between the sociocultural and psychological factors that influence customer choice.
10. **Demonstrate** in what ways social class affects a customer's choice.
11. **Describe** a subculture or peer group to which you belong. Identify purchases that are unique to your subculture.

12. **Explain** how family roles such as carer or provider affect customer choice.
13. **Identify** some of your own reference groups. **Outline** how reference groups influence customer choice.
14. Collect a number of print advertisements from a magazine. **Identify** the psychological and/or sociocultural influence to which each advertisement is appealing.
15. **Summarise** the impact that economic conditions may have on business, consumers and the marketing plan.
16. **How** do government policies and regulations influence the marketing environment?

Read the case study 'Coronavirus shifts consumer behaviour and helps some businesses boom' and answer questions 17 to 21.

17. **Identify** some businesses that thrived during the COVID-19 pandemic.
18. **Justify** which industries will increase their reliance on Zoom.
19. **Why** did online delivery services and car sharing organisations experience an increase in sales during the pandemic?
20. **Identify** products that experienced an increase in demand.
21. **How** did some small businesses adapt during the COVID-19 pandemic?

Read the case study 'How the coronacession influenced customer choice' and answer questions 22 to 24.

22. **Identify** those industries that have been hit hardest by the COVID-19 recession.
23. **Explain** how Australian spending habits changed during the pandemic.
24. Account for **why** there was an increase in online shopping.

Extension

25. 'Through knowledge of customer buying behaviour, marketing managers can learn to manipulate customers to purchase their products.' **Assess** the validity of this statement.
26. 'Perception is reality; what we think is true about a product does not matter.' **Critically analyse** this statement.
27. Suppose research at Apple reveals that potential customers are apprehensive about buying an iPad for home use. **Determine** what strategies you might recommend to Apple to reduce customer apprehension.

8.2 Exam questions

Question 1 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q7

Vinh's friends tell him that a particular brand makes poor quality jeans. He does not buy this brand due to his friends' opinions.

Which factor is influencing his choice?

A. Economic
B. Government
C. Sociocultural
D. Psychological

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q7

A person purchases his clothing from a discount store because he is a low-income earner.

What factor is influencing his consumer choice?

A. Economic
B. Legal
C. Psychological
D. Sociocultural

Question 3 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q1

Sally shops at a particular store as she has always received excellent service there.

What type of factor is influencing her choice of store?

A. Economic
B. Government
C. Psychological
D. Sociocultural

Question 4 (2 marks)

The owner of an organic food restaurant has decided that he appeals to customers who are affected by economic and psychological factors. Outline features of these factors affecting customer choice.

Question 5 (1 mark)

Source: HSC 2004 Business Studies Exam, Section I, Q17

Which of the following consumer choices is influenced by a psychological factor?

A. Making food choices based on medical advice
B. Purchasing a generic brand in preference to a more expensive manufacturer's brand
C. Purchasing takeaway food in order to provide more time for family
D. Choosing a healthy food from the canteen rather than a deep-fried product, to encourage weight loss

More exam questions are available in your learnON title.

8.3 Consumer laws

SYLLABUS LINK In this subtopic you will learn about consumer laws and their impact on deceptive and misleading advertising, price discrimination, implied conditions and warranties.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Since the 1960s, the broad area of business law that relates to dealings between consumers and businesses has been subject to radical and fairly continuous change. Governments, both federal and state, have introduced laws to improve the protection and rights of consumers, and to clarify the rights and responsibilities of businesses. Marketers do not have to be skilled lawyers, but they should be familiar with the laws that regulate their activities. Ignorance of the law is no defence. Marketers must also ensure they are aware of any changes to the laws if those changes apply to their particular business. Their responsibility is to understand and apply laws within their business where needed. They may need to introduce changes, such as an alternative advertising promotion, a repackaging of a product or a change in the credit policy for customers. Whatever the change, a business must ensure it is up to date with the current laws and that it applies them to all marketing practices.

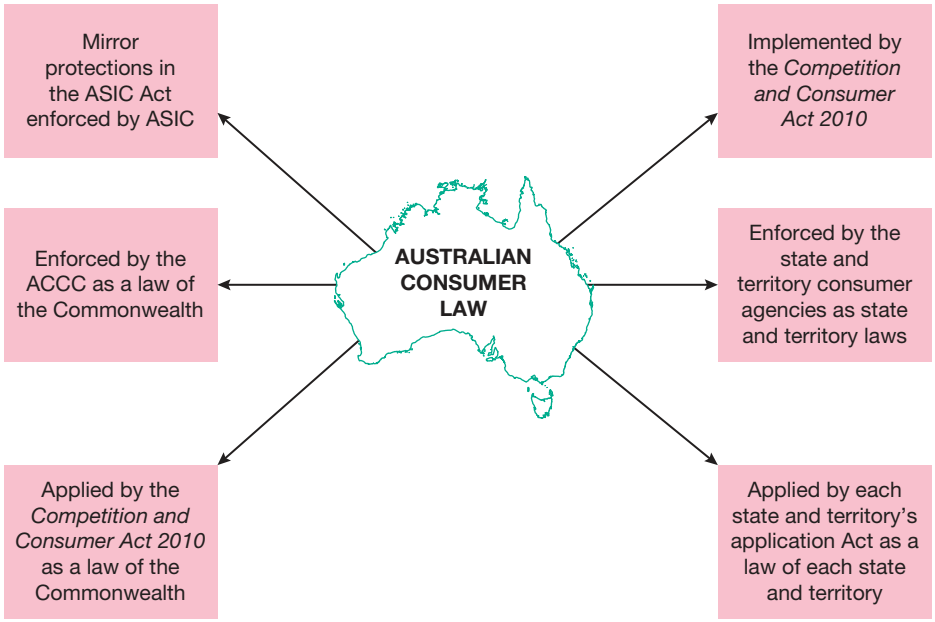
8.3.1 The Australian Consumer Law

In 2011, a single, national consumer law — the Australian Consumer Law (ACL) — was introduced, which replaced 17 existing national, state and territory consumer laws. The ACL applies in the same way to all Australian consumers and businesses regardless of where the business operates or where consumers shop.

BizFACT

The ACL will benefit the Australian community by giving Australian consumers the same rights and protections wherever they are in Australia.

FIGURE 8.6 From 2011, the ACL replaced different national, state and territory laws that set out consumer rights and business obligations when selling goods and services with a single, national set of rules. The ACL is an application law, which will be applied and enforced as a law of each jurisdiction in Australia.



8.3.2 Competition and Consumer Act 2010

The *Competition and Consumer Act 2010* (Cwlth) is one of the most important pieces of legislation affecting marketing and business practices in Australia. The Act has two major purposes:

1. to protect consumers against undesirable practices, such as misrepresenting the contents of products or their place of production, and misleading and deceptive advertising
2. to regulate certain trade practices that restrict competition. The government also wants to ensure a number of businesses are operating at any one time in the same market to encourage competition.

The Competition and Consumer Act (CCA) applies to virtually all businesses in Australia, including the commercial activities of government. The CCA is enforced and administered by the Australian Competition and Consumer Commission (ACCC), each state and territory's consumer agency, and the Australian Securities and Investments Commission (ASIC) in respect of financial services.

FIGURE 8.7 In 2019 the ACCC initiated proceedings again Samsung accusing the company of deceiving consumers by telling them that various Galaxy phones were water resistant, while knowing they were not. The ACCC alleges Samsung's advertising made consumers believe their phones would continue working even if exposed to all types of water, when that was not the case. These misleading claims were made in more than 300 advertisements.



A breach of any of the consumer protection provisions of the Competition and Consumer Act can result in the ACCC — or the relevant consumer agency — taking civil or criminal proceedings against the business or individual concerned.

In 2018, the maximum penalties per breach of the ACL were increased, including for **unconscionable conduct**, making false or misleading representations, and supplying consumer goods or certain services that do not comply with safety standards or which are banned. The penalty for companies was increased from $1.1 million per breach to the greater of $10 million, three times the value of the benefit received, or where the benefit cannot be calculated, 10 per cent of annual turnover in the preceding 12 months. Penalties against individuals under the ACL also increased from $220 000 to $500 000 per breach. In addition, the consumer can sue the business for compensation. When legal fees and the damage to the business's reputation are included, the cost of breaching the CCA can be substantial.

Where the ACCC has reasonable grounds to believe a person has breached the provisions of the ACL they have the power to issue an Infringement Notice (fine) in respect of the following: unconscionable conduct; false or misleading conduct; pyramid selling; certain product safety and product information provisions; failure to respond to a substantiation notice; false or misleading information in response to a substantiation notice. The penalty amount in each infringement notice will vary, depending on the alleged breach, but in most cases it is $13 320 for a corporation (or $133 200 for a listed corporation) and $2 664 for an individual for each alleged infringement of the CCA without having to undertake court action.

The ACCC can also now issue 'public warning notices' to warn consumers of suspected illegal activity. Previously, the ACCC had to gather evidence and then seek a temporary court injunction (ban), while the suspected illegal activity continued.

Businesses must ensure that they are up to date with the current laws and that they apply them to all marketing practices. The following are some of the undesirable and misleading practices that are illegal under the Competition and Consumer Act.

8.3.3 Deceptive and misleading advertising

The Competition and Consumer Act makes deceptive and misleading advertising illegal. The general rule is that when a business makes any representation (direct or implied), the business must ensure that the representation is not untrue or false and is not likely to mislead the type of consumers at which the advertisement is targeted. Even though this is illegal, a number of methods are still used by some businesses. Some examples of deceptive or misleading advertising include:

- *Bait advertising*. This involves advertising products that are not available, or only available in very limited quantities, at reduced prices to attract customers. When the advertised products quickly run out, customers are directed (or switched) to higher priced items.
- *Fine print and qualifications*. When important conditions are written in a small-sized print. This information must not contradict the overall message of the advertisement.
- *Comparative advertising*. If an advertisement compares products or services to others on the market, the advertising can be misleading if the comparison is inaccurate or does not appropriately compare products.
- *Environmental ('green') claims*. When businesses make environmental claims about products, they must be able to substantiate them.
- *Country of origin*. It is illegal to make false or misleading claims about the country of origin of goods.
- *Premium (or credence) claims*. Claims that give the impression that a product, or one of its attributes, has some kind of added benefit when compared to similar products, can be made only if the claims are not misleading and can be substantiated, e.g. 'fat free', '100% recyclable', etc.

unconscionable conduct any practice by a business that is not reasonable and often illegal

- *Prize giveaways and competitions*. If a business gives away free items or prizes, they must not mislead consumers about the items on offer or the chances of receiving these items. If there is a catch, they must let people know at the outset.
- *Dishonest advertising*. Advertisements must not use words that are deceptive or claim that a product has some specific quality when it does not. Such actions convey a false impression of the exact nature of the product (see the following case study). As well, price reduction, specials or free-gift offers must all be genuine.

FIGURE 8.8 The makers of Voltaren admitted they breached the Australian Consumer Law and were fined $4.5 million in 2020 for making false and misleading representations in their marketing. The company admitted they marketed Osteo Gel as being more effective than Emulgen (which is 33 per cent cheaper) in treating osteoarthritis despite the two products being essentially the same.



BizFACT

In 2019 the Federal Court ordered training college Empower Institute to pay $26.5 million in penalties for breaches of the ACL. The Court also ordered Empower to repay more than $56 million to the Commonwealth for funding it had received to provide the courses. The Court found that Empower had engaged in a system of unconscionable conduct when it enrolled consumers in VET FEE-HELP funded courses, by marketing courses to vulnerable and disadvantaged consumers, making false or misleading representations, and in some cases offering inducements such as free Google Chromebooks.

SNAPSHOT

Case study: Volkswagen fined for misleading customers



In 2019 Volkswagen AG was ordered to pay a $125 million penalty for misleading consumers about its diesel emissions. The Federal Court declared by consent that the company breached the Australian Consumer Law by making false representations about compliance with Australian diesel emissions standards.

The $125 million that Volkswagen was ordered to pay is the highest total penalty order ever made by the Federal Court for contravening consumer law.

The car manufacturer admitted that, when it requested approval to supply and import more than 57 000 vehicles into Australia between 2011 and 2015, it did not disclose to the Australian government that its cars had two-mode software that hid the true nature of nitrogen oxide (NOx) emissions.

Cars were tested for emissions in 'Mode one' and Volkswagen admitted that when 'Mode one' was switched on for the purposes of this testing, the software caused its vehicles to produce lower NOx emissions. However, when the vehicles are driven on road conditions, they switch to 'Mode two' and produced higher NOx emissions.

Volkswagen engineers designed the two-mode software in 2006 and it was kept secret until it was discovered in 2015. This software essentially made their diesel vehicles operate in two modes: one that was designed to test well and another that operated when the vehicle was actually being driven.

The Federal Court found Volkswagen should have disclosed the information to the government when it sought approval to supply and import the vehicles into Australia. All new motor vehicles imported into Australia must comply with Australian standards for exhaust emissions. If these vehicles had been tested while operating in "Mode two", they would have exceeded the NOx limits allowed.

Volkswagen also admitted that it made false representations when applying for the vehicles to be published on the government's Green Vehicle Guide website. Their vehicles would not have received the ratings they did if the government was aware of the effect of the two-mode software.

8.3.4 Price discrimination

Ever tried to catch an Uber in peak hour and find that prices have increased? Well, this is because the app assumes people will pay the increased price. In 2017 Uber introduced a new fare system called 'route-based pricing' which charges customers based on what it predicts they're willing to pay. The company uses Dynamic Pricing, which determines what price to charge based on different variables such as location, time of day, traffic patterns and user history. The data are collected and an algorithm predicts the top price a user would be willing to pay.

One of the biggest predictors of whether or not consumers are going to be sensitive to a surge in price is how much battery they have left on their phone. People are more likely to accept an increased price if their phone is about to die because they need the ride home immediately and can't afford to wait to see if the price drops down again. Uber knows when its users' phone batteries are running low because the app switches into power-saving mode.

Price discrimination involves charging customers different prices for the same product or service based on what the seller thinks they can get the customer to agree to. Price discrimination is used based on the seller's belief that customers in certain groups can be asked to pay more or less based on certain demographics or on how they value the product or service in question.

price discrimination the setting of different prices for a product in separate markets

When the Trade Practices Act (now the Competition and Consumer Act) was originally introduced in 1974, it contained a prohibition on price discrimination. After numerous recommendations, it was eventually repealed. Price discrimination is no longer separately prohibited in Australia. However, in appropriate circumstances, price discrimination may contravene section 46 of the Act, which prohibits misuse of market power. The Competition and Consumer Act prohibits price discrimination if the discrimination could substantially reduce competition. This means that a business cannot give favoured treatment to some customers while denying it to others.

SNAPSHOT

Case study: Price discrimination

Price discrimination is legal in Australia where sellers will typically pick an opening price based on the likelihood that someone will pay it. We take a look at how you can get the best deal on airfares in the second part of a series exploring how technology is changing tourism.

Few things are more annoying than spending a large sum of money on a purchase, only to discover that someone else got the same thing for a lower price. This often happens with airfares. You go the same website, search the same airline, choose the same seat row and fare conditions, but you're offered a different price depending on when and where you do it. Why?

Often it's a result of price discrimination. This happens when a seller charges you what you're willing to pay. Of course, it also needs to be at a level that the seller is willing to accept.

When it comes to airfares, there are two levels of price discrimination, both driven by algorithms. First, there is price discrimination by the airline. Airline pricing is typically dynamic. That is, the prices are higher for more popular flights. Then there are intermediary platforms, such as travel agents or price comparison websites, which can introduce a further level of price discrimination.

How it works

Websites create cookies that record interactions between a user and a website. Often there are other tags and beacons created. From these, the website provider can obtain information, such as the browser type and the kind of device being used. Flight sales providers use this information to determine the price offered to a customer.

For example, if the same user checks a website multiple times for a flight at a specific time and on a particular date, the provider might assume this is the only time and date the user is interested in. It might respond by increasing the price offered, since it knows the travel decision is made. Alternatively, it might reduce the price to lock in the customer.

Clearing cookies or using a search engine that does not share search history (such as Duck Duck Go) can reduce this effect.

Price discrimination is legal

In Australia, like in many countries, price discrimination is legal. Sellers will typically pick an opening price based on the likelihood that someone will pay it. You see this happen at garage sales. Indeed, perfect price discrimination may mean that no two people pay the same price for the same product or service.

There are a few different ways of thinking about this

In one sense, this is just how markets operate. If both buyers and sellers operate in a self-interested manner, efficient outcomes arise that are better for everyone — it's the 'invisible hand'. Of course, this doesn't prevent people from feeling ripped off.

The market can also provide intermediaries. Instead of paying the airline's asking price, you could get an intermediary to buy the fare for you at a lower price. After all, you might not mind paying more than the minimum price available, provided that it's less than you thought was reasonable to start off with. In airline searches, this is the type of service offered by businesses such as SkyScanner.

Limitations

There is a legal issue which limits the use of price discrimination — such as if a seller engages in actual discrimination. If a website discriminates against an identifiable group, for example by charging more to women with an Italian surname, it would risk being in breach of the Racial Discrimination Act.

Another limitation is the potential for social media backlash against the practice, which could lead to reputational harm. In the retail space, Amazon issued a statement denying that it engages in price discrimination, after angry customers found they had been charged different prices for the same product. Platforms engaged specifically in airline sales haven't disclosed whether or not they engage in price discrimination, but they are likely at risk of similar customer backlash.

In the end, if you want to get a better deal on your airfare, the answer is still to shop around. And using comparison services, clearing cookies from your browser cache, and leaving as few breadcrumbs as possible is likely to yield the best deals.

Source: 'Why you might be paying more for your airfare than the person seated next to you', *The Conversation*, 9 October 2018.

8.3.5 Implied conditions

Implied conditions are the unspoken and unwritten terms of a contract. These conditions are assumed to exist regardless of whether they were especially mentioned or written into a contract.

With the introduction of the *Competition and Consumer Act 2010*, new national **consumer guarantees** were introduced. The consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL.

Under the ACL, when you buy products and services they come with automatic guarantees that they will work and do what you asked for. If you buy something that isn't right, you have consumer rights.

The following consumer guarantees on products and services apply.

- Products must be of **acceptable quality**, that is:
  - safe, lasting, with no faults
  - look acceptable
  - do all the things someone would normally expect them to do.

  Acceptable quality takes into account what would normally be expected for the type of product and cost.
- Products must also:
  - match descriptions made by the salesperson, on packaging and labels, and in promotions or advertising
  - match any demonstration model or sample you asked for
  - be fit for the purpose the business told you they would be fit for and for any purpose that you made known to the business before purchasing
  - not carry any hidden debts or extra charges
  - meet any extra promises made about performance, condition and quality, such as lifetime guarantees and money back offers
  - have spare parts and repair facilities available for a reasonable time after purchase unless you were told otherwise.
- Services must be:
  - provided with acceptable care and skill or technical knowledge and taking all necessary steps to avoid loss and damage
  - fit for the purpose or give the results that you and the business had agreed to
  - delivered within a reasonable time when there is no agreed end date.

implied conditions the unspoken and unwritten terms of a contract

consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL

acceptable quality products that are safe, lasting and with no faults, look acceptable and do all the things someone would normally expect them to do

Consumers can claim a remedy from the retailer if the products do not meet any one or more of the consumer guarantees. The retailer cannot refuse to help you by sending you to the manufacturer or importer.

Consumers can claim a remedy from the supplier if the services do not meet any of the consumer guarantees in relation to services. Remedies include cancelling a service and in some cases compensation for damages and loss.

FIGURE 8.9 In 2019 Jetstar Airways was ordered to pay $1.95 million in penalties for making false representations about consumer guarantee rights under the ACL. The Federal Court found that Jetstar made misleading statements on its website about the rights and remedies available to consumers under the ACL by claiming some fares were not refundable. However, where a flight is cancelled or significantly delayed, passengers may be entitled to a refund under the consumer guarantees.



8.3.6 Warranties

All businesses have certain obligations with regard to the products they sell. These obligations are designed to offer a degree of protection to the customer if the good is faulty or if the service is not carried out with due care and skill. One important obligation is to provide a warranty. A **warranty** is a promise made by a business that they will correct any defects in the goods that they produce or in the services that they deliver; that is, it is a promise to repair or replace faulty products. The use of warranties can be a good marketing tool. For example, if your business offers longer warranties than your competitors, then this will give customers the impression that your good is of superior quality.

warranty a promise made by a business that they will correct any defects in the goods they produce or services they deliver

In recent years, government legislation has made it necessary for businesses to state, clearly and simply, the terms and conditions of the warranty. A warranty assures the customer that the business has confidence in the quality of its product and will repair or replace any faulty items. A warranty can be used as an aggressive marketing tool if it includes superior options to those of a competitive product.

False or misleading statements concerning the existence, exclusion or certain conditions of the warranty are prohibited under the Competition and Consumer Act. In particular, the legislation clearly outlines the rights of consumers with regard to refunds and exchanges.

FIGURE 8.10 In 2020 Sony was ordered to pay $3.5 million in penalties for making false representations to four consumers who purchased faulty PlayStation games. Customer service representatives told them they were not entitled to a refund if the game had been downloaded, or if 14 days had passed since it was purchased. The Federal Court declared these representations were false as, under the ACL, people are entitled to a remedy if a product fails to meet a consumer guarantee and these rights do not expire after 14 days.



Refunds and exchanges (returns)

A business is required by law to offer a refund if the products provided:

- are faulty
- do not match the description or a sample
- fail to do the job they were supposed to do.

There is no obligation to offer a refund if the customer has simply changed their mind or found the same product at a cheaper price in another store, or if damage has occurred after the purchase was made.

It is also important that accurate signs regarding refunds and exchanges are displayed. Signs such as 'no refunds given' or 'no refunds on sale items' are meaningless. The Competition and Consumer Act gives consumers certain rights and remedies. A more accurate sign would read either 'no refunds given if you change your mind' or 'no refunds or exchanges unless your purchase is defective'.

on Resources

Weblinks Australian Competition and Consumer Commission (ACCC)
NSW Fair Trading 2

KEY IDEAS

- In 2011, a single, national consumer law — the Australian Consumer Law (ACL) — was introduced.
- *The Competition and Consumer Act 2010* protects consumers against undesirable business practices and prohibits various unfair (restrictive) business practices.
- The Competition and Consumer Act is administered and enforced by the Australian Competition and Consumer Commission (ACCC) and relevant state and territory consumer agencies.
- Breaches of the Competition and Consumer Act can result in the ACCC taking civil proceedings against the business or individual engaged in unconscionable conduct.
- Deceptive and misleading advertising is illegal under the Competition and Consumer Act. Businesses are not allowed to make statements or claims that are incorrect or likely to create a false impression.
- Price discrimination involves charging customers different prices for the same product or service based on what the seller thinks they can get the customer to agree to.
- The Australian Consumer Law introduced a single set of statutory consumer guarantees that replaced the previous system of implied conditions and warranties.
- Implied conditions are unspoken and/or unwritten terms of a contract.
- Consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL.
- A warranty is a promise to repair or replace faulty products.
- A business is required by law to offer a refund if the products provided:
  - are faulty
  - do not match the description or a sample
  - fail to do the job they were supposed to do.

8.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

8.3 Quick quiz on | **8.3 Exercise** | **8.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 3, 4, 5, 10, 11, 12, 14, 19	1, 6, 7, 8, 9, 13, 15, 17, 20, 21	16, 18, 22, 23

8.3 Exercise

Revision

1. **Why** should marketers be familiar with consumer laws?
2. **State** the two main aims of the Competition and Consumer Act.
3. **Recall** the federal government authority that administers and enforces the Competition and Consumer Act.
4. **Define** the term 'unconscionable conduct'.
5. **Summarise** the penalties that can be applied for breaches of the Competition and Consumer Act.
6. **Discuss** the advantages of the ACCC being able to issue on-the-spot infringement notices and public warning notices.
7. **Explain** why it is important for a marketer to comply with the consumer protection provisions of the Competition and Consumer Act.
8. In small groups:
   a. **discuss** whether the fines for business owners who breach the Competition and Consumer Act are adequate
   b. **propose** some alternative punishments.
   Select a spokesperson to present your responses to the rest of the class.
9. Select what you consider to be the two most serious examples of deceptive and misleading advertising. **Justify** your selection.
10. In each of the following examples, **state** whether there has been a breach of the Competition and Consumer Act. If so, **describe** the type of breach found.
    a. A company advertises a particular brand of television and states that it is at a cheaper price than a competitor. This statement is false.
    b. A company advertises jumpers and claims that they are made in Australia, when in fact they are made in Hong Kong.
    c. A company offers its customers a 10 per cent discount if they provide the names and addresses of five potential customers for the company.
    d. A company advertises that the special deal is for one week only, when in fact it plans to extend it to two months.
    e. A company advertises a motor vehicle as having low mileage, when in fact it has travelled 200 000 kilometres.
11. **State** under what circumstances price discrimination is considered a breach of the Competition and Consumer Act.
12. a. **Define** the term 'consumer guarantees'.
    b. **Identify** the features a product must possess to be considered of acceptable quality.
13. **Distinguish** between a warranty and a refund.
14. **Identify** under what circumstances a business is required to offer a refund.
15. **Why** are disagreements over warranties and refunds a common source of consumer complaints?
16. **Predict** how you would expect the ACCC to deal with each of the following situations:
    a. The only two garden maintenance businesses in a country town decide to merge and form one business.
    b. The owners of five petrol retailers along a major stretch of road met each week to determine how much they would all charge on each day of the week.

c. The manufacturer of a range of electrical goods provides all retail outlets selling its products with a list of recommended retail prices for each product, and refuses to supply them unless the outlets stick to those prices.
d. A branch of a major supermarket chain, located in the same shopping centre as an independent supermarket, consistently prices all its products five per cent below those of the independent supermarket. When the independent business lowers its prices to try to match its competitor, the major supermarket lowers its prices even further.

Read the case study 'Volkswagen fined for misleading customers' and answer questions 17 and 18.

17. **How** did Volkswagen mislead consumers?
18. **Assess** the impact this decision will have on different stakeholders of the company.

Read the case study 'Price discrimination' and answer questions 19 to 21.

19. **Outline** a situation in which price discrimination would be considered illegal.
20. **Explain** why airlines engage in price discrimination.
21. **Discuss** the use of price discrimination.

Extension

22. The media releases page of the ACCC website contains details of recent cases dealt with by the ACCC. Use the **Australian Competition and Consumer Commission (ACCC)** weblink to visit the site, navigate to the media releases page, select and read one story, and then answer the following:
    a. Identify the issue in question.
    b. **Evaluate** the decision, actions or recommendations the ACCC made in relation to the issue.
23. You have been employed as a business reporter with the local newspaper. Your editor has asked you to **create** a 300-word article about bait and switch advertising scams. The headline of your article is 'Don't get hooked — the bait and switch scam'. To help you commence your investigation, find case studies from NSW Fair Trading. Share your article with other class members.

8.3 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q4

Australian businesses are required by law to offer a refund if the product or service

A. does not match the description.
B. is no longer required by the customer.
C. is damaged by the customer after purchase.
D. is available at a competitor's business for a cheaper price.

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q14

Recently a business has removed one of its products from sale because it may contain toxic ingredients that could pose a health risk. What is the most likely influence on this marketing decision?

A. Competitive fairness
B. Product differentiation
C. Government legislation
D. Economic considerations

Question 3 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q8

A customer returns a chainsaw to the place of purchase as it does not cut branches.

On what basis must the business refund the cost of the chainsaw?

A. Implied conditions
B. Ethical considerations
C. Relationship marketing
D. Accuracy in advertising

Question 4 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q10

Salty Sunscreens sells the following sunscreens, both containing the same ingredients.



This is an example of which of the following?

A. Price leading
B. Price skimming
C. Price penetration
D. Price discrimination

Question 5 (4 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q22a

An Australian company sells educational toys for pre-school aged children.

Why is ethical behaviour important in the marketing of this business?

More exam questions are available in your learnON title.

8.4 Ethical influences

SYLLABUS LINK In this subtopic you will learn about ethical influences including truth and accuracy in advertising, good taste in advertising, products that may damage health, engaging in fair competition and sugging.

You will also learn to examine why ethical behaviour and government regulation are important in marketing.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

In marketing, as with all business practices, there are ethical and legal dilemmas involved. Although the many laws regulating marketing strategies prescribe legal standards, ethical standards are more difficult to define. Ethical behaviour refers to conduct that goes beyond the legal requirements. While some of the marketing strategies outlined below might be legal, they are still considered wrong or unethical.

8.4.1 Ethical criticisms of marketing

Critics of marketing argue that the industry does not always adopt ethical practices. They believe it often blurs the lines between what is ethically right and wrong. The main ethical criticisms of marketing include the following.

1. *Creation of needs — materialism.* **Materialism** is an individual's desire to constantly acquire possessions. Critics of product promotion feel that most businesses, especially large businesses, use sophisticated and powerful promotional strategies (particularly advertisements) to persuade and manipulate customers to buy whatever the firm wants to sell.
2. *Use of stereotyping.* The way groups of people are portrayed in advertisements does not always fully represent reality. Common examples of stereotyping in marketing include gender roles, racial stereotypes and stereotypes involving children. Stereotyping is very prevalent in advertising, with gender stereotypes being the most common. In most advertisements it tends to be the male who uses the power tools, or who watches sport with his mates. Females, on the other hand, are portrayed preparing meals, cleaning the house or caring for the children (see figure 8.11).

FIGURE 8.11 A study of advertisements in 2019, published in the *Journal of Consumer Culture*, found that advertising continues to reinforce gender stereotypes from the 1950s, with brands overwhelmingly portraying women seeking knowledge to cook, care and clean. This is despite shifts in attitudes that appear to share the role of caring within a family. In contrast, men were depicted as bumbling idiots in the rare occasions when they were shown using domestic products.



BizFACT

A Sofitel Hotels advertisement of a young couple in a hotel bed, both reading over breakfast looked innocent enough at first sight. However, it was the couple's choice of reading material that led to criticism and accusations of gender stereotyping. The man was reading the *Australian Financial Review* and the woman was looking through a Chanel coffee table book. Sofitel Brisbane apologised for any offence the ad caused and removed it from future campaigns.

BizFACT

The UK introduced laws in 2019 banning the depiction of men and women engaged in gender-stereotypical activities. One of the first television ads banned was for Philadelphia cream cheese which featured new dads eating at a restaurant where food circulated on a conveyor belt. While the dads were chatting, their babies were whisked away on the conveyer. The Advertising Standards Board banned the ad, stating that the harmful stereotype suggested men were incapable of caring for children.

3. *Use of sex to sell products.* There is often an overuse of sexual themes and connotations to sell products. Unrealistic images are portrayed as attainable. Advertisers use sex appeal to suggest to consumers that the product will increase the attractiveness or charm of the user. Although many people are sceptical of such claims, advertisements that use sex appeal can have subtle and persuasive impacts.
4. *Product placement.* The inclusion of advertising in entertainment is a promotion strategy referred to as **product placement**. Generally, the insertion of these products is subtle: an actor in a tv show or movie driving a Mercedes-Benz or speaking to someone on an iPhone; while at other times they are prominently displayed. Businesses are keen to use this promotional technique because it allows them to reach savvy, but advertisement-weary, consumers. However, critics of product placement argue that, because of its 'concealed' nature, this type of advertising blurs the line between what is advertising and what is entertainment.

materialism an individual's desire to constantly acquire possessions
product placement the inclusion of advertising in entertainment

BizFACT

James Bond films have a reputation for being shameless about product placement. Ever since the first movie, the successful franchise has relied on product placement to help fund each film. For example, BMW paid $3 million to have their as yet unreleased Z3 appear in *GoldenEye*. The placement was a success and saw a $240 million increase in sales after the car featured in this film.

5 *Invasion of privacy.* The recent growth in online advertising is raising a number of ethical issues, with the most serious being the tracking of web users and using this information to target them with advertisements. Collection of data in this way may breach consumer privacy. Presently, because most websites infer consent (the consumer agrees to their web searches being tracked unless the person opts out by ticking a box), many consumers are unaware that data is being collected on them. This behavioural data is collected and resold by data exchange companies and then used by businesses for target advertising purposes.

advertising a paid, non-personal message communicated through a mass medium

BizFACT

Many consumers overlook the fact that loyalty cards collect information on their individual buying habits. Do you really want your supermarket to know what you drink or how often? Or are you prepared to sacrifice this privacy for the benefits a reward program offers?

Ultimately, marketing managers should never forget that the business exists because of its customers. By satisfying customers, a business may operate profitably. Dishonest or unethical marketing strategies eventually drive customers away.

8.4.2 Truth and accuracy in advertising

Advertising can represent real ethical dilemmas. Exaggeration in advertising seems to be the rule of thumb. You need only to watch TV, listen to the radio or read magazines to see examples of over-the-top advertisements. Ethical businesses should ensure their advertising is truthful as they can be held morally responsible for misleading the public by using an untruth in an advertisement. For example, the use of terms such as 'special', 'great value', 'low fat', 'light' and 'once in a lifetime' can be interpreted in many different ways (see figure 8.12)

When consumers discover that advertisements are untrue or inaccurate, they may feel cheated and stop buying the product. They may also decide to complain to the relevant government agencies, in which case the bad publicity this generates can do untold long-term damage to a business's reputation.

The main unethical marketing practices include untruths due to concealed facts, exaggerated claims, vague statements and invasion of privacy.

FIGURE 8.12 When you look at product labels, you may think 'low fat', 'reduced fat', 'fat free' or 'light' are going to be healthier options, but quite the opposite is true. Just because a product is labelled in this way, doesn't mean that it's lower in calories. In fact, most low fat foods will add sugar, refined carbohydrates and chemicals to make up for the loss in taste. Many companies market their foods in this way to increase sales from people who think they can eat twice as much as before and not worry about gaining weight.



Untruths due to concealed facts

Many customers are aware that advertising takes liberties with the 'truth'; they do not perceive advertisements to be believable or honest. An advertised product may not make a consumer more successful, glamorous, sexy, happy, healthy or wealthy. However, the unethical practice of concealed facts — pieces of information purposely omitted from an advertisement — can severely harm the trust customers have in a product or a business.

Exaggerated claims

Puffery refers to exaggerated claims used for promotional purposes, that no reasonable person would take as factual. It is not misleading or deceptive to use exaggerated claims where the audience could not reasonably be misled. For example, many cafés advertise that they have 'the best coffee in town'; however a reasonable consumer is likely to recognise this as advertising puffery and is unlikely to rely on that statement or find it misleading. On the other hand, a brand of sparkling mineral water advertised the fact that the bubbles were 'natural' and bottled at source. This was shown to be misleading for the bubbles were added later during the bottling process.

puffery exaggerated claims used for promotional purposes, that no reasonable person would take as factual

SNAPSHOT

Case study: Puffery — can ice-cream really make you happy?

A billboard in New Zealand by Unilever Australasia's Streets brand was originally ordered to be taken down for being 'extremely irresponsible'. The advertisement showed three types of Streets ice-creams — Paddle Pop, Splice and Magnum — with the slogan 'ICE CREAM MAKES U HAPPY'.



But a local resident complained to the Advertising Standards Authority in New Zealand, calling the slogan socially irresponsible due to the obesity issues in the country. The complainant felt that ice-cream should not be promoted in a way to improve people's mood due to its high fat and sugar content. He was concerned about the impact the ad would have on children as well as their parents.

The Advertising Standards Authority initially upheld the complaint, even though Streets argued that the slogan was puffery and that no reasonable person could possibly treat the statement seriously or find it misleading. They felt that consumers would not interpret that the advertisement was claiming that eating ice-cream would provide nutritional value that is beneficial to their health. They felt the slogan represented the fact that eating ice-cream is an enjoyable experience.

The fact that the Advertising Standards Complaints Board ruled in favour of the complainant caused a great deal of controversy and so Streets appealed. The original decision was later reversed by the Advertising Standards Complaints Appeal Board. In its ruling, the Appeal Board found the advertisement was not in breach of the Advertising Standards Code, as the phrase was puffery and the ad did not undermine an individual's health and wellbeing.

BizFact

Fairfax Media's subsidiary Domain was sued by their main competitor REA Group (who runs Realestate.com.au) over their advertising campaign in 2016, which claimed that Domain was 'the highest rated property app' with the 'best property listings'. The judge in the Federal Court ruled that most of the content did not breach consumer laws and were entirely reasonable claims or just 'advertising puffery'.

Vague statements

Another type of unethical advertising practice involves the use of vague statements — statements using words so ambiguous that the consumer will assume the advertiser's intended message. These 'weasel' words — deliberately misleading or ambiguous language — are by their nature vague and allow the marketer to deny any intention to mislead or deceive. For example, *helps* is a common weasel word, as in 'helps fight against', 'helps restore' or 'helps to make you feel'. Although some marketers regard such statements as acceptable, others do not.

8.4.3 Good taste in advertising

What is considered to be in 'good taste' is highly subjective. Some consumers may regard an advertisement as offensive, while others might view it as inoffensive. There is usually common agreement as to what society considers acceptable and marketers must be aware of community sensitivities.

FIGURE 8.13 In 2019, Asaleo Care, which makes Libra period products, was criticised for an ad campaign that depicted some of the different ways young girls experience menstruation. The ad actually showed menstrual blood for the first time on Australian TV. Despite receiving over 600 complaints about the ad being in 'bad taste', Ad Standards dismissed them all and found the company did not breach any section of the industry's code of ethics.



However, as with many creative pursuits, and advertising is no exception, there are always some marketers wanting to push the boundaries.

Sportsbet, for instance, have created many tasteless ads that have offended viewers and generated a number of complaints. In fact, they have been found to have breached advertising standards on at least eight separate occasions. In 2018 their 'manscaping' ad set the record for the most complained-about advertisement in Ad Standards' 20-year history. The TV ad featured a man naked from the waist up 'manscaping' in the bathroom, with his leg on a chair shaving his genitals. A voiceover then yells loudly, causing the man to slip and hurt himself with the razor. Ad Standards received 793 complaints about the ad. The panel upheld the complaints, deeming that the ad breached section 2.4 of the AANA Code of Ethics, and the ad was removed from air.

BizFACT

Ultra Tune has topped Ad Standards' list of the most complained-about ads for the first half of 2020. A total of 309 complaints were made about one of Ultra Tune's advertisements, which featured Pamela Anderson and Warwick Capper and took on TV program *Baywatch*'s slow motion running trope. Complaints regarding exploitation, nudity, sexism and dangerous behaviour were dismissed by the Ad Standards community panel.

Within society, there is recognition of the growing role that mass media is playing in children's lives, and the fact that advertisers and marketers are now targeting children more than ever. One area of marketing to children that has received widespread publicity in Australia in recent years is the sexualisation of children in advertising. According to the Australia Institute, a leading progressive Australian think tank, sexualisation of children in the media 'leads to a range of risks for children'. In their report *Letting Children be Children*, they highlight that premature sexualisation of children can result in increased risk of depression, self-esteem and identity disorders, and premature sexual activity.

SNAPSHOT

Case study: KFC ad slammed for 'gender stereotypes' and 'sexist grooming of boys'



Fast-food giant KFC has been condemned for running an ad that objectifies women and plays on the sexist idea 'boys will be boys'.

The ad recently came to the attention of Collective Shout, a grassroots movement against the objectification of women, and was called out for its unhealthy stereotyping.

The 15-second commercial for KFC's Zinger popcorn box opens with a young woman checking her appearance in the reflection of a parked car window.

As she leans forward to adjust her cleavage, the window rolls down to reveal a very unhappy mother and two young boys staring open-mouthed.

The woman 'saves' herself from further embarrassment by saying 'Did someone say KFC?' — a catchphrase that is part of a series of ads showing people using KFC to get out of awkward situations.

According to Collective Shout spokesperson Melinda Liszewski, the ad 'grooms young boys' by playing on certain 'sexist' behavioural expectations.

'The ad is a play on tired old stereotypes, where young women are sexually objectified for the benefit of men — even young boys — and the males are helplessly transfixed when confronted with the opportunity to ogle a woman's body,' she said.

'Ads like this reinforce the false idea that we can't expect better from boys. It is another manifestation of the "boys will be boys" trope which presents an obstacle to challenging the sexist ideas that underpin gender inequality and violence against women.'

Ms Liszewski said the ad was also problematic in that it potentially contributed to reinforcing harmful 'gendered stereotypes' and cultivating unhealthy attitudes towards women.

'The research is solid: attitudes shape behaviour. A growing number of reports show how re-enforcing of gender stereotypes — including in advertising — contributes to a lesser view of women, resulting in their mistreatment,' she said.

The commercial, which is running during the Big Bash League coverage, is also featured on KFC's YouTube channel; however, comments have been turned off.

On social media, some who've seen the ad have been offended, expressing surprise the ad was given the green light by censors.

'How did this commercial pass the censors on prime time?' one person posted on Facebook.

On Twitter, following a post by a radio station in response to claims by Collective Shout, commenters didn't seem quite as bothered.

'They should apologise for the 3 pieces of overcooked tough-as-nails pieces I got last Friday … I won't be back in a hurry,' one said.

Another added: 'You forgot to add the word 'pathetic' in front of the word 'group'.'

In response to the claims, KFC Australia has said the ad wasn't meant to cause any offence, and it apologised to those who were upset.

'We apologise if anyone was offended by our latest commercial,' a KFC spokesperson said.

'Our intention was not to stereotype women and young boys in a negative light.'

Source: Emilia Mazza, 'KFC slammed for "gender stereotypes" and "sexist grooming of boys"', www.news.com.au, 21 January 2020.

BizFACT

The ACCC initiated proceedings against Heinz in relation to their Little Kids Shredz products alleging Heinz made false and misleading representations about these products being healthy options for young children despite the fact they contain over 60 per cent sugar. The ACCC alleges that the images on their packages of fresh fruit and vegetables, as well as statements such as '99% fruit and veg' and 'nutritious foods' represent to consumers that the products are of equivalent nutritional value to fruit and vegetables.

8.4.4 Products that may damage health

All consumer products supplied must be safe and meet consumer guarantees under the ACL. Businesses cannot sell banned products and must ensure that their products or product-related services comply with the relevant mandatory standards before they are offered for sale.

Consumer guarantees give people the right to a refund if a product is unsafe. Consumers can seek compensation for damages and loss caused by a safety defect in products. Generally, the manufacturer of the products is liable, but if other suppliers, such as retailers, cannot identify the manufacturer, they may be held liable for the damages.

There are also two mandatory notification requirements under the ACL. If there is:

- a risk that a product will or may cause injury, it must be recalled
- awareness of a death, serious injury or illness associated with a product a business supplies, they must report it within two days, which is known as mandatory reporting.

FIGURE 8.14 The Parents' Voice Fame & Shame Awards raise awareness of marketing techniques the food industry uses to promote unhealthy foods and drinks to children. In 2019 several food manufacturers were given a red card: Kellogg's won the pester power award for using appealing packaging targeting children for their highly processed unhealthy options; PepsiCo was shamed for their billboards that bombard kids with unhealthy food advertising; and McDonalds was shamed for their Happy Meal social media ads and apps.



The marketing of junk food, which is often portrayed as an essential part of a balanced diet, is an area presently being criticised by nutritionists and health advocates, especially as childhood obesity rates approach epidemic proportions (see figure 8.14).

BizFACT

In 2019 the Queensland Government banned outdoor advertising for junk food at government-owned sites as part of an effort to curb an obesity crisis. These marketing restrictions will affect more than 2000 outdoor advertising spaces, including billboards, bus stops and train stations. London implemented similar restrictions the same year when junk food advertising was banned on the entire Transport for London network.

Nutritionists argue that the self-regulatory advertising codes, such as the *Responsible Children's Marketing Initiative* and the *Australian Quick Service Restaurant Industry Initiative for Responsible Advertising and Marketing to Children* (which allow fast-food companies to advertise certain products in children's television programs only if they meet specific nutritional guidelines) aimed at reducing junk-food marketing, are not working (see the following case study). For example, only advertisements screened during designated children's programs or 'designed for children' are covered by the code of nutritional guidelines. It does not, however, cover television programs popular with children, such as *Neighbours* and *Home & Away*, and fast-food companies.

As well as industry established codes, the federal government sets restrictions on children's advertising. In Australia, no advertising is allowed during programs for pre-school children.

The proliferation of smartphone apps and social-networking sites such as Facebook, Instagram, Twitter and Snapchat provide marketers with new and largely unregulated ways of advertising junk food to children. This form of advertising raises new ethical issues.

BizFACT

In 2013, the Center for Environmental Health (in America) released test results showing that Pepsi intentionally covered up the presence of high levels of 4-Mel (a known carcinogen) in its soft drinks. A settlement in a class action lawsuit against Pepsi gained approval in California. As part of the proposed settlement, Pepsi agreed to ensure its 4-Mel levels do not exceed 100 parts per billion and to test the soda using specific protocols.

SNAPSHOT

Case study: Junk food advertisers put profits before children's health — and we let them



For the first time in history, Australian children could live shorter lives than their parents. The reason? High rates of excess weight and obesity.

Despite mounting evidence that junk food marketing is a big part of the problem, a report reveals that Australian governments are failing to step in and protect our children.

In fact, Australia's already weak system of self-regulation to protect children from unhealthy food marketing — including advertisements on TV, radio and digital platforms — has gone backwards.

Self-regulation: nothing but a charade

The Obesity Policy Coalition (OPC) report, End the Charade!, shows how the self-regulation of junk food marketing in Australia is simply not working.

Profit-hungry food advertisers exploit the loopholes that exist in already weak codes and use sneaky tactics so they can bombard children with junk food advertising.

The Australian Food and Grocery Council's (AFGC) codes, known as the Responsible Children's Marketing Initiative (RCMI) and the Quick Service Restaurant Initiative (QSRI), are 'an industry framework to make sure only healthier products are promoted directly to children'.

Ironically, signing up to these codes allows big food companies to appear socially responsible — even when their sole motivation is maximising profit, at the expense of children's health.

The report found that since an initial investigation by the OPC in 2012 the system has been relaxed even further. Examples include:

- A looser definition of healthy food that fails to stop Kellogg's categorising of Coco Pops as a 'healthier dietary choice' and therefore appropriate for marketing to children.
- A weakened interpretation of advertising 'directly targeted to children' allowing Nestlé to use fairytale imagery to advertise Wonka Cookie Creamery chocolate, arguing it was 'designed to appeal to an adult's sense of nostalgia for childhood'.
- A slow and complex system in which the Advertising Standards Board failed to consider a complaint about Peter's 'Zombie Guts' and 'Zombie Snot' icy-poles because the ad campaign had ended by the time it received the complaint.

Food manufacturers' influence extends well beyond individual advertisements. It relies on huge volumes and placement within a range of platforms, such as websites, mobile phone apps, interactive games, billboards at bus stops and promotions in supermarkets. This ensures junk food advertising is wallpaper in our children's lives.

Given that around 40 per cent of what Australian school-aged children eat is unhealthy food, the millions of dollars companies spend to create demand for their products is a marketing success and public health failure.

Advertising influences food choices, now and in future

Extensive research has found that unhealthy food advertising influences what children want to eat and what they do eat. This also creates pester power and undermines efforts by parents, schools and communities to encourage healthy habits.

Children are vulnerable consumers and are likely to have reduced capacity to understand the commercial and persuasive intent behind advertising messages. In targeting children through fun advertisements and engaging characters, food companies are able to build positive brand associations that can stay with them throughout their adult life.

Restricting junk food marketing to children is acknowledged by peak health bodies including the World Health Organization (WHO) as an important and necessary step to help improve children's diets and slow obesity rates in Australia.

Government-led regulation urgently needed

Research from here and overseas has shown that self-regulation of unhealthy food marketing is ineffective to reduce the amount of food advertising and promotion that children see. To reduce children's exposure to unhealthy food marketing, we urgently need government-led action.

As a first step, the Australian Communications and Media Authority should monitor and measure children's exposure to unhealthy food advertising on television.

The federal government should then introduce comprehensive regulations or, at the very least, instruct broadcasting, advertising and food industries on how to strengthen their existing approaches.

Amendments should also be made to the advertising codes or regulations to:

- clearly define key terms, including 'unhealthy food', 'unhealthy food marketing', 'children' and 'directed to children'
- consistently and transparently define 'unhealthy food' in accordance with government and scientific guidelines
- expand their scope to apply to all forms, media and locations of marketing of unhealthy food (including brand marketing) that is directed to, or appeals to, children
- restrict all unhealthy food marketing on television during times when large numbers of children are likely to be watching (weekdays 6–9 am and 4–9 pm, and weekends and school holidays 6 am–12 pm and 4–9 pm)
- ensure compliance is regularly monitored.

The food and advertising industries seem primarily motivated to create an appearance of corporate social responsibility and ward off tighter government regulation. Only through significant improvements led by government will children be protected from predatory junk food marketers exploiting their vulnerabilities.

Industry has had a chance to show that they can act responsibly and our scrutiny has shown they have failed miserably. Now government leadership is necessary to support parents and put children's health first.

Source: Jane Martin, 'Junk food advertisers put profits before children's health — and we let them', *The Conversation*, 1 December 2015.

BizFACT

On average, children spend 32 hours a week on screens at home. During peak TV viewing times, children are exposed to 3 unhealthy food advertisements an hour and 44% of food advertisements are for unhealthy foods.

BizFACT

The Australian Medical Association (AMA) urged the government to introduce a sugar tax as part of their positioning paper on the country's nutrition. They recommended the government implement a tax policy to force up the prices of sugar-sweetened drinks to change behaviour - to make us drink them less, or even, not at all.

8.4.5 Engaging in fair competition

Competition in the marketplace is a fact of life. Businesses compete against each other to attract the greatest number of customers. Those businesses that compete successfully will usually increase their sales revenue and profit.

FIGURE 8.15 In 2019 the Federal Court ordered the airline Garuda Indonesia to pay a $19 million penalty for colluding on fees and surcharges for air freight services. The ACCC launched legal action against a global air cargo cartel involving 14 other airlines including Qantas, Air New Zealad and Cathay Pacific, for fixing the price of certain charges and fees on flights into Australia. The other airlines combined were penalised $132.5 million.



The amount of competition in the marketplace can be intense so there is a temptation for some businesses to engage in unfair marketing strategies. For example, businesses should be fair when referring to their competitors in their marketing and their advertisements should not insult or make false assertions towards their competitors.

The *Competition and Consumer Act 2010* requires businesses to compete fairly and contains provisions relating to fair competition. Part IV of the Act aims to deter certain anti-competitive behaviour that limits or prevents competition.

Some examples of anti-competitive conduct that is prohibited include the following.

- *Cartel conduct.* A cartel exists if two or more businesses that would normally be in competition with each other agree to act together. The Act prohibits businesses from making agreements with competitors to fix prices, rig bids, share markets or restrict outputs. These types of agreements are designed to increase the profits of the cartel members while putting other companies out of business. For example, it is illegal for businesses to communicate before lodging bids and agree among themselves who will win and at what price (rigging bids). It is illegal for two businesses in competition with each other to agree to set identical prices for their products (price fixing).

- *Anti-competitive agreements.* Contracts or arrangements containing provisions that substantially lessen competition in a market are prohibited.
- *Misuse of market power.* The Act prohibits businesses with a substantial degree of market power from engaging in conduct that has the purpose, or has or is likely to have the effect of substantially lessening competition in a market. For example, a business should not take advantage of its power to damage or get rid of a competitor, prevent anyone from competing in a market or prevent another competitor from entering a market.
- *Exclusive dealing.* This occurs when one person or business trades with another and then imposes restrictions on them; for example, if a hair products supplier will only sell to a hairdresser on the condition that the hairdresser does not purchase hair products from any other supplier. This can be legal in some circumstances if it is not seen to lessen competition in the market for the products in question. For example, McDonald's sells Coca-Cola products but not Pepsi, and they are permitted to do so. This is because KFC sells Pepsi and not Coke, so the overall market for soft drinks is still competitive. Businesses that wish to enter such an arrangement must notify the ACCC of the proposed agreement. The ACCC will then examine the details before either approving or disallowing the arrangement.
- *Resale price maintenance.* This occurs if a supplier sets the price at which retailers will sell the products they supply them. Suppliers can recommend a retail price for the sale of their goods, but it is illegal to attempt to force a retailer to sell at that price. Retailers must be free to compete on price with other retailers selling the same products. It is also illegal to set a minimum price that sellers must not sell below, or to force a retailer not to discount goods. On the other hand, it is quite legal for a supplier to set a maximum price for its products. This is to prevent any retailer that has no competitors in a particular location from unfairly overcharging customers.
- *Mergers and acquisitions*. While most mergers or acquisitions are legal and can be very beneficial, the Competition and Consumer Act prohibits any merger or acquisition that would have the effect, or be likely to have the effect, of substantially reducing competition in that particular market. The Act prohibits mergers and acquisitions between two or more businesses if this results in competition being substantially reduced. Businesses proposing a merger or acquisition can ask the ACCC for permission. The ACCC may permit this, but only if it will not substantially limit competition. If businesses proceed without seeking permission, the ACCC can investigate and will have the power to take action against the businesses if it finds that the merger or acquisition has substantially limited competition.

BizFACT

A few years ago, Woolworths was fined $7 million for attempting to prevent some restaurants and bars from selling packaged liquor in competition with its own liquor outlets. When these other businesses applied for liquor licences, Woolworths lodged objections with the government licensing authority. They then proposed to withdraw the objections if the other businesses agreed not to sell take-away alcohol products to their customers. A court found that Woolworths was in breach of the law for attempting to misuse its market power to restrict the operations of competing liquor outlets.

BizFACT

In 2020, the Federal Court dismissed an attempt by the ACCC to block a plan for Vodafone to merge with TPG on the grounds that it could substantially lessen competition in the mobile telecommunications market. The ACCC opposed the merger because it considered that TPG could become an innovative and disruptive competitor and that their presence would result in stronger competition and cheaper services. The Federal Court allowed the merger to proceed.

FIGURE 8.16 Mergers and acquisitions have occurred regularly in the banking industry. In 2008, Bendigo Bank and Adelaide Bank merged; the Commonwealth Bank took over Bankwest; and Westpac acquired St George Bank. However, the big four banks, ANZ, NAB, Westpac and the Commonwealth Bank are specifically banned from merging with each other as this would result in a big reduction in competition.



8.4.6 Sugging

Have you ever been approached by someone in a shopping centre and asked to complete a short survey? Perhaps you have been contacted by telephone and surveyed about a particular product only to discover the person was really trying to sell you something? If so, then you have just been 'sugged'. **Sugging**, selling under the guise of a survey, is a sales technique disguised as market research.

Although this technique is not illegal, it does raise several ethical issues, including invasion of privacy and deception.

Sugging also has long-term negative consequences for market research. The cooperation of consumers is becoming more difficult with response rates to surveys and questionnaires steadily declining. Current indications are that about one-third of individuals now refuse to participate in telephone, online and personal surveys because of suspicion that the survey is really a case of sugging.

sugging 'selling under the guise of a survey'; a sales technique disguised as market research

BizFACT

Three questions you could ask to determine if a call is a legitimate survey are:
1. Are you selling anything?
2. Will my participation in this survey result in anyone contacting me to try to sell me anything?
3. Will my name and personal information be sold or provided to anyone who will contact me to try to sell me anything?

8.4.7 A marketing code of ethics

In 2012 a code of ethics was developed for marketers in relation to advertising — the Australian Association of National Advertisers (AANA) Code of Ethics 2012. The objectives of this Code of Ethics are to set standards, and ensure that advertisements and other forms of marketing communications are legal, decent and truthful and that they have been prepared with a sense of obligation to the consumer and society and a sense of fairness and responsibility to competitors. If consumers feel that an advertisement breaches the code, they can make a complaint to Ad Standards. The role of Ad Standards is to ensure that the Code of Ethics is followed.

Ad Standards manages the complaint resolution process of the advertising **self-regulation** system. Consumers can complain to Ad Standards who will then consider and assess any complaints in light of the codes before they make a submission to the Ad Standards Community Panel for determination. The advertiser is then notified of the complaint and is requested to provide a written response. The Community Panel reaches its decision by way of simple majority and can make one of two determinations:

- Dismissed complaints — a complaint is dismissed if the Community Panel determines there is no breach of a code or initiative.
- Upheld complaints — a complaint is upheld if the Community Panel determines there is a breach of a code or initiative and the advertiser is then requested to remove or amend the offending advertisement as soon as possible.

Many consumer organisations argue that a self-regulatory system for advertising standards is ineffective because Ad Standards lacks the authority to enforce the Code of Ethics. The critics believe that advertising standards should be regulated by the government, otherwise there may be a temptation by marketers to ignore industry-established guidelines.

BizFACT

In 2020 Ad Standards banned an advertisement for AHM health insurance featuring former Australian cricketing legend Andrew Symonds after numerous complaints about it were received. The ad depicts Symonds shoulder charging a production assistant, re-enacting an infamous moment in cricket history when Symonds decked a streaker who ran onto the pitch. The ad promoted AHM's chiropractor cover. Ad Standards said the ad depicts an act of assault in the workplace and glorifies unprovoked violence and bullying.

8.4.8 Examine why ethical behaviour and government regulation are important in marketing

Why is ethical behaviour important? The benefits of ethical behaviour are becoming increasingly evident and include the following.

- Ethical behaviour can lead to significant marketing and business opportunities. Ethical businesses enjoy regular publicity in the media, in journals and on the internet. This creates a positive image of the business.

self-regulation a system by which a business or industry controls its own activities rather than being publicly regulated by an outside organisation such as the government

- Ethical behaviour can attract customers to the business and increase customer loyalty. Customers will reward ethical businesses by purchasing more of their products. An increasing number of consumers are becoming more ethically minded and will actively purchase products or brands that they believe are ethical. This in turn leads to increasing sales and profits.
- It can have a positive effect on employment relations. Productivity, staff retention and absenteeism rates can improve as more employees will want to stay with the business. It will also enable the business to attract the most talented employees.
- It may attract more investors and be more appealing to stakeholders.
- Ethical behaviour can improve a business's reputation.

Customers eventually find out which businesses are acting ethically and which are not. Unethical behaviour, by comparison, will go against the company's image and may damage a business's reputation. Customers may react and boycott certain products if they learn that the business is acting unethically. There have been many examples of businesses who have acted unethically, leading to negative publicity and a refusal by certain customers to purchase products from them. Unethical behaviour may also make the business less appealing to stakeholders.

Why is government regulation important? Government regulations relating to marketing are important as they:

- protect consumers
- protect businesses
- increase consumer trust and confidence in businesses. This results in people buying more products, which is good for the economy
- promote and stimulate competition and fair trade, which benefits consumers, businesses and the community in general
- encourage businesses to do the right thing
- promote competition and create a more equal playing field.

on Resources

Weblinks Australian Association of National Advertisers (AANA)
Australian Competition and Consumer Commission (ACCC) and advertising

KEY IDEAS

- Critics of marketing argue that the industry does not always adopt ethical practices and that it sometimes blurs the lines between what is ethically right and wrong.
- The main ethical criticisms include:
  - creation of needs — materialism
  - use of stereotyping
  - use of sex to sell products
  - product placement
  - invasion of privacy.
- Dishonest or unethical marketing practices ultimately drive customers away.
- Unethical marketing practices relating to truth and accuracy in advertising can range from:
  - untruths due to concealed facts
  - exaggerated claims — puffery
  - vague statements.
- Marketers should ensure that their advertisements are not offensive and are in good taste.
- Marketers have been heavily criticised by consumer and health groups for promoting products that damage health, especially junk food.
- There may be a temptation for marketers to engage in strategies that can limit or prevent competition. The *Competition and Consumer Act 2010* requires businesses to engage in fair competition.
- Sugging — selling under the guise of a survey — is not illegal, but it raises several ethical issues including invasion of privacy and deception.

- The Australian Association of National Advertisers (AANA) Code of Ethics 2012 was developed to regulate marketing.
- The role of Ad Standards is to manage the complaint resolution process of the advertising self-regulation system to ensure that ethical advertising standards are followed.
- Ethical behaviour and complying with government regulations are important in marketing as they protect consumers and can lead to significant marketing and business opportunities.

8.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

8.4 Quick quiz on	8.4 Exercise	8.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 14, 19, 23, 25	2, 3, 4, 5, 6, 7, 8, 9, 12, 13, 15, 16, 17, 18, 19, 20, 21, 24, 26, 27, 28, 31, 32, 33	10, 11, 22, 29, 30

8.4 Exercise

Revision

1. **Define** the term 'materialism'.
2. As a class, **discuss** whether advertising creates unrealistic expectations that many consumers can never attain. Record the main points on the board. Write a paragraph in your notebook summarising the points recorded.
3. **Discuss** whether you think advertising:
   a. leads or reflects the change in gender roles
   b. could be criticised for over-emphasising sex to sell products.
4. **Why** are businesses keen to use product placement?
5. **Justify** whether you consider product placement an ethical or unethical marketing strategy. **Compare** your answer with those of other class members.
6. **Demonstrate** how the following advertising strategies may mislead consumers.
   a. 'Before' and 'after' advertisements
   b. Puffery
   c. 'Weasel' words
7. **Propose** three reasons why the collection of consumer behavioural data, by tracking web users, could be considered unethical.
8. In a recent survey of 350 Australian and overseas marketing managers, 64 per cent responded 'yes' to the question: 'Is it reasonable behaviour to bend the law if you do not actually break it?' **Propose** how you would answer this question.
9. Even though some ads that are considered unethical are forced to be removed, they create a great deal of attention — which is one of the main purposes of advertising. **Justify** whether you agree or disagree with this statement.
10. a. Using the format shown in the following table,examine five advertisements and record your observations. Choose two advertisements that you think were the most effective. Justify your selection.

Name of company	Product	Marketing strategy used	Effectiveness rating 1–5

b. **Determine** whether any of the advertisements you viewed were unethical. Give reasons for your answer.

11. In small groups, use the brainstorm technique to **critically analyse** the ethical issues involved in: advertising to young children during morning television programs using sexual overtones and imagery in advertisements.
12. 'Digital advertising to children should remain unregulated and allow the fast-food industry to develop its own set of guidelines.' **Discuss**.
13. **Construct** a concept map summarising examples of anti-competitive practices.
14. Find the Australian Association of National Advertisers Code of Ethics.
    a. **Clarify** the objectives of the Code of Ethics.
    b. **Identify** the four AANA Codes.
15. **Why** are ethical behaviour and government regulation important in marketing?
16. **Discuss** the impact of marketing that is considered unethical.
17. **Why** is competition between businesses beneficial for consumers?

Read the case study 'Puffery — can ice-cream really make you happy?' and answer questions 18 to 20.

18. **Why** were complaints made about the ad?
19. **State** whether or not you agree with the original decision of the Advertising Standards Complaint Board Justify your answer.
20. **Examine** whether puffery should be illegal.

Read the case study 'KFC ad slammed for 'gender stereotypes' and 'sexist grooming of boys" and answer questions 21 to 24.

21. **Explain** why this ad has been criticised.
22. **Assess** the impact this ad will have on KFC.
23. **State** whether you think KFC should have been forced to remove the ad. Justify your decision.
24. **Recommend** what actions consumers offended by this ad could take.

Read the case study 'Junk food advertisers put profits before children's health — and we let them' and answer questions 25 to 28.

25. **Outline** some flaws of the current self-regulatory system of junk food marketing.
26. **Explain** how unhealthy food advertising can have a negative impact on children.
27. **Why** is government-led regulation needed?
28. **Recommend** one amendment that should be made to the current advertising codes.

Extension

29. Examine what advertising standards must be met before an advertisement can be aired on television. Discuss why we have advertising standards and **determine** whether there are any areas where advertising certain types of products should be subject to stricter regulation.
30. You have been asked by your manager to place a 'special' sign on a number of items, but the price is not to be lowered. **Assess** whether this is an ethical or unethical practice. As an employee, **determine** what you could do. Compare your answer with those of other class members.
31. Research the Australian Competition and Consumer Commission (ACCC) to answer the following questions.
    a. Outline what information the ACCC provides about advertising.
    b. **How** does knowledge of this information influence marketing promotion practices?
32. **Discuss** whether a marketing manager should refuse to produce a product that could have harmful side effects, even though consumers are demanding the product. **Compare** your answer with those of other class members.
33. If you were the marketing manager for a food company account, **investigate** which you would prefer: government regulation of food additives or a voluntary industry code. In your answer provide advantages and disadvantages for each alternative.

8.4 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q7

Which term refers to a sales technique disguised as market research?

A. Sugging
B. Telemarketing
C. Implied conditions
D. Engaging in fair competition

Question 2 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q11

Sam is asked by a company to participate in a survey on home security. After a few questions, she is asked if she would like to purchase a burglar alarm from the company.

What strategy is the company using?

A. Sugging, which is illegal
B. Sugging, which is legal but may be unethical
C. Misleading and deceptive advertising, which is illegal
D. Misleading and deceptive advertising, which is legal but may be unethical

Question 3 (20 marks)

Source: HSC 2012 Business Studies Exam, Section IV, Q26

Why are ethical behaviour and government regulation important in marketing?

Question 4 (20 marks)

Source: Adapted from HSC 2011 Business Studies Exam, Section III, Q26

Rushworth Pty Ltd is a manufacturer of football jerseys that supplies to a range of schools and sports teams. It has 200 employees and uses a hierarchical organisational structure. Management is concerned about negative comments in the media about some legal and ethical aspects of its marketing.

The managers have also provided the following information:

	2009	2010
Staff turnover	5%	15%
Absenteeism	8%	19%
Overdraft	$15 000	$70 000
Accounts receivable	$25 000	$70 000
Sales	$200 000	$200 000

You have been employed as a consultant by Rushworth Pty Ltd to prepare a report to the managers. In your report you should:

- describe TWO possible legal and/or ethical influences on marketing that Rushworth Pty Ltd may need to address.
- recommend TWO strategies that could be used to address ONE financial issue shown in the data.

Question 5 (6 marks)

Source: Adapted from HSC 2010 Business Studies Exam, Section II, Q23b

ENERGO is a new fruit-based drink that contains high levels of caffeine and sugar. The manufacturer would like the drink to be seen as a healthy product. Market research results show that 75% of 8–12 year olds would like ENERGO sold at their school canteen. Analyse how ONE consumer law or ONE ethical influence on marketing might impact ENERGO.

More exam questions are available in your learnON title.

8.5 Review

8.5.1 Summary

Factors influencing customer choice

- Marketers examine the behaviour of customers (consumers) to understand what influences customer choice.
- Customer choice is influenced by four main factors.
  1. Psychological:
     - influences within an individual that affect his or her buying behaviour
     - psychological factors include the buyer's perceptions, motives, attitudes, personality and self-image, and learning.
  2. Sociocultural:
     - influences exerted by other people and groups that affect an individual's buying behaviour
     - sociocultural factors include the buyer's social class, culture and subculture, family role, and peer groups.
  3. Economic:
     - economic forces that influence a business's capacity to compete, and a customer's willingness and ability to spend
     - the level of economic activity fluctuates from boom to recession.
  4. Government:
     - policies that directly or indirectly influence business activity and customers' spending habits
     - laws such as the *Competition and Consumer Act 2010* (Cwlth), *Sale of Goods Act 1923* (NSW) and the *Fair Trading Act 1987* (NSW) that influence marketing decisions.

Consumer laws

- In 2011, a single, national consumer law — the Australian Consumer Law (ACL) — was introduced.
- *The Competition and Consumer Act 2010* protects consumers against undesirable business practices and prohibits various unfair (restrictive) business practices.
- The Competition and Consumer Act is administered and enforced by the Australian Competition and Consumer Commission (ACCC) and relevant state and territory consumer agencies.
- Breaches of the Competition and Consumer Act can result in the ACCC taking civil proceedings against the business or individual engaged in unconscionable conduct.
- Deceptive and misleading advertising is illegal under the Competition and Consumer Act. Businesses are not allowed to make statements or claims that are incorrect or likely to create a false impression.
- Price discrimination involves charging customers different prices for the same product or service based on what the seller thinks they can get the customer to agree to.
- The Australian Consumer Law introduced a single set of statutory consumer guarantees that replaced the previous system of implied conditions and warranties.
- Implied conditions are unspoken and/or unwritten terms of a contract.
- Consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL.
- A warranty is a promise to repair or replace faulty products.
- A business is required by law to offer a refund if the products provided: are faulty, do not match the description or a sample, or fail to do the job they were supposed to do.

Ethical influences

- Critics of marketing argue that the industry does not always adopt ethical practices and that it sometimes blurs the lines between what is ethically right and wrong.
- The main ethical criticisms include:
  - creation of needs — materialism
  - use of stereotyping
  - use of sex to sell products

  - product placement
  - invasion of privacy.
- Dishonest or unethical marketing practices ultimately drive customers away.
- Unethical marketing practices relating to truth and accuracy in advertising can range from:
  - untruths due to concealed facts
  - exaggerated claims — puffery
  - vague statements.
- Marketers should ensure that their advertisements are not offensive and are in good taste.
- Marketers have been heavily criticised by consumer and health groups for promoting products that damage health, especially junk food.
- There may be a temptation for marketers to engage in strategies that can limit or prevent competition. The *Competition and Consumer Act 2010* requires businesses to engage in fair competition.
- Sugging — selling under the guise of a survey — is not illegal, but it raises several ethical issues including invasion of privacy and deception.
- The Australian Association of National Advertisers (AANA) Code of Ethics 2012 was developed to regulate marketing.
- The role of Ad Standards is to manage the complaint resolution process of the advertising self-regulation system to ensure that ethical advertising standards are followed.
- Ethical behaviour and complying with government regulations is important in marketing as it protects consumers and can lead to significant marketing and business opportunities.

8.5.2 Key terms

acceptable quality products that are safe, lasting and with no faults, look acceptable and do all the things someone would normally expect them to do
advertising a paid, non-personal message communicated through a mass medium
attitude a person's overall feeling about an object or activity
brand loyalty when a favourable attitude towards a single brand results in repeat sales over time
consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL
customer choice (buying behaviour) the decisions and actions of customers when they search for, evaluate, select and purchase goods and services
implied conditions the unspoken and unwritten terms of a contract
learning changes in an individual's behaviour caused by information and experiences
materialism an individual's desire to constantly acquire possessions
motive an individual's reason for doing something
perception the process through which people select, organise and interpret information to create meaning
personality the collection of all the behaviours and characteristics that make up an individual
price discrimination the setting of different prices for a product in separate markets
product placement the inclusion of advertising in entertainment
psychological factors influences within an individual that affect his or her buying behaviour
puffery exaggerated claims used for promotional purposes, that no reasonable person would take as factual
reference or **peer group** a group of people with whom a person closely identifies, adopting their attitudes, values and beliefs
self-image how a person views himself or herself
self-regulation a system by which a business or industry controls its own activities rather than being publicly regulated by an outside organisation such as the government
social class or **socioeconomic status** a person's relative rank in society, based on his or her education, income or occupation
sociocultural influences forces exerted by other people and groups that affect an individual's buying behaviour
sugging 'selling under the guise of a survey'; a sales technique disguised as market research
unconscionable conduct any practice by a business that is not reasonable and often illegal
warranty a promise made by a business that they will correct any defects in the goods they produce or services they deliver

Resources

Digital documents	Key terms glossary (doc-35575) Chapter crossword (doc-36215)
Interactivity	Chapter crossword (int-7159)
Exam question booklet	Chapter 8 Exam question booklet (eqb-0030)

8.5 Activities

learnON

To answer questions and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. **A downloadable solutions** file is also available in the Resources tab.

Exercise 1: Multiple choice questions

1. Which of the following are *not* significant influences on marketing?
   - **A.** Consumer laws such as legislation governing warranties
   - **B.** Implementating, monitoring and controlling the marketing plan
   - **C.** Consumer choice factors; for example, economic influences on consumer buying behaviour
   - **D.** Ethical factors like truth, accuracy and good taste in advertising
2. Which of the following both influence customer choice?
   - **A.** Psychological factors and implied conditions
   - **B.** Implied conditions and sociocultural factors
   - **C.** Sociocultural factors and economic factors
   - **D.** Economic factors and warranties
3. Which of the following would occur during a recession?
   - **A.** Incomes fall
   - **B.** Decreasing unemployment
   - **C.** Increase in consumer spending
   - **D.** Customers optimistic about the future
4. The marketing manager of plant store Bonza Bonsais is concerned that customers see bonsai trees as unfashionable and only for serious gardening enthusiasts. To address this, their marketing plan has been adjusted to show bonsai trees as trendy plants. What is this strategy attempting to change?
   - **A.** Customer perception
   - **B.** Customer motives
   - **C.** Customer attitude
   - **D.** Customer personality and self-image
5. A yoghurt company advertised their yoghurt as '98% fat free'. Independent tests revealed that the fat content is actually higher than this. Which influence on marketing is this an example of?
   - **A.** Sugging
   - **B.** Implied conditions
   - **C.** Engaging in fair competition
   - **D.** Deceptive and misleading advertising
6. After seeing his best friend change shoe brands, David has asked his parents to buy the same brand shoe as his friend. Which factor influencing customer choice is this an example of?
   - **A.** Economic
   - **B.** Sociocultural
   - **C.** Psychological
   - **D.** Government
7. Which of the following would be an example of price discrimination?
   - **A.** An optometrist offers discounts to pensioners
   - **B.** Kmart and Target each sell the same scooter but at different prices
   - **C.** A computer manufacturer sells their computers to different retailers at different prices
   - **D.** An ice-cream store sells ice cream to consumers located in different geographic areas at different prices

8. The consumer guarantee that products must be of acceptable quality is an example of which influence on marketing?
   A. Warranty
   B. Implied conditions
   C. Good taste in advertising
   D. Engaging in fair competition

9. Who enforces the Australian Consumer Law?
   A. ASIC
   B. ACCC
   C. Ad Standards
   D. The Competition and Consumer Act

10. An international clothing manufacturer created an ad campaign that was banned due to the sexualisation of the ads, which were aimed at teens. Which ethical influence on marketing would this be an example of?
   A. Good taste
   B. Truth and accuracy
   C. Engaging in fair competition
   D. Deceptive and misleading advertising

Exercise 2: Exam practice questions

Question 1 (4 marks)
Outline TWO factors influencing customer choice.

Question 2 (3 marks)
Describe one ethical influence on marketing.

Question 3 (4 marks)
Explain how implied conditions can influence marketing.

Question 4 (4 marks)
Explain how ONE consumer law can influence marketing.

Question 5 (5 marks)
Examine why ethical behaviour and government regulation are important in marketing.

Question 6 (5 marks)
Analyse how economic forces can influence customer choice.

on Resources

Teacher-led video Chapter 8 Exam practice solutions (tlvd-1859)

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9 Marketing process

9.1 Overview

LEARNING SEQUENCE

9.1 Overview
9.2 Situational analysis
9.3 Market research
9.4 Establishing market objectives
9.5 Identifying target markets
9.6 Developing marketing strategies
9.7 Implementation, monitoring and controlling
9.8 Review

9.1.1 Introduction

As outlined in chapter 7, a marketing plan gives a purpose and direction to all the business's activities. Everyone in the business needs to know the plan, so all departments are working towards achieving the goal. For this reason, it is referred to as an integrated marketing plan. The marketing plan needs to 'mesh' with the business's operational plan, financial plan and human resources plan.

BizFACT

The acronym SMEIDI will help you remember the steps involved in developing a marketing plan.

Situational analysis

Market research

Establishing marketing objectives

Identifying target markets

Developing marketing strategies

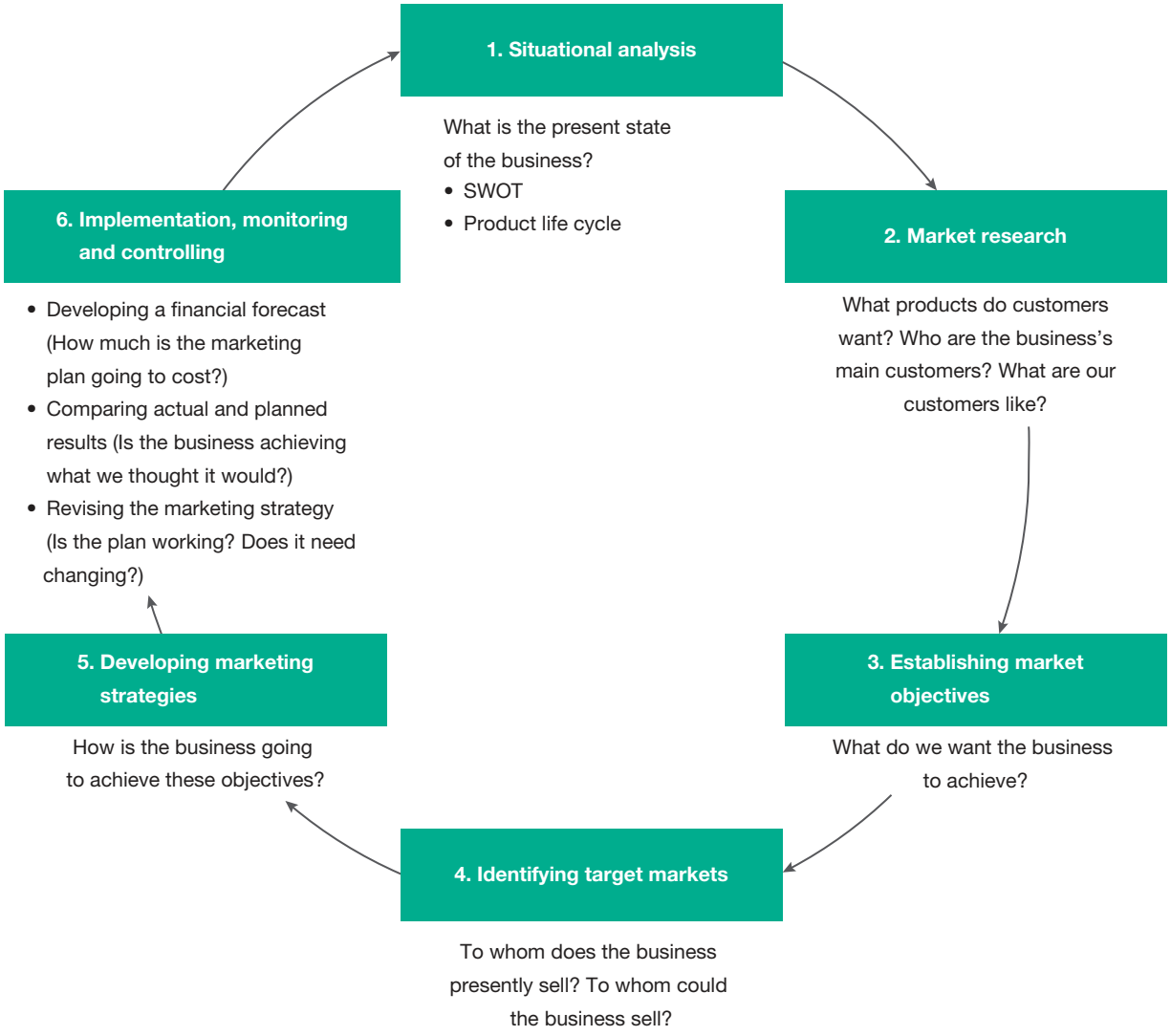
Implementation, monitoring and controlling

The steps involved in developing a marketing plan are shown in figure 9.1.

There is no set format for developing a marketing plan. Each plan will reflect the individual characteristics of the business. However, all marketing plans should have two features in common. They should be:

- realistic in the light of the situational analysis
- achievable within the business's resources and budgets.

FIGURE 9.1 Steps involved in developing a strategic marketing plan. Strategic marketing planning provides a mechanism for businesses to gain a clear picture of where the business is at present, and where it could be in the future. In this sense, it is the 'road map' for marketing.



on Resources

Digital document Key terms glossary (doc-35666)

Exam question booklet Chapter 9 Exam question booklet (eqb-0031)

9.2 Situational analysis

SYLLABUS LINK In this subtopic you will learn about situational analysis, SWOT and product life cycle.

***Source**: Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The most crucial step of the marketing plan is that management has a precise understanding of the business's current position and a clear picture of where it is heading. That is, a situational analysis must be undertaken based on meaningful market research. Two methods of analysis include a SWOT analysis and a product life cycle.

9.2.1 SWOT

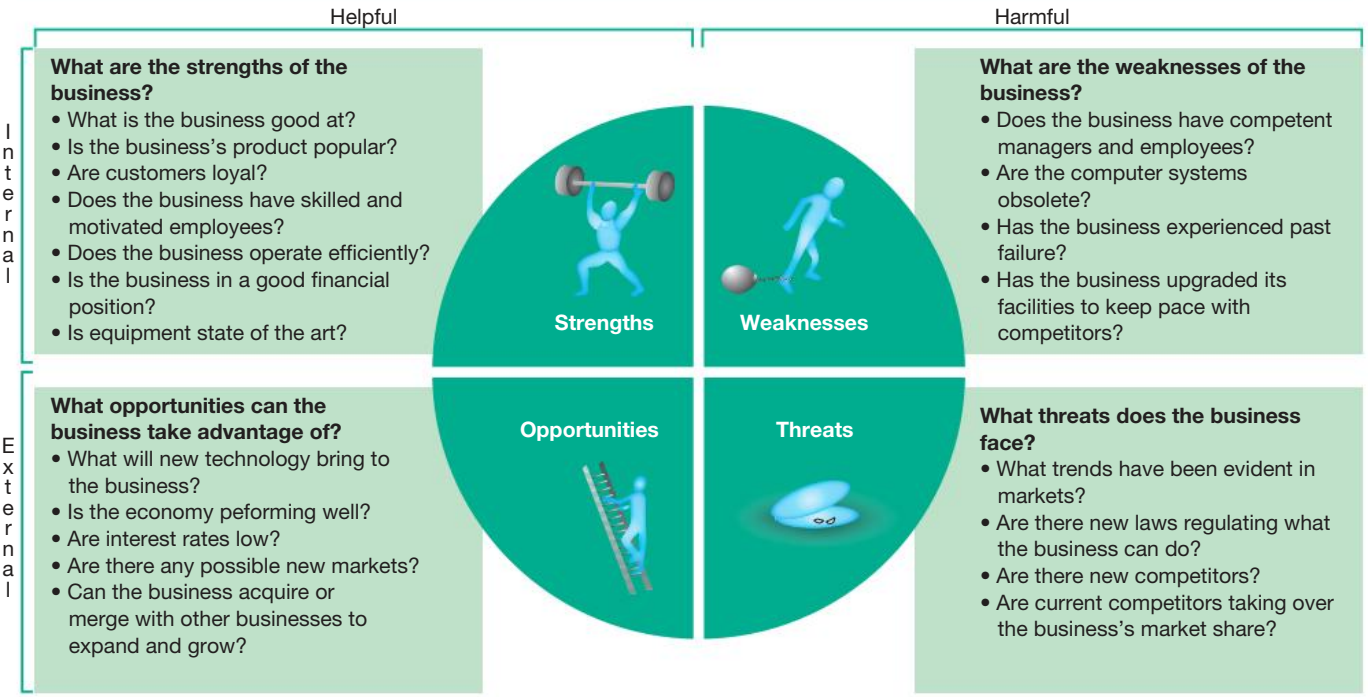
Changes in the external environment can dramatically alter the course of a business. For this reason, a business must constantly monitor these changes, looking for any opportunities to exploit and any threats to avoid.

Internal forces operate from inside the organisation and are largely within the control of the business. These internal forces are unique to each business and, by analysing them, management can assess the strengths and weaknesses of the business.

To develop a clear understanding of both the external and internal environments, a SWOT (strengths, weaknesses, opportunities and threats) analysis should be conducted. A **SWOT analysis** involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment. It provides the information needed to complete the situational analysis and gives a clear indication of the business's position compared with its competitors. The marketing plan should be modified to reflect this information.

SWOT analysis involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment

FIGURE 9.2 A SWOT analysis is a powerful tool that can be used at all stages of the marketing planning process.



Once the SWOT analysis has been conducted, an assessment of the product's position on the product life cycle should be carried out. This is necessary because different marketing strategies will need to be used at different stages of a product's life.

SNAPSHOT

Case study: SWOT analysis of Kellogg's

Kellogg's is an American multinational food manufacturing company that produces cereal and convenience foods. Below is a SWOT analysis of the company.



Strengths

- Wide range of high-quality products
- Market leader in the industry
- Sells some of the world's most iconic brands, e.g. Corn Flakes, Coco Pops, Rice Bubbles
- Has a strong global presence. Kellogg's manufactures their foods in 18 countries and offers them in more than 180 countries.
- One of the world's top 10 snack and bakery companies with $13 578 billion net sales in 2019
- Growth through strategic acquisitions. As consumers become more health-conscious, Kellogg's has made several acquisitions of more health-focused brands and expanded on their traditional products.
- Strong brand awareness. Kellogg's is the world's largest cereal maker by sales and spends more than $1 billion a year on brand advertising and marketing.
- Demonstrates corporate social responsibility in a number of areas. In 2019 they were recognised by the Ethisphere Institute as one of the 2019 World's Most Ethical Companies.

Weaknesses

- Questionable marketing campaigns. Some of Kellogg's marketing methods have been considered unethical, especially their marketing targeting children to products that are high in sugar.
- High sugar content and syrups in many products

Opportunities

- Potential new markets overseas.
- Possible expansion of product range
- Social influence of changing lifestyle. Due to modern busy lifestyles, people are looking for convenience foods and easy meals to save time.
- Opportunities to partner with the segment of restaurants and hotel chains to expand their business

Threats

- Intense competition — there are many substitute products available
- Government regulations and policies relating to products that are high in sugar, as well as policies regulating marketing
- Some of their products have fallen out of favour with today's more health-conscious consumers.
- Economic downturn and decrease in customer spending could lead to lower sales.

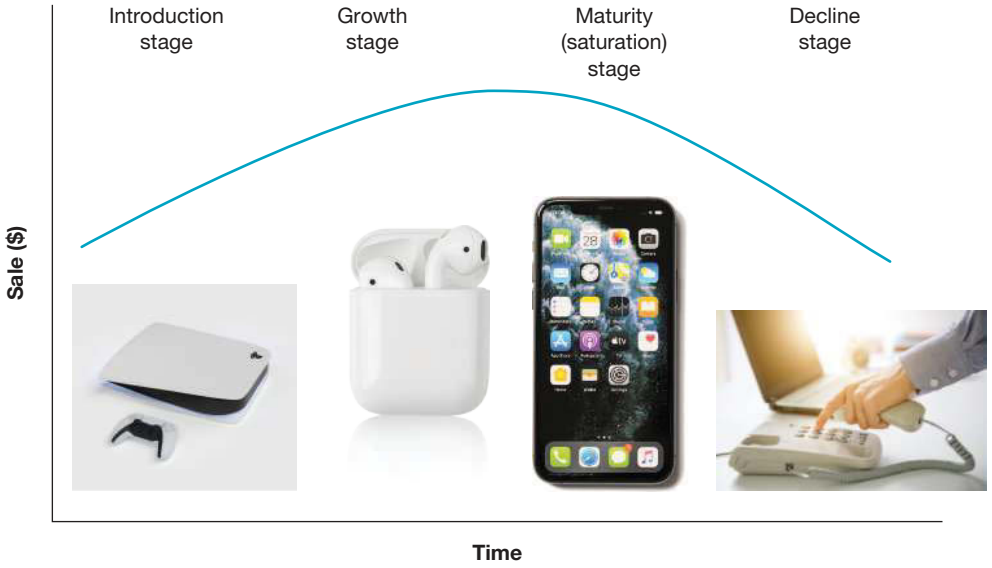
9.2.2 Product life cycle

The **product life cycle** consists of the stages a product passes through: introduction, growth, maturity and decline (see figure 9.3). Many businesses start because of someone's great idea to produce a product (a good or service) that is new and perhaps superior to what is available. From that tiny seed, a

product life cycle the stages a product passes through: introduction, growth, maturity and decline

successful business may grow; but like all good things, there is eventually an end to the cycle. Your parents and grandparents were familiar with many products that you would consider old-fashioned relics from the past, such as black and white television sets or cut-throat razor blades. Products such as these experienced the same cycle of introduction, growth, maturity and decline that products continue to experience today.

FIGURE 9.3 A business must be able to launch, modify and delete products in response to changes in the product life cycle. This diagram shows the PlayStation 5 in the introduction phase of the product life cycle and growth in Apple AirPods. iPhones are in the maturity phase due to their plateauing sales and mobile phones will eventually make landline phones extinct, placing landlines in the decline stage of the product life cycle.



At each stage of the product's life cycle, a different marketing strategy is necessary.

Table 9.1 outlines the marketing strategies relevant to the different stages of the product life cycle.

TABLE 9.1 Marketing strategies relevant to different stages of the product life cycle

	Introduction stage	Growth stage	Maturity stage	Decline stage
Description	The business tries to increase consumer awareness and build a market share for the new product.	Brand acceptance and market share are actively pursued by the producers of the product.	Sales plateau as the market becomes saturated.	Sales begin to decline as the business faces several options.
Product	Brand and reliability are established.	Quality is maintained and improved and support services may be added.	Features and packaging try to differentiate the product from those of competitors.	Product is maintained with some improvements or rejuvenation. Cut the losses by selling it to another business.
Price	Price is often noticeably lower than competitors' prices in order to gain a market foothold.	Price per unit of production is maintained as the firm enjoys increased consumer demand and a growing market share.	Price may need to be adjusted downwards to hold off competitors and maintain market share.	Price is reduced to sell the remaining stock.

(continued)

TABLE 9.1 Marketing strategies relevant to different stages of the product life cycle *(continued)*

	Introduction stage	Growth stage	Maturity stage	Decline stage
Promotion	Directed at early buyers and users. Communications seek to educate potential customers about the merits of the new product.	Promotion now seeks a wider audience.	Continues to suggest the product is tried and true — it's still the best.	Promotion is discontinued.
Distribution	Distribution is selective, which enables consumers to gradually form an acceptance of the product.	Distribution channels are increased as the product becomes more popular.	Incentives may need to be offered to encourage preference over rival products.	Distribution channels are reduced and product is offered to a loyal segment of the market only.

Why do some products decline?

Products end for various reasons (see the next case study). These include the changing public perception of what is fashionable at certain times. New technologies are constantly being introduced and with them come new products replacing old ones. New products also sometimes reduce demand for older ones. Fluctuations in the level of economic activity constantly result in shifts in customer spending habits.

Consumer behaviour is dramatically changing in light of shock events such as the COVID-19 pandemic and the ongoing need to reduce carbon emissions in order to prevent more devastating climate change. Consumers expect products to be more environmentally friendly. Some businesses will grasp this opportunity to create new, greener and more ecologically sustainable products, while other products will disappear.

Today, for example, car manufacturers are a good example of large-scale manufacturers throughout the world that are confronted with the unpleasant reality that consumers are more globally aware. They will no longer continue buying unsustainable products the way they once did.

FIGURE 9.4 Some tech products that seemed innovative when they were first released and have now experienced a decline in sales due to the increasing popularity of smartphones and tablets include MP3 players, e-readers, landline phones, personal computers, digital cameras and GPS units.



SNAPSHOT

Case study: Product life cycle of Apple iPad

Apple invented the iPad because Steve Jobs, the CEO at the time, wanted to create a new category of device that would be better than an iPhone or MacBook at certain tasks such as browsing the web, watching videos, taking photos and listening to music. The iPad was a completely new concept that revolutionised the computer tablet market. Below is a summary of the iPad's progression through the four stages of the product life cycle.

Introduction: 2010

- iPad announced and unveiled on 27 January 2010.
- Apple began taking pre-orders of the first-generation iPad in March 2010.
- First-generation iPad released in the USA on 3 April 2010. Apple sold an astonishing 300 000 iPads on the first day of availability.
- Released in Australia, Canada, France, Japan, Italy, Spain, Switzerland and the UK on May 28 2010.
- By 3 May 2010 Apple had sold 1 million iPads and by June 2010, 80 days after the release of the first iPad, Apple had sold 3 million units.
- The iPad achieved very high sales at first — 2 million iPads were sold in less than two months from its launch.
- Profits were low at the start and costs were quite high.
- There was no competition for the first five months.
- Apple priced iPad high — used price skimming.
- No competition — there were no other tablet computers on the market.
- iPads were only available through Apple online and retail stores.

Growth: 2011 to 2012

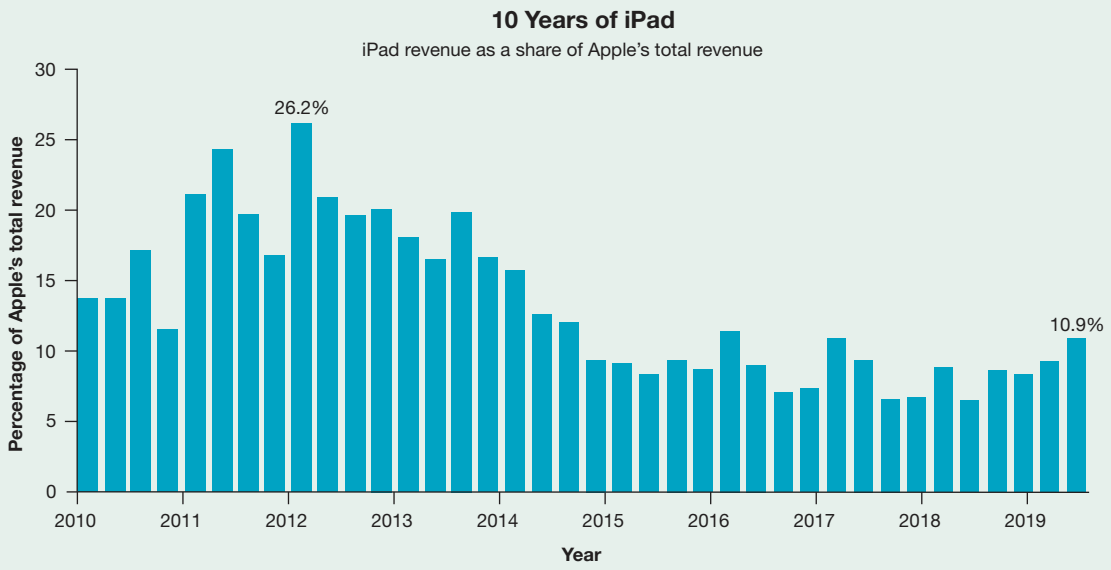
- A total of 15 million iPads were sold by the end of 2010.
- Prices of iPads began to drop.
- There were new entrants to the market. Apple began facing competition from Samsung, HP, LG and Cisco who had developed tablets to compete with the iPad.
- The iPad 2 was released on 11 March 2011. The iPad 2 included a dual-facing camera.
- In 2012, just before sales peaked, Apple introduced the smaller and more affordable iPad mini, which was better priced to take on competition from Google and Amazon.
- The iPad became available from other retailers.

Maturity: 2012 to 2014

- iPad sales peaked in 2014.
- By this stage there were multiple screen sizes, colours, price points and accessories.
- iPads faced increasing competition.
- Due to increasing competition, prices needed to be further lowered.
- Over the years the iPad was rejuvenated numerous times to avoid the product going into the decline stage. In fact, a total of 21 versions had been released by the end of 2019.

Decline: 2014 to present

- Apple attempted to tackle the decline stage well.
- iPad sales dropped dramatically each year from 2014 despite different iPads being introduced.
- Apple began targeting the enterprise and education markets. For example, Apple grew its IBM partnership and developed the Classroom application for teachers.
- Larger iPhones have now become a threat to iPad sales. The iPad was initially launched to be better than an iPhone for certain tasks, however newer iPhones are now able to do similar functions.



KEY IDEAS

- A marketing plan gives a purpose and direction to all the business's activities.
- The steps involved in the marketing process are:
  - situational analysis
  - market research
  - establishing marketing objectives
  - identifying target markets
  - developing marketing strategies
  - implementation, monitoring and controlling.
- A situational analysis provides a precise understanding of the business's current position and where it is heading.
- A SWOT (strengths, weaknesses, opportunities and threats) analysis provides the information needed to complete the situational analysis and assesses the business's position compared with its competitors.
- The product life cycle consists of the stages a product passes through: introduction, growth, maturity and decline.
- At each stage of the product's life cycle a different marketing strategy is necessary.

9.2 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

9.2 Quick quiz on	9.2 Exercise	9.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5, 6, 7, 8, 11, 13	3, 9, 10, 12, 14, 15, 16, 17	18

9.2 Exercise

Revision

1. **Clarify** why everyone in the business needs to know the marketing plan.
2. **Identify** the two features all marketing plans should have.
3. **Examine** figure 9.1, then copy the table below into your notebook. Complete the table by recalling and then writing against each step the appropriate statement from those given below. The first step has been completed for you.

Developing a marketing plan	Statement
Step 1: Situational analysis	The business currently has a market share of 28 per cent. The market is growing but new competitors are likely to enter the market.
Step 2: Market research	
Step 3: Establish market objectives	
Step 4: Identify target markets	
Step 5: Develop marketing strategies	
Step 6: Implement, monitor and control the plan	

Statements

a. The business will design a new promotional campaign featuring younger women. Direct selling methods will also be introduced.
b. The market share percentage will be examined every three months. If the results are negative, then the objectives will be reviewed.
c. The business is to increase its market share to 35 per cent within the next 12 months.
d. The business presently sells to 35- to 45-year-old females across all income groups. However, the product could be made to appeal to the 25 to 35 age group.
e. The business needs to collect information about existing and potential customers.

4. **State** what the acronym SWOT represents.
5. **Outline** the value of a SWOT analysis when reviewing the business's situation.
6. **Define** the term 'product life cycle'.
7. **Outline** the four stages of the product life cycle and provide an example of a product in each stage.
8. **Identify** at which stage of the product life cycle the following products are located.
   a. CD
   b. Personal computers
   c. Electric vehicles
   d. Plant-based foods
9. **Explain** why the marketing strategies should change as a product advances through the stages of its life cycle.
10. **Compare** the marketing strategies for a product in the growth stage with one in the decline stage.
11. **State** the main reasons why the sales of many products eventually decline.
12. **Construct** a SWOT analysis for a business you are familiar with.

Read the case study 'SWOT analysis of Kellogg's' and answer questions 13 to 15.

13. **Describe** how Kellogg's could take advantage of some of the opportunities outlined in the SWOT.

14. **Explain** the impact some of the threats mentioned could have on Kellogg's.
15. **Recommend** marketing strategies Kellogg's could implement to overcome their weaknesses or threats.

Read the case study 'Product life cycle of Apple iPad' and answer questions 16 and 17.

16. **Deduce** some factors that have led to the decline in iPad sales.
17. **Recommend** marketing strategies that Apple could implement to respond to the challenges they face.

Extension

18. 'Knowledge of the product's life cycle can provide valuable insights into ways the product can be managed to enhance sales and profitability.' **Assess** the accuracy of this statement.

9.2 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q10

A company has reduced the price of their current razor as a new model will be released soon.

Which stage of the product life cycle for the current razor is indicated by this decision?

A. Introduction
B. Growth
C. Maturity
D. Decline

Question 2 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q3

As a result of a SWOT analysis, a gym operator finds that a new larger gym is opening nearby. The operator then decides to extend its opening hours.

The aim of this strategy is to use

A. a strength to overcome a threat.
B. a strength to overcome a weakness.
C. an opportunity to overcome a threat.
D. an opportunity to overcome a weakness.

Question 3 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q3

While developing a new marketing plan a business discovers that many customers think its website is boring and confusing.

At what stage in the marketing process should this have been identified?

A. Identifying target markets
B. Developing marketing strategies
C. Conducting a situational analysis
D. Establishing marketing objectives

Question 4 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q4

At which stage of the marketing process would a business examine its internal and external influences?

A. When identifying target markets
B. When conducting a situational analysis
C. When establishing its marketing objectives
D. When developing its marketing strategies

Question 5 (4 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q22a & b

Bill and Jane have owned and operated a café in a busy restaurant area for many years. They specialise in fast healthy food that is popular with 18–30 year-olds. Recently a multinational franchise opened in the area in response to an expected increase in population.

a. Outline TWO strengths of the café. **(2 marks)**
b. Outline TWO opportunities for the café. **(2 marks)**

More exam questions are available in your learnON title.

9.3 Market research

SYLLABUS LINK In this subtopic you will learn about the three steps of the market research process.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

9.3.1 Importance of market research

Imagine you have just been given an assessable task for your Business Studies class. If you want to achieve satisfactory results, it is important that you undertake some type of research. The research could consist of reading books and magazines, conducting surveys, accessing internet sites, carrying out experiments and talking to people. Marketing managers also have to undertake research of their market.

Market research is the process of systematically collecting, recording and analysing information concerning a specific marketing problem.

market research the process of systematically collecting, recording and analysing information concerning a specific marketing problem

Just as a well-researched assessable task will lead to better results, marketing strategies perform best when they are based on accurate, up-to-date, detailed and relevant information. Being well-informed about all aspects of the market, especially the buying behaviour of existing and potential customers, places the business in a stronger position.

SNAPSHOT

Case study: Market research is at the heart of IKEA's expansion



Market research is at the heart of IKEA's expansion. This focus came about as a result of the problems they encountered when entering the US market due to their lack of research. Since then, IKEA has invested a lot of time conducting marketing research and studying consumers. This is especially the case when they make the decision to expand to new countries with cultures distinctly different from their own.

IKEA founder Ingvar Kamprad was a firm believer in conducting his own market research (i.e. primary research). Before entering a new market, the company carries out their own market analysis instead of relying on conventional research involving market studies. IKEA finds this to be more practical and intuitive as it allows the business to gain access to extensive amounts of cross-cultural data.

IKEA found that surveying people doesn't always give them the right answers. Many people say things that are not entirely accurate and what they actually do may be very different to what they say. This could be because people respond to questions in a way they think they're supposed to or answer in a way that makes them sound better; often this is because people are not always fully aware of how they behave.

To overcome this, IKEA have developed a number of research methods that go deeper and give them a better understanding of how people actually behave and what they actually want and need. Their researchers take a firsthand look at customers themselves. They frequently do home visits and set up cameras in people's homes, filming them for a number of days (with their permission). Through their research they want to come closer to people's everyday lives and reality. First their researchers watch the footage and analyse it and then they sit with their subjects and get them to watch the footage. Their subjects are often surprised as they are often not aware of how they actually behave.

The following are two examples of how IKEA's research led to the development of new products to better meet consumer's needs:

- IKEA recently studied over 8000 people across eight cities to observe their morning routines. What they found was that, regardless of the city, many people find the process of picking out their outfit for the day stressful, with women spending more time on this than men. Based on this data, IKEA invented a freestanding mirror called the Knapper that has a rack on the back to hang clothes and jewellery. This mirror is meant to help customers assemble an outfit (including clothes and accessories) the night before to cut down on morning anxiety.
- Other research revealed that more and more of the world's population are living in cities with smaller living spaces. This lead to the creation of more multifunctional products such as their new range of 'wireless chargers' — a range of products that blend in with people's homes and make it possible to charge mobile devices where they need them most, without having to chase after outlets or hide messy cables.

Releasing a new product onto the market is risky. Minimising the risk is the main purpose of market research. By collecting and assessing information about the needs and wants of consumers, a more accurate and responsive marketing plan can be designed and, therefore, reduce the risk of market failure. Market research attempts to identify and outline both marketing opportunities and problems as well as evaluating the implementation of the marketing plan. Effective market research can establish whether it is worth launching or promoting a product at all.

Without adequate, reliable and correct information, businesses expose themselves to market embarrassments, which could result in the product failing to sell.

BizFACT

In 2018 the Australian Centre for Business Growth revealed new research, which identified the top five reasons Australian SMEs are failing. Data was collected from CEOs whose small or medium-sized companies had failed. The top five reasons (in order) were lack of leadership and management skills including poor planning, insufficient market research and sales skills, mismanagement of financials, underestimating the impact of externalities, and poor governance structures.

FIGURE 9.5 The founders of Twitter originally designed a podcasting platform called Odeo. Soon after, Apple launched iTunes podcasting, so the founders invested significant time researching other opportunities to build on the platform they'd already created. They eventually decided to create a portal where people could share what they were up to. With this idea in mind, the founders researched existing social networking sites and surveyed users to discover what they didn't like about those sites. In 2006 Twitter was born.



9.3.2 The three steps of the market research process

It is often said that the recipe for effective decisions is 90 per cent information and 10 per cent inspiration. However, the information must be relevant to the situation or problem.

To obtain accurate information, marketing managers usually follow a three-step approach (see figure 9.6).

You will probably be familiar with this process as it uses similar steps to those needed to complete a research assignment.

FIGURE 9.6 The three steps of the market research process

Step	Explanation
1. Determining information needs	The problem is clearly and accurately stated to determine what needs to be measured and the issues involved. This is a crucial step.
2. Collecting data from primary and secondary sources	At this stage, the researchers know the facts that are needed and those that are already available. Plans must be made to gather missing data. Information may be collected by telephone, personal surveys and online, as well as by personal observation or from private data sources.
3. Analysing and interpreting data	Facts by themselves do not always provide a solution to the marketing problem. They need to be analysed and interpreted to determine what they mean.

Step 1: Determining information needs

The information collected must be relevant to the issue or problem being investigated. The best method to determine
the relevance of data is to constantly ask questions concerning its ultimate use. Information is useful if it:

- results in marketing strategies that meet the needs of the business's target market
- assists the business to achieve its marketing objectives
- may be used to increase sales and profits.

Ideally, marketing managers should treat information in the same way as other resources within the business, and weigh up the costs of collecting information against the benefits it provides.

Step 2: Data collection — primary and secondary sources

Marketing data refers to the information — usually facts and figures — relevant to the defined marketing problem. Normally, market researchers use a combination of two types of data: primary and secondary data (see figure 9.7.)

Primary data

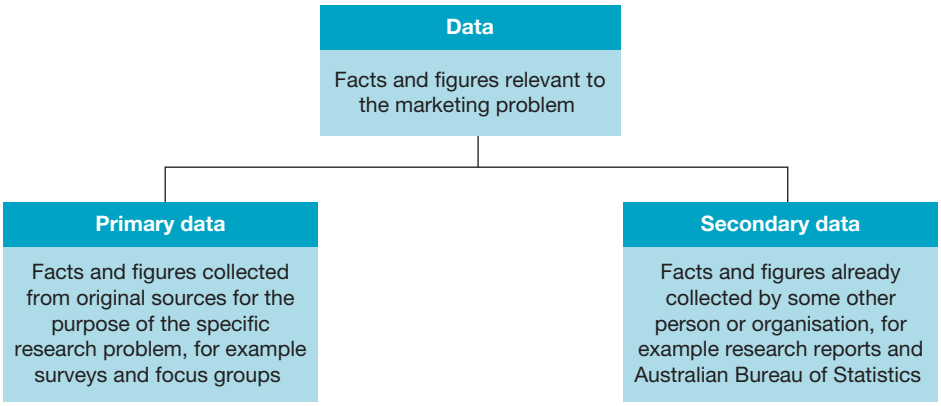
Primary data are the facts and figures collected from original sources for the purpose of the specific research problem. This information can be collected by the business itself, a process that may be time consuming and expensive. Many businesses outsource this activity.

The main advantage of primary data is that their collection is directed at solving a specific marketing problem. Their main function is to find out exactly what the customer is thinking.

marketing data the information relevant to the defined marketing problem

primary data the facts and figures collected from original sources for the purpose of the specific research problem

FIGURE 9.7 Two types of marketing data: primary and secondary



Three main methods are used to gather primary data.

1. *The survey method*. Conducting a **survey** means gathering data by asking or interviewing people. Surveys may be carried out by:
   - personal interviews — face-to-face interviews conducted in public places
   - focus groups — small groups of people who meet with the researchers
   - electronic methods of collection — telephone, mail and internet
   - questionnaires — a set of specific questions requiring a response from the person.

The main benefit of a survey is that it gathers first-hand information that provides details of customers' opinions. However, gathering information through surveys is becoming more difficult because respondent rates are declining. To overcome this problem, marketing companies are using electronic methods of collecting information about consumer behaviour, as outlined in the previous chapter.

survey the gathering of data by asking or interviewing people

BizFACT

Online surveys are increasingly being used by businesses to conduct market research. This is because they are faster, cheaper and easier to use for both participants and researchers.

2. *The observation method*. Observation involves recording the behaviour of customers. No interviews are involved and direct contact with respondents is avoided. Instead, the actions of the customers are systematically observed. Such methods can raise serious ethical issues, especially with regard to privacy. Information may be gathered through:
   - personal observation, such as when a researcher poses as a customer in a store
   - electronic observation, using camera or counting machines. For example, the scanner and cash register at a store checkout counter can record data on sales and customers' purchase patterns (see figure 9.8).

   This method of data collection has become very popular over recent years, especially with the development of computerised technology. It is now possible for a business to access its loyalty program, customer spending habits and customer database all at once, through the use of smart cards and bar coding (see the following case study).
   Such observation methods can be highly accurate, but their main limitation is that they explain only *what* happens, not *why* it happens.
3. *The experiment method*. Experiments involve gathering data by altering factors under tightly controlled conditions to evaluate cause and effect. Market researchers do this to determine whether changing one of the factors (a cause) will alter the behaviour of what is being studied (the effect). Experiments carried out in the field are called test marketing.

FIGURE 9.8 Many shopping centres, such as Westfield, offer free wi-fi to gather data on shoppers. When consumers access the free wi-fi service, the company tracks their shopping behaviour, internet and social media use, including the time they spend in stores and the websites they browse while shopping. It uses this data to send marketing messages on behalf of stores, and provides feedback to shopping centres and retailers on ways to attract and retain these customers and encourage them to spend more.



SNAPSHOT

Case study: How Coles and Woolworths gather data

Coles and Woolworths, who have a combined 80 per cent market share of the Australian grocery market, have invested heavily in data analytics and artificial intelligence capabilities to help them profile and target shoppers and thus gain a competitive advantage. These technologies will help them analyse the vast amount of data they collect through their loyalty programs, apps and online shopping sites. This strategy has further cemented their dominance in the industry and made it harder for smaller competitors who don't possess this sophisticated technology to compete.



Woolworths Rewards loyalty program and Coles Fly Buys program provide the stores with the ability to engage with customers on a personalised level. It enables the stores to gather a huge amount of data they can leverage through these new technologies. Loyalty programs provide retailers with an abundance of information and data. When people initially sign up, the company can find out a great deal of demographic data about their customers such as age, gender and address. In addition, each time a customer's card is scanned, the transaction is recorded and over time the business can gather data about customer preferences and their shopping habits, including the location, timing and frequency of their purchases. Retailers then use that information to build a profile of each customer so they can promote specific goods or services they are more likely to buy in a way that most appeals to them.

The data analytic technologies have assisted Woolworth and Coles to make their marketing and promotions more effective. For example, these stores can use the data gathered to target shoppers with emails notifying them when products they have previously purchased go on sale. This will enable Woolworths and Coles to assign their spending on promotion more efficiently, based on how customers are likely to respond. Artificial intelligence will be able to analyse the success of each promotion and then the business can improve on these promotional strategies in future.

Secondary data

Secondary data comprises information that has already been collected by some other person or organisation. It is referred to as secondary because it is information that has been collected for some other purpose; for example, census data and household expenditure surveys gathered by government and private organisations. With the advent of computer databases, an abundance of secondary data are available to market researchers.

secondary data information that has already been collected by some other person or organisation

There are two types of secondary data. These are:

- ***internal data***. This is information that has already been collected from internal sources — that is, from inside the business. Such data include customer feedback, sales and management reports, and research reports.
- ***external data***. This is published data from sources outside the business. Examples include magazines, industry association newsletters, internet sources and private data collection agencies. Probably the best known are the numerous reports produced by the Australian Bureau of Statistics (ABS).

BizFACT

The Roy Morgan Research Centre monitors what a targeted group of customers read, when and what they watch on television, what they buy, where they buy, and what they think of different products.

FIGURE 9.9 The Australian Bureau of Statistics (ABS) is Australia's official statistical organisation. It provides businesses with a range of resources to assist them with their planning and research activities. The ABS also provides a range of services to small businesses. It assists them with market research, profiling customers and planning. It can provide businesses with a wide range of data on their industry, their community, and the social and economic climate, as well as hints and tips.



Step 3: Data analysis and interpretation

Once the data has been gathered, conclusions need to be drawn. Raw data is of little value until it has been analysed and interpreted. **Statistical interpretation analysis** is the process of focusing on the data that represents average, typical or deviations from typical patterns.

The first step in drawing conclusions (analysis and interpretation) is to tabulate the data — that is, display the information in table format. The use of a spreadsheet computer program greatly simplifies this task. Cross-tabulation will allow comparisons to be made between individual categories. For example, cross-tabulation could show how men and women display different shopping habits, or the differences between the purchasing behaviour of high- and low-income earners.

This interpretation will largely be based on the marketing manager's judgement, experience and intuition. For this reason, it is preferable to involve a number of people in the interpretation of data so as to gain a wider perspective and, therefore, avoid the error of personal bias.

FIGURE 9.10 Around the time the film *Avatar* was launched, LG and Sony invested millions of dollars developing 3D TVs. While focus groups showed some enthusiasm, these companies assumed demand would be there based on *Avatar*'s success. The inconvenience of having to wear special glasses and the motion sickness experienced by many viewers led to the technology's demise. Another factor was the reluctance of producers wanting to invest in creating 3D material. Sony and LG have now ceased production of these TVs and could have saved millions of dollars if they had invested in extensive market research.



statistical interpretation analysis the process of focusing on the data that represents average, typical or deviations from typical patterns

on Resources

Weblink The Realise Group

KEY IDEAS

- Market research is the process of systematically collecting, recording and analysing information concerning a specific marketing problem.
- To obtain reliable and accurate information, marketers follow a three-step approach.
  - Step 1: Determining information needs. The problem is clearly stated to determine what needs to be measured and the issues involved.
  - Step 2: Collecting data from primary and secondary sources. Data are collected by mail, telephone and personal surveys, personal observation or from private data sources.
    - Primary data: information from original sources. Example: interviews and surveys
    - Secondary data: information collected by other organisations. Example: industry reports and Australian Bureau of Statistics
  - Step 3: Data analysis and interpretation. Determine what the data means.
    - Statistics are processed to determine if responses show trends or patterns that can be used in the business.

9.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

9.3 Quick quiz on	9.3 Exercise	9.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 5, 7, 12, 13	2, 6, 8, 9, 10, 11, 15, 16, 17, 20	14, 18, 19, 21

9.3 Exercise

Revision

1. **Define** the term 'market research'.
2. **Explain** why it is important for businesses to undertake market research.
3. **Outline** the three steps of the market research process.
4. Complete the following sentences by **recalling** the correct term from the list below.

resources	data	information	investigated	relevant	questions

   a. Information collected must be _____ to the problem being _____.
   b. The best method to determine the relevance of the _____ is to constantly ask _____ concerning its ultimate use.
   c. Marketers should treat _____ in the same way as other _____ within the business.
5. **Define** the term 'marketing data'.
6. **Distinguish** between primary and secondary data.
7. **Identify** the four methods used for gathering survey data. **State** under what circumstances each should be used.
8. **Account** for the increased use of electronic scanners to collect data.
9. **Distinguish** between the survey, observation and experiment methods of data collection.
10. **Compare** internal and external secondary data.
11. **Explain** the purpose of analysis and interpretation of data.
12. Investigate The Realise Group online to **identify** the services this market research and mystery shopping company offers its clients. Select and **summarise** one of the company's services.

Read the case study 'Market research is at the heart of IKEA's expansion' and answer questions 13 to 15.

13. **Outline** some of the market research techniques used by IKEA.
14. **Assess** IKEA's most successful method of market research (i.e. filming people in their homes).
15. **How** has market research contributed to IKEA's success?

Read the case study 'How Coles and Woolworths gather data' and answer questions 16 to 18.

16. **How** have Coles and Woolworths achieved a competitive advantage?
17. **Explain** the types of primary data Coles and Woolworths gather.
18. **Discuss** the use of loyalty programs for both businesses and consumers.

Extension

19. Choose a business partner in your class. Assume both of you are managers in an ice-cream manufacturing business. **Analyse** how you might use different types of market research (surveys, focus groups, observations and experiments) to determine customer reaction to a new kind of ice-cream.
20. Think about your school, or a business for which you work part-time.
    a. **Explain** how the organisation collects and processes marketing information.
    b. **Explain** what the information is used for.
    c. **Propose** what secondary sources could be used to supplement this data.

21. As the owner of a supermarket, you believe you could sell more strawberries by displaying them loose on a tray, rather than packaging them in punnets.
a. Describe an experiment to test this idea.
b. Determine the difficulties in conducting the experiment.

9.3 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q5

A business collects its own primary data through market research prior to developing a new product.

Which of the following could this business have used to provide primary data?

A. Customer survey
B. Published journal
C. Australian Bureau of Statistics catalogue
D. Australian Bureau of Statistics census data

Question 2 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q3

Customers at a furniture store are asked to give their postcodes at the checkout.

What is this an example of?

A. Primary research to determine target market
B. Secondary research to determine target market
C. Primary research to determine product life cycle
D. Secondary research to determine product life cycle

Question 3 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q20

The table shows, for 2014 and 2015, the number of viewers of four television programs and the total number of viewers at the times when the programs were shown.

	2014		2015	
Program	Program viewers	Total television viewers	Program viewers	Total television viewers
A	200 000	1 000 000	250 000	1 250 000
B	200 000	1 200 000	200 000	1 000 000
C	300 000	1 200 000	350 000	1 500 000
D	400 000	1 200 000	400 000	1 400 000

Which television program has increased its market share from 2014 to 2015?

A. Program A
B. Program B
C. Program C
D. Program D

Question 4 (2 marks)

Source: HSC 2013 Business Studies Exam, Section II, Q25a

Robin and Pat are planning to establish a sporting goods business. They have decided to adopt a niche market approach to maximise profits.

Outline ONE method that could be used by this business to collect relevant data about its target market.

Question 5 (2 marks)

Source: HSC 2011 Business Studies Exam, Section II, Q24a

Sam and Jody want to start a hairdressing business in their local area. They are very concerned about the number of other hairdressers already in the area and they want to quickly establish market share. How can market research help Sam and Jody determine their target market?

More exam questions are available in your learnON title.

9.4 Establishing market objectives

SYLLABUS LINK In this subtopic you will learn about the formulation of market objectives such as:
- increasing market share expanding the product range
- maximising customer service.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The next step in the marketing process is the formulation of marketing objectives. **Marketing objectives** are the realistic and measurable goals to be achieved through the marketing plan. It is of little value for a business to plan and implement a marketing strategy without first deciding what it wants to achieve. This decision is considered the most important step in the marketing planning process. The marketing objectives should be closely aligned to the overall business goals, but more customer-oriented than the goals for the entire business. They are also concerned with products and markets.

Three common marketing objectives include:
- increasing market share
- expanding the product range
- maximising customer service.

Such objectives can be measured, and should include specific targets to be met — for example, 'increase market share by 10 per cent within the next 12 months'.

marketing objectives the realistic and measurable goals to be achieved through the marketing plan

market share the business's share of the total industry sales for a particular product

9.4.1 Increasing market share

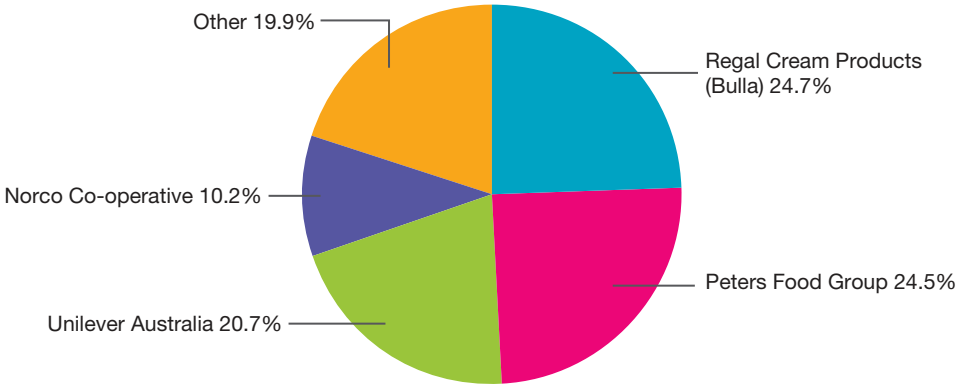
All marketing plans aim to achieve a specified market share. **Market share** refers to the business's share of the total industry sales for a particular product. Businesses often develop an extensive product range, using many different brand names to gain an extra few percentage points of market share. The metropolitan free-to-air (FTA) commercial television broadcasters Nine Network, Seven Network and Network Ten, for example, are constantly trying to increase their market share of the viewing public as measured by the 'rating' of a program. The 'rating' is an estimate of the number of television sets tuned in to a program. The network with the highest ratings for any program can charge advertisers more for a commercial spot. Consequently, each network is constantly battling for the largest share of the total viewing audience. To achieve this, networks offer a range of products (television programs) to attract the largest number of viewers. With the development of digital television broadcasting in Australia, the FTA television stations created sub-brands of their primary channels. Consequently, they have been able to divide (segment) the TV viewing audiences into more narrowly divided market groups. The motive behind offering these different sub-brands is to broaden the appeal, attract new customers (viewers) and consequently increase market share.

BizFACT

Google has dominated the search engine market with more than 90 per cent global market share. That's the average figure of how many people use Google a day, which translates to at least 5.6 billion searches per day.

Increasing market share is an important marketing objective for businesses that dominate the market, because small market gains often translate into large profits.

FIGURE 9.11 According to an IBISWorld Report, the ice-cream manufacturing industry earns $131 million a year in profits on turnover of $1.1 billion. While the industry was characterised by strong growth, rising health consciousness among consumers has slowed down industry growth in recent years. Out of the 212 businesses in the industry, those holding the largest market share are shown in the graph. In order to increase their market share, many of these companies have introduced low-fat or low-sugar ranges.



9.4.2 Expanding the product mix

The total range of products offered by a business is referred to as the business's **product mix**. Businesses are usually keen to expand their product mix, as this will increase profits in the long term. The same product mix will not remain effective for long because customers' tastes and preferences change over time, and demand for a particular product may decrease.

product mix the total range of products offered by a business

FIGURE 9.12 Not all businesses have an objective of expanding their product mix. An important element of Aldi's strategy is a very limited range of products, overwhelmingly private brands. The company's smaller range (some 1500 units as opposed to 20 000 to 30 000 in a large Coles or Woolworths outlet) has several advantages — a smaller store, lower warehousing costs and supplier discounts. These savings are passed on to consumers to ensure Aldi's appeal to people who are cost-conscious. This strategy has propelled the company's growth.



To develop the ideal product range, businesses must understand customers' needs. Each item in a product line should attempt to satisfy the needs of different target markets.

9.4.3 Maximising customer service

Of all the objectives examined so far, maximising customer service is perhaps the most important. **Customer service** means responding to the needs and problems of the customer. High levels of customer service will result in improved customer satisfaction and a positive reaction from customers towards the products they purchase. This establishes a sound customer base with the possibility of repeat purchases.

customer service how well a business meets and exceeds the expectations of customers in all aspects of its operations

BizFACT

Officeworks reported a 7.6 per cent increase in sales and an 8 per cent increase in revenue for the 2019 financial year. One reason provided for the improvements in sales and earnings was Officeworks' new and expanded product range. Product-range expansion included the educational, commercial furniture and commercial technology categories.

The old saying 'the customer is always right' is still correct today. Customers are the lifeblood of any business. To keep existing customers and attract new ones, the business needs to talk and listen to the customers. Research has shown that one dissatisfied customer usually tells eleven others, who in turn will each tell another five. Such 'word-of-mouth' marketing has the potential to make or break a business.

FIGURE 9.13 The Australian Services Excellence Awards (ASEAs) are Australia's premier customer service awards program. In 2019 Melbourne Cricket Club was the overall winner. The judging panel recognised their continued investment in their people and partners, as well as the sustained growth in customer service satisfaction levels year on year. In addition, the introduction of a range of new services specifically designed to take the customer experience to the next level was a key point of differentiation from other entrants.



Customer service can no longer be regarded as merely explaining the refund policy or providing a complaints department. Rather, it is an attitude that should be adopted by everyone within the business.

The strategies a business can use to maximise customer service include:

- asking customers what they want
- training employees and rewarding them for excellent customer service
- anticipating market trends by conducting research
- finding out what competitors are offering and then reviewing the product mix
- establishing and maintaining long-term relationships with customers
- encouraging employees to focus their attention on the customer's needs (customer-oriented) and not just on making a sale (sales-oriented).

KEY IDEAS

- Marketing objectives are the realistic and measurable goals to be achieved through the marketing plan.
- The marketing objectives should be more customer-oriented than the goals for the entire business, and should include specific targets to be met — for example, 'Increase market share by 5 per cent over 12 months'.
- Marketing objectives include:
  - Increase market share. Market share refers to the business's total share of the total industry sales for a particular market.
  - Expand the product range. Product mix is the total range of products offered by a business.
  - Maximise customer service. Customer service means responding to the needs and problems of the customer.

9.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

9.4 Quick quiz on	9.4 Exercise	9.4 Exam questions

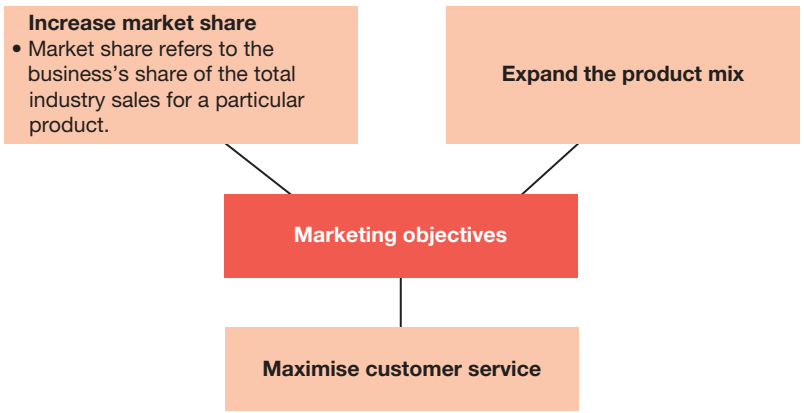
Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2	3, 4, 5	6, 7, 8

9.4 Exercise

Revision

1. **Construct** a concept map (started below) summarising the three main marketing objectives.



2. In the following examples, **identify** which marketing objective the business is trying to achieve.
   a. The business introduces a customer feedback form to measure the level of customer satisfaction.
   b. The business undertakes an extensive promotional campaign in an attempt to attract new customers.
   c. The business decides to offer a wider variety of products.
3. **Explain** why businesses wish to increase their market share.
4. a. Define the term 'product mix'.
   b. **Explain** why businesses are usually keen to increase their product mix.
5. **Explain** the relationship between customer satisfaction and profits.

Extension

6. 'The most important step in the marketing plan process is the formulation of the marketing objectives.' **Evaluate** the accuracy of this statement.
7. Develop a strategic marketing plan for your school's canteen. How could the canteen maximise its customer service? **Predict** what major problems it would face in trying to expand off campus.
8. 'There are only two ways to create and maintain outstanding business performance. First, take exceptional care of the customer and, second, develop new products. It is that simple.' **Analyse** the relationship between customer service, product mix and market share.

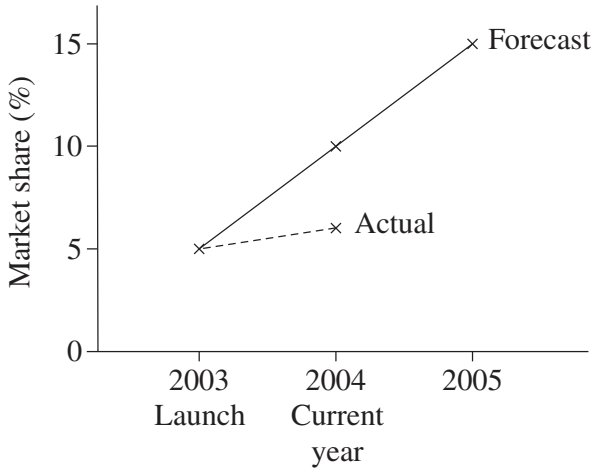
9.4 Exam questions

Question 1 (1 mark)

Source: HSC 2004 Business Studies Exam, Section II, Q21a

NuCam markets a digital video camera. This product is in the growth phase of its life cycle. Management is reviewing the performance of the product on the market.

Market share for NuCam digital video camera



Referring to the graph, identify a marketing objective that NuCam management has established for the digital video camera.

Question 2 (1 mark)

Grange Doors has stated that by 2015 they will be the largest provider of doors in NSW. Which of the following best describes this marketing objective?

A. Market share
B. Sales
C. Expansion into new markets
D. Expand product range

Question 3 (1 mark)

Bobo has set a break-even point for costs and revenue. Which of the following is the most likely market objective for Bobo?

A. Market share
B. Sales
C. Expansion into new markets
D. Expand product range

Question 4 (3 marks)

Rani has called together the management team to set marketing objectives for her business. Explain the role of marketing objectives in the marketing process.

More exam questions are available in your learnON title.

9.5 Identifying target markets

SYLLABUS LINK In this subtopic you will learn about how a business identifies and selects a target market.

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9.5.1 Introduction

A **target market** is a group of present and potential customers to which a business intends to sell its product. The customers within the target market share similar characteristics such as age, income, lifestyle, location and spending patterns. Because you are a senior high school student, you're part of a major target market — the teenage/young adult market. The teenage/young adult market:

- consists of people between 13 and 19 years of age
- has more disposable income than in the past
- is more willing to spend on themselves, especially designer brands and electronic devices
- makes up only 8 per cent of the Australian population but influences more than 70 per cent of their parents' clothes and fast-food purchases
- spend on average $5000 a year of their parents' money.

target market a group of present and potential customers to which a business intends to sell its product

primary target market the market segment at which most of the marketing resources are directed

secondary target market a smaller and less important market segment than the primary target market

Consequently, marketers want to tap into this highly profitable target market.

Sometimes a business may be able to identify a primary and a secondary target market. A **primary target market** is the market segment at which most of the marketing resources are directed. A **secondary target market** is usually a smaller and less important market segment (see figure 9.14).

FIGURE 9.14 Stationery retailer Smiggle ('between a smile and a giggle') has children and young teens aged from 4 to 14 as its primary target market. Its brightly coloured products are regarded as an essential fashion accessory by this age group. It is said that its secondary target market is the grandparents of young Smiggle fans!



A business's primary target market will generate most of its revenue. These are the customers who are loyal to a particular business and make repeat purchases. Research has found that a small percentage of customers are usually responsible for the majority of sales. This is referred to as the 80/20 principle, according to which 80 per cent of sales comes from 20 per cent of a business's customer base. The secondary target market should not, however, be ignored, for while the number of customers may be small, it does provide an alternative in case there is a loss of customers from the primary target market.

BIZFACT

Research from the Financial Planning Association (FPA) of Australia revealed that kids these days are a lot more well-off than most people think, with some getting up to $40 a week in pocket money. For older teenagers aged between 14 and 18, the weekly pocket money rate starts at $10 and goes all the way up to $39.

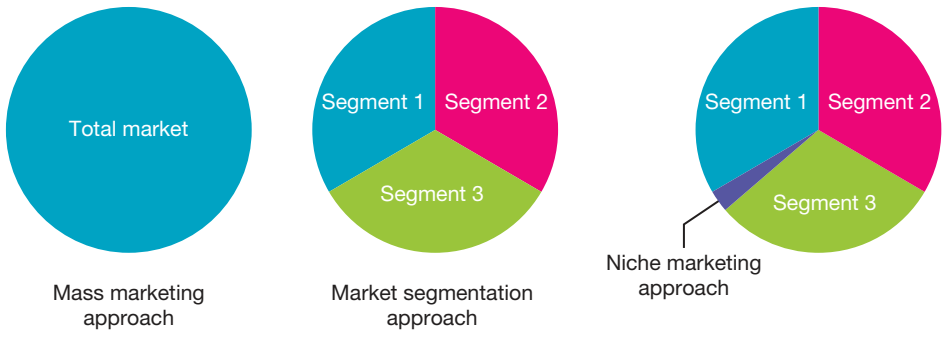
9.5.2 Why identify and select a target market?

A business identifies and selects a target market so it can direct its marketing strategies to that group of customers. This allows the business to better satisfy the wants and needs of the targeted group. This occurs because the business is able to:

- use its marketing resources more efficiently, which is likely to result in the marketing campaigns being more cost effective and time efficient
- make promotion material more relevant to the customers' needs, and therefore more likely to be noticed
- better understand the consumer buying behaviour of the target market
- collect data more effectively and make comparisons within the target market over time
- refine the marketing strategies used to influence customer choice.

Businesses can choose one of three approaches to identifying and selecting a consumer target market: the mass marketing approach, the market segmentation approach or the niche market approach (see figure 9.15).

FIGURE 9.15 Identifying and selecting a market to be the target market



SNAPSHOT

Case study: Fila's change in target market

Originally started in 1911, Fila's popularity ended in the 2000s when sales began declining rapidly. A rebranding campaign was launched to change people's perception of Fila. The goal was to redesign their brand identity, rejuvenate their image and focus on creating a brand that is viewed not only as a 'sports' brand but a 'lifestyle' as well.

Central to Fila's comeback was the decision made by the company to change their target market in 2018 and tap into a new generation of consumers. Fila went from targeting people in their 30s and 40s to younger customers. The new brand focuses on young, trendy sports and the lifestyle the consumer lives outside athletics. They now target young stylish people who consider sport as an integral part of their life and sportswear a key asset to improve performance; young people who want to look good while doing trendy athletic activities. Fila also caters for the middle-to high-income groups.



One of their biggest challenges is trying to keep pace with the younger generation. One way Fila are targeting younger consumers is through the development of products which are truly sport-inspired and with superior lifestyle appeal. Another way they have appealed to this demographic is by teaming up with celebrities to wear their products. For instance, Kendall Jenner and Rihanna have both been seen in Fila clothing. They have also collaborated with renowned fashion designers including Fendi, Jason Wu and 3.1 Phillip Lim to emphasis their trendsetter position.

Since the rebranding, Fila has been recognised as a leading brand that combines fashion and sports elements. This rebranding has paid off. In the first half of 2019, Fila's revenue increased by 79.9 per cent and gross profit grew by 79.2 per cent.

9.5.3 Mass marketing approach

mass marketing approach a marketing approach that seeks a large range of customers

As outlined in chapter 7, seventy years ago marketers commonly spoke about 'mass market'. In other words, there was a large demand for a standard product. In a mass market, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers. The Model T Ford, for example, was the first motor vehicle to be produced and sold to the mass market. A **mass marketing approach** seeks a large range of customers.

The mass marketing approach assumes that individual customers in the target market have similar needs. The business therefore develops a single marketing mix and directs it at the entire market for the product. This means there is one type of product with little or no variation, one promotional program aimed at everyone, one price, and one distribution system used to reach all customers.

BizFACT

One of the main objectives of conducting market research is to identify the business's target market for its products.

9.5.4 Market segmentation approach

Few businesses can sell their products to the entire market — the market is just too big. Therefore, a business will divide the market into distinct segments. A business that is marketing motor vehicles, for example, would not direct its marketing efforts towards every person in the total vehicle market. Some people might want only a sports car; others might want a four-wheel drive. The business would thus direct its efforts towards a particular segment of the total market for motor vehicles.

market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics

Market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics. Once the market has been segmented, the business selects one of these segments to become the target market. Segmenting a market enables a business to design a marketing plan that meets the needs of a relatively uniform group. Marketing segmentation is explained in more detail in chapter 10.

9.5.5 Niche market approach

An extension of the market segmentation approach is that of the niche market, which is a narrowly selected target market segment. In a sense, it is a segment within a segment, or a 'micro-market'. For example, an exclusive fashion boutique can carve out a niche market and, therefore, avoid direct competition with large department stores. In the last few years, some hotels have developed a niche market for their own 'boutique' beers, brewed on the premises. Such businesses market to a narrow, specific customer base (see figure 9.16).

FIGURE 9.16 Lorna Jane Clarkson is the founder of workout fashion business Lorna Jane. She began making leotards from a young age and realised there was a demand for fashionable activewear. She opened her first store in 1993 and now there are more than 200 Lorna Jane stores worldwide. Lorna Jane Clarkson has never been afraid to take a risk. While other businesses believed that the market for fitness garments was too small to make a profit, she decided to focus on that niche market anyway.



The needs of customers in these markets are often neglected by large businesses because it is rarely profitable for them to alter their marketing mix to cater for very small groups.

KEY IDEAS

- A target market is a group of present and potential customers to which a business intends to sell its product.
- Sometimes a business may be able to identify a primary and a secondary target market.
- A business identifies and selects a target market so it can direct its marketing strategies to that group of customers.
- Businesses can choose one of three approaches to identifying and selecting a consumer target market:
  - mass marketing approach — the seller mass-produces, mass-distributes and mass-promotes one product to all buyers
  - market segmentation approach — the total market is subdivided into groups of people who share one or more common characteristics
  - niche market approach — a narrowly selected target market segment.

9.5 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

9.5 Quick quiz on	9.5 Exercise	9.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 9, 10, 12, 14	1, 2, 4, 5, 6, 7, 8, 13, 15	11

9.5 Exercise

Revision

1. **Why** would marketers want to target the teenage/young adult market?
2. **Distinguish** between primary and secondary target markets and give an example of each.
3. Complete the following sentences by **recalling** the correct word from the list below.

customers	primary	segmentation
niche	characteristic	narrowly
target	subdivided	present

   a. A _____ market is a group of _____ and potential _____ to which a business intends to sell its product.
   b. Sometimes a business may be able to identify a _____ and a secondary target market.
   c. Market _____ occurs when the total market is _____ into groups of people who share one or more common _____.
   d. An extension of the market segmentation approach is that of the _____ market, which is a _____ selected target market segment.
4. **Why** do businesses identify and select a target market?
5. **Compare** the mass marketing approach with the segmented marketing approach.
6. **Why** is market segmentation the most common marketing approach used by businesses today?
7. **How** are market segmentation and target market linked?
8. **Explain** the relationship between market segmentation and niche market.

Read the case study 'Fila's change in target market' and answer questions 9 and 10.

9. **Outline** the characteristics of Fila's target market according to some of the common elements businesses use to segment customer markets, i.e. demographic, psychographic, geographic and behavioural.
10. **Describe** the marketing strategies Fila has used to appeal to their new target market.

Extension

11. In pairs, conduct a survey of 30 people to find out what television shows they enjoy watching. Using a database, classify the respondents by age and gender. **Analyse** your results and present them to the rest of the class.

Research a business of your choice and answer questions 12 to 15.

12. **Identify** the primary and secondary target markets of the business you have chosen.
13. **Calculate** the importance of these markets to the business.
14. **Identify** the variables the business owner uses to segment the target market.
15. **How** does market segmentation help the owner to achieve long-term goals?

9.5 Exam questions

Question 1 (1 mark)

Source: HSC 2007 Business Studies Exam, Section II, Q25a

A chain of fitness centres in the city is used by office workers. The owners plan to open a new branch in a shopping complex in a new suburb.

Identify ONE possible target market for the new branch.

Question 2 (3 marks)

Source: HSC 2002 Business Studies Exam, Section II, Q21

Ron is planning to set up a restaurant. He has undertaken market research which revealed that the proposed location for the restaurant would suit business people or families with young children.

a. Identify Ron's TWO possible target markets. **(1 mark)**
b. Describe TWO factors that Ron may consider in selecting his target market. **(2 marks)**

Question 3 (1 mark)

Outline the term 'target market' as it applies to the marketing process.

Question 4 (2 marks)

'We now know who our target market is and this is crucial to our success,' states the CEO of a hotel. Why does the CEO make this statement?

More exam questions are available in your learnON title.

9.6 Developing marketing strategies

SYLLABUS LINK In this subtopic you will learn about the four Ps that make up the marketing mix:
- Product
- Price
- Promotion
- Place.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

9.6.1 Marketing mix — the four Ps

Once the business has undertaken a situational analysis, conducted market research, established the marketing objectives, and identified and selected a target market, the next process of the marketing plan is to develop marketing strategies to achieve the marketing objectives. **Marketing strategies** are actions undertaken to achieve the business's marketing objectives through the marketing mix.

marketing strategies actions undertaken to achieve the business's marketing objectives through the marketing mix

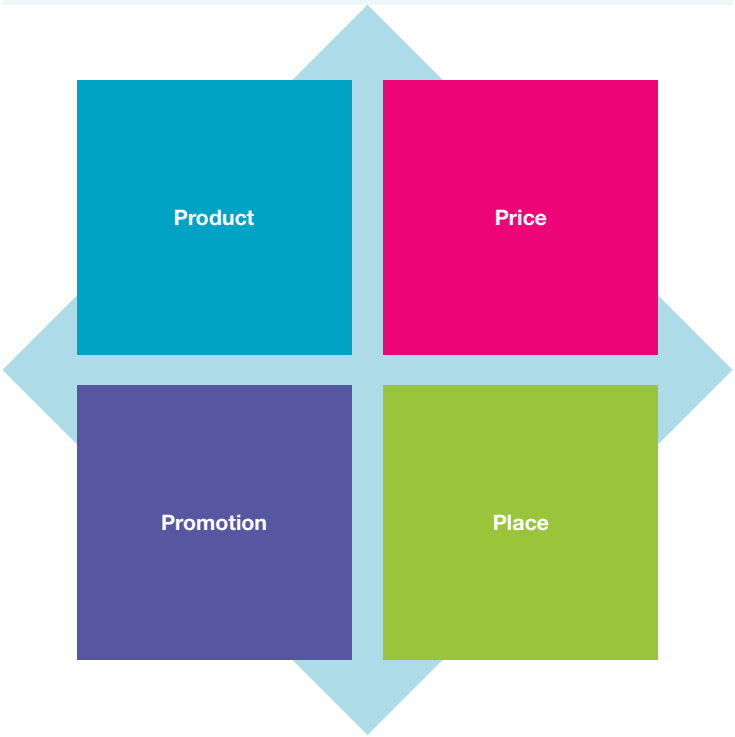
marketing mix refers to the combination of the four elements of marketing, the four Ps — product, price, promotion and place — that make up the marketing strategy

One of the most useful ways of understanding how to develop a marketing strategy is to examine each of the elements of the marketing mix. The **marketing mix** refers to the combination of the four Ps — product, price, promotion and place/distribution. A business has control over the four Ps and uses them to reach its target market. Additionally, the business has control over other business resources — such as information, finances and employees — that may also be used to achieve marketing objectives.

Once the four Ps have been established, the business must then determine the emphasis it will place on each of the variables. This will largely be determined by where the product is positioned or its stage in the product life cycle. For example, a product that is being marketed with an image of exclusivity and prestige will require a marketing mix totally different from a no-frills, generic item. A different marketing mix will also be required for a product in its introductory stage than when it reaches the decline stage.

The following section will provide a brief introduction to the main marketing strategies based on the 'four Ps' of marketing. This information will be examined in greater detail in chapter 10. Also in chapter 10, you will be introduced to the extended marketing mix, which includes people, processes and physical evidence — the seven Ps of marketing.

FIGURE 9.17 The four Ps, also known as the marketing mix, is probably the most well-known term in marketing and considered to be the essential elements for any marketing campaign.



9.6.2 Product (goods and/or services)

This element of the marketing mix involves much more than just deciding which product to make. The business also needs to determine such features as the product's quality, packaging/labelling, design, brand name and guarantee. The product is a combination of all these variables.

Customers will buy products that not only satisfy their needs and wants but also provide intangible benefits such as a feeling of security, prestige, satisfaction or influence. Much careful planning needs to be undertaken when developing the product strategy. The product element of the marketing mix will be examined in more detail in subtopic 10.4.

9.6.3 Price

Selecting the 'correct' price — the amount of money a customer is prepared to offer in exchange for a product — can sometimes be difficult. The major pricing decision is whether to set a price above, below or about even with the competitors' prices. Of course, a business must consider other factors too, such as the costs of production and level of consumer demand. Price does not just refer to what the price is, but rather, the method or strategy the business uses to decide its prices. The different pricing strategies and methods will be examined in more detail in subtopic 10.5.

9.6.4 Promotion

A promotion strategy details the methods to be used by a business to inform, persuade and remind customers about its products. The main forms of promotion include advertising, personal selling and relationship marketing, sales promotion, publicity and public relations.

Changes in technology, especially advances in information and communication technology (ICT), are having a significant impact on how businesses promote their products. The internet, for example, has become an effective advertising tool used by businesses to deliver specific messages to its target market. Marketing mix will be examined in more detail in subtopic 10.6.

FIGURE 9.18 Michael from Belle Property relies heavily on social media to grow his business and build his reputation as a local market leader. He uses Facebook and Instagram to showcase new listings and sales, report on industry trends, run competitions and post testimonials and live videos. Social media has proven to be an effective way for him to connect with his community, clients and potential buyers and sellers.



9.6.5 Place/distribution

This element of the marketing mix deals with the channels of distribution: the ways of getting the product to the customer. This process usually involves a number of intermediaries or 'go betweens', such as the wholesaler or retailer. Apart from the retailer, the other intermediaries are often invisible; that is, the customer knows little about their role and operation.

The number of intermediaries chosen will determine how widely the product will be distributed. The business may wish to keep supply of the product restricted to a few specialised outlets, which is the distribution method usually selected by expensive products. For example, Gucci and Louis Vuitton fashion accessories are available in only a few selected locations. Alternatively, distribution may be as wide as is practically possible, which is the method used by Coca-Cola. Its distribution channels include retail stores, supermarkets, vending machines, restaurants, clubs, hotels, cafes and fast-food outlets. Today, you can buy a Coca-Cola product anywhere from London to Beijing, Cape Town to Santiago. The place element of the marketing mix will be examined in more detail in subtopic 10.7.

KEY IDEAS

- Marketing strategies are actions undertaken to achieve the business's marketing objectives through the marketing mix.
- The marketing mix refers to the combination of the four Ps — product, price, promotion and place/distribution.
- Once the four Ps have been established, the business must then determine the emphasis it will place on each of the variables.
- A business may vary its marketing mix when it wants to reach different target markets.
- A product is a good or service that can be exchanged for money.
- The price is the amount of money a customer is prepared to offer in exchange for a product. It refers to the method or strategy the business uses to decide their prices.
- Promotion describes the methods used to inform, persuade and remind customers about a business's products.
- Place is the element of the marketing mix that deals with the channels of distribution: the ways of getting the product to the customer.

9.6 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

9.6 Quick quiz on	9.6 Exercise	9.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 3, 4, 5	1, 6	7

9.6 Exercise

Revision

1. **Explain** the link between marketing strategies and marketing mix.
2. **Outline** the four Ps of the marketing mix.
3. **State** what determines the emphasis a business places on each of the four Ps of the marketing mix.
4. **Identify** the factors that need to be considered when determining strategies related to product.

5. **Summarise** briefly the four Ps of the marketing mix by completing the table below. The first one has been started for you.

Marketing mix element	Key features
Product	• Goods or services exchanged for money
Price	
Promotion	
Place	

Extension

6. 'The four Ps are the variables that marketing managers can control, unlike the variables in the marketing environment.' **Discuss**.
7. Referring to a business you are familiar with, examine and **evaluate** the promotion methods used for one of their products.

9.6 Exam questions

Question 1 (1 mark)

Source: HSC 2008 Business Studies Exam, Section I, Q8

Which of the following includes ALL four elements of the marketing mix?

A. Credit terms, positioning, segmentation, pricing
B. Advertising, warranties, pricing, public relations
C. Discounting, packaging, advertising, distribution
D. Personal selling, branding, warehousing, publicity

Question 2 (1 mark)

Source: HSC 2005 Business Studies Exam, Section I, Q2

An engineering business that has been producing pollution control components for ten years is now redesigning components to meet new environmental standards.

What marketing strategy is the business currently concerned with?

A. Place
B. Price
C. Product
D. Promotion

Question 3 (1 mark)

Han has the responsibility of ensuring that products are stored and dispatched as quickly and as cheaply as possible so that the price and promoted image of service and customer satisfaction are maintained.

For which marketing strategy is Han responsible?

A. Price
B. Product
C. Place
D. Promotion

Question 4 (6 marks)

'Marketing is a coordinated effort. The effort is only as strong as its weakest point. Each aspect is linked and interdependent. It is the attention to detail that leads to success.'

Analyse the role of place/distribution as an interdependent part of successful marketing strategies.

More exam questions are available in your learnON title.

9.7 Implementation, monitoring and controlling

SYLLABUS LINK In this subtopic you will learn about:
- implementation, monitoring and controlling
- developing a financial forecast
- comparing actual and planned results
- revising the marketing strategy.

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9.7.1 Introduction

A marketing plan is a meaningless piece of paper until the plan is implemented. **Implementation** is the process of putting the marketing strategies into operation. Implementation involves the daily, weekly and monthly decisions that have to be made to make sure the plan is effective.

The previous elements of the marketing plan outlined what had to be done and why it had to be done, whereas the implementation stage is the *how, where* and *when* it is to be done. This is a crucial part of the process.

To implement the marketing plan effectively, a number of basic questions need to be answered:
- Is the plan fully integrated with all other sections of the business?
- How should the business be structured and organised?
- Have effective lines of communication been established between the marketing department and all other departments?
- Who are the best people for the various tasks needed to implement the plan?
- Are the marketing personnel motivated and focused on achieving the marketing objectives?
- Are all other employees familiar with the marketing objectives and marketing strategies?

The implementation stage is quite difficult, especially as unforeseen situations may arise that put in jeopardy the success of the entire marketing plan.

Once the marketing plan has been implemented, it must be carefully monitored and controlled. **Monitoring** means checking and observing the actual progress of the marketing plan. This requires the marketing department personnel, as well as other employees, to gather information and report on any important changes, problems or opportunities that arise during the life of the marketing plan (see figure 9.19).

FIGURE 9.19 A very simple way businesses can monitor which types of marketing strategies are generating the best results for their business is by asking their customers how they found out about their business.



implementation process of putting marketing strategies into operation

monitoring the process of measuring actual performance against planned performance

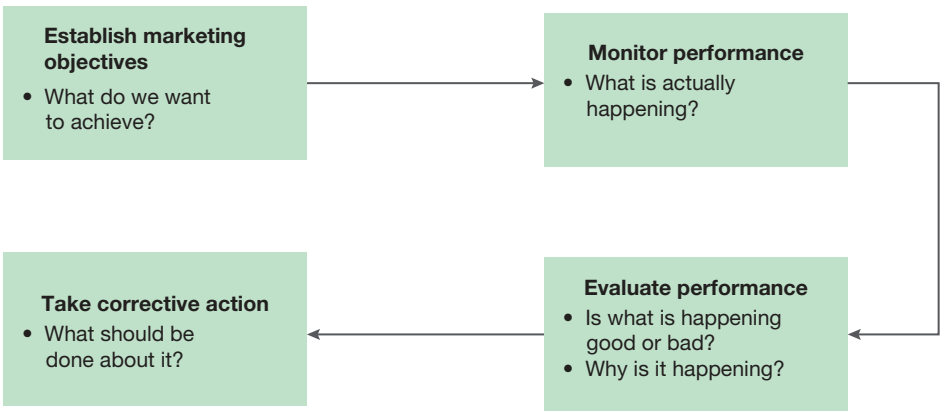
The information collected during the monitoring stage is now used to control the plan. **Controlling** involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained (see figure 9.20). To achieve this, the marketing manager needs to constantly ask two questions regarding the marketing plan:

1. What does the business want the marketing plan to achieve; that is, what are the objectives?
2. Are these objectives being achieved?

The first step in the controlling process requires the business to outline what is to be accomplished; that is, to establish a key performance indicator (KPI). A KPI is a forecast level of performance against which actual performance can be compared. For example, a KPI could be:

- increase monthly sales by 5 per cent
- improve sales revenue per salesperson by 10 per cent over the next six months.

FIGURE 9.20 Once marketing objectives have been established, they must be monitored to ensure they are being met; otherwise corrective action must be taken.



The second step in the controlling process is to compare or evaluate actual performance against the KPI. Budgets, sales statistics and cost analyses can be used to evaluate results. For example, a marketing manager could compare each salesperson's results with his or her sales quota. It is only by establishing KPIs and then comparing them with actual performance that a marketing manager can evaluate the effectiveness of the marketing plan.

9.7.2 Developing a financial forecast

When evaluating alternative marketing strategies, a business must develop a **financial forecast** that details the costs and revenues for each strategy. By measuring the sales potential and revenue forecasts (benefits) for each strategy, and comparing these with the anticipated expenditures (costs), a business is in the best position to decide how to allocate its marketing resources. Once this information has been gathered, it is possible to determine the most appropriate course of action using a cost–benefit analysis.

Although financial forecasting allows the marketing manager to undertake a cost–benefit analysis, the results are always open to individual interpretation.

Until a detailed analysis of the forecast cost and revenue is undertaken, a business is making decisions based merely on 'gut feelings', which is an inappropriate approach in today's competitive environment.

controlling involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained

financial forecast the business's predictions about the future

Developing a financial forecast requires two steps:

1. *Cost estimate*. How much is the marketing plan expected to cost? Costs of the marketing plan can be divided into four major components: market research; product development; promotion, including advertising and packaging; and distribution.

2. *Revenue estimate*. How much revenue (sales) is the marketing plan expected to generate? Forecasting revenues will be based on two major components: how much consumers are expected to buy and for what price, and what sales staff predict they will sell. As time goes by, actual revenue can be compared with the forecast revenue data to determine the effectiveness of the marketing strategy.

Marketing costs are easier to forecast than revenue, because these activities are largely controlled by the business. Calculating the projected marketing revenue is much more difficult because of changes in the external environment, over which the business has little or no control. However, being able to accurately analyse both projected costs and revenues allows the business to forecast profit levels.

9.7.3 Comparing actual and planned results

Performance indicators are the means by which a business can measure its performance and evaluate the degree to which it is achieving its objectives. Three key performance indicators used to measure the success of the marketing plan are:

1. sales analysis
2. market share analysis
3. marketing return on investment.

sales analysis the comparing of actual sales with forecast sales to determine the effectiveness of the marketing strategy

Sales analysis

A **sales analysis** uses sales data to evaluate a business's current performance and the effectiveness of a marketing strategy. The more the sales figures are broken down, the clearer the picture becomes, as can be seen by examining table 9.2.

TABLE 9.2 Sales analysis: sales revenue by territories — 1st quarter

Sales territory	Sales quota ($)	Actual sales ($)	Difference ($)	% change (– decrease + increase)
1	50 000	58 000	8 000	+16.0
2	80 000	85 000	5 000	+6.3
3	70 000	76 000	6 000	+8.6
4	65 000	72 000	7 000	+10.8
5	90 000	94 000	4 000	+4.4
Total sales revenue	355 000	385 000	30 000	+8.4

To calculate the difference, use the formula Actual sales – Sales quota.

To calculate the % change, use the formula $\frac{\text{Difference}}{\text{Sales quota}} \times 100$

BizFACT

The use of computerised sales has made the collection, storage, retrieval and analysis of sales data much easier. Computerised sales reports can be prepared, showing:

- daily, weekly, monthly, quarterly and yearly sales reports
- product line sales
- credit as opposed to cash sales analysis
- sales reports for individual sales representatives
- company division sales reports
- any combination of the above.

A cursory glance at the bottom line of table 9.2 shows that the total sales revenue has increased by $30 000 or 8.4 per cent above the quota — a pleasing result and confirmation that the marketing plan is a success.

The main strength of sales analysis is that sales figures are relatively inexpensive to collect and process. Their main weakness, however, is that data for sales revenue do not reveal the exact profit level; such information can only be gleaned from further investigations of total expenditure.

Market share analysis/ratios

Just as sales can be analysed, so too can a business's market share. By undertaking a market share analysis, a business is able to evaluate its marketing strategies as compared with those of its competitors. This evaluation can reveal whether changes in total sales, either increases or decreases, have resulted from the business's marketing strategies or have been due to some uncontrollable external factor. For example, if a business's total sales revenue declined but its market share remained stable, then the marketing manager can assume that overall industry sales have fallen, perhaps due to a downturn in the economy. However, if a business's total sales revenue and market share have declined, then the marketing strategies need to be reviewed. Businesses place a great deal of importance on analysing market share statistics — a 1 per cent fall in market share can represent millions of dollars in lost sales.

Marketing return on investment (ROI)

Sales and market share analyses, while useful, do not present the full picture. This can only be done by analysing the marketing costs involved with each marketing strategy. At the most basic level, **marketing ROI** measures how much revenue a marketing campaign is generating compared to the cost of running that campaign. Basically, it's how a business can measure the impact of their marketing strategies on their revenue growth. It gives them a holistic view of their efforts and the impact it is having on their business, allowing them to justify marketing spend and budget for current and future initiatives.

In order to calculate the marketing ROI, you take the sales growth from that business or product line, subtract the marketing costs, and then divide by the marketing cost.

$$\frac{(\text{Sales Growth} - \text{Marketing Cost})}{\text{Marketing Cost}} \times \frac{100}{1} = \text{Marketing ROI}$$

So, if sales grew by $2000 and the marketing campaign cost $200, then the simple ROI is 900 per cent.

$$\frac{(\$2000 - \$200)}{\$200} \times \frac{100}{1} = 900\%$$

Let's say we have a company that averages 4 per cent organic sales growth and they run a $10 000 campaign for a month. The sales growth for that month is $15 000. The calculation goes:

$$\text{Return on Marketing Investment} = \frac{\$15\,000 - \$10\,000}{\$10\,000} \times \frac{100}{1} = 50\%$$

By comparing the costs of specific marketing activities with the results achieved, a marketing manager can assess the effectiveness of each activity. This evaluation also helps in deciding how best to allocate marketing resources in the future. A good marketing ROI is 5:1.

marketing ROI measures how much revenue a marketing campaign is generating compared to the cost of running that campaign

9.7.4 Revising the marketing strategy

Once the results of the sales, market share and profitability analysis have been calculated, the business is now in a position to assess which objectives are being met and which are not. Based on this information, the marketing plan can be revised (modified). Revision of the marketing plan is equally as important as all the other steps involved in creating successful marketing strategies.

Changes in the marketing mix

Because the marketing plan is operating in a dynamic business environment, the marketing mix will constantly need to be revised. Changes that could be introduced include:

- *production modifications*. No product is perfect. Businesses that continually upgrade their products will be able to maintain a competitive advantage.
- *price modifications*. Prices fluctuate due to a variety of reasons. Therefore, the price component of the marketing mix will need to be revised in response to changes in the external business environment.
- *promotion modifications*. Promotion costs will be high when a new product is first launched onto the market. During the later stages of the product's life cycle, promotion costs may stabilise and even fall during the decline stage. Promotion strategies will, therefore, need to change over time corresponding to the life cycle of the product.
- *place modifications*. As a product's success increases, the distribution channels will need to be expanded to cater for the growing market. New overseas markets may be tapped, while old markets may decrease due to demographic changes. With the development of electronic communications, new distribution channels, such as the internet, may be used.

New product development

The product life cycle tells us that all products have a life span of somewhere between five to 10 years. Therefore, if a business wants to achieve long-term growth, it must continually introduce new products. For example, if Sony had stopped product development at the transistor radio, it would probably be out of business today. However, Sony, like many other large businesses, spends vast amounts on research and development (R&D) to stay at the forefront of technology and introduce new products.

FIGURE 9.21 R&D helps keep products innovative, which assists companies to achieve a competitive advantage. Samsung invests in R&D more than any other technology company, having spent more than $14.9 billion in 2020. This investment allows them to develop and produce some of the most sought-after electronic parts and is a major contributing factor to their success.



Product deletion

To maintain an effective product mix, a business will have to eliminate some lines of products. This is called **product deletion**. Outdated products may create an unfavourable image and this negativity may rub off on other products sold by the business. Most businesses find it difficult to delete a product, especially if it has been successful for a long time. However, when a product is in the decline stage, a decision will eventually have to be made to either delete or redevelop the product.

product deletion the elimination of some lines of products

BizFACT

Car manufacturers continually delete models due to poor performance or the introduction of new models. In 2013 Mazda made the decision to discontinue the CX-7 and Tribute to make way for the CX-5. The CX-5 is more fuel efficient, has more cargo capacity and overall interior volume than the CX-7 and is better able to compete more directly with other small SUVs.

on Resources

Weblink iSentia

KEY IDEAS

- Implementing the marketing plan means putting the marketing strategies into operation.
- Once the marketing plan has been implemented, it must be carefully monitored and controlled.
- Monitoring means checking and observing the actual progress of the marketing plan.
- Controlling involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained.
- When evaluating alternative marketing strategies, a business must develop a financial forecast that details the costs and revenues for each strategy.
- Developing a financial forecast requires two steps.
  - Step 1: Estimate the cost of the marketing plan.
  - Step 2: Estimate the revenue (sales) the marketing plan is expected to generate.
- Three key performance indicators used to measure the success of the marketing plan are:
  - sales analysis
  - market share analysis
  - marketing return on investment (ROI).
- The marketing plan can be revised by:
  - changes in the marketing mix
  - new product development
  - product deletion.

9.7 Activities

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9.7 Quick quiz on	9.7 Exercise	9.7 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 4, 5, 11, 12	1, 2, 6, 7, 8, 9, 10, 13, 14, 15, 17	16, 18

9.7 Exercise

Revision

1. **Why** is the implementation stage as important as developing marketing objectives?
2. a. **Distinguish** between 'monitoring' and 'controlling'.
   b. **How** are the two processes linked?
3. Research online to examine the function of the company iSentia.
   a. **Outline** the role of iSentia.
   b. **State** iSentia's mission.
   c. Select a 'Products and Services' that interests you and explain how a business would use this product or service.
4. **Recall** the two questions a marketing manager needs to ask in the controlling process.
5. **Summarise** the two steps involved in developing a financial forecast.
6. **Why** is it easier for a business to forecast marketing costs than revenue?
7. A business has a sales potential of $90 000 but achieves actual sales of only $25 000.
   a. **Deduce** what this signifies.
   b. **Propose** what the business should do next.
8. 'Any business that fails to conduct a sales analysis will not be able to assess the effectiveness of its marketing strategies.' **Discuss**.
9. **Examine** the following market share results for Electronic Appliances Ltd.

Year	Sales revenue ($ million)	Market share (%)
2018	28	18
2019	25	18
2020	33	14

   a. **Explain** how it is possible for sales revenue to decrease between 2018 and 2019 but market share to remain the same.
   b. If you were the marketing manager, **calculate** with which year's results you would be most pleased. **Justify** your answer.
10. **Distinguish** between 'sales analysis' and 'market share' analysis.
11. **Clarify** the importance of a marketing profitability analysis.
12. **Summarise** four changes that could be made to revise the marketing mix.
13. **Distinguish** between 'new product development' and 'product deletion'. Provide examples in your answer.
14. **Calculate** the marketing return on investment (ROI) for a business that spent $50 000 on a new marketing campaign and experienced a growth in sales of $10 000.

Extension

15. **Account** for why a business's marketing performance should be constantly evaluated. **Investigate** some methods that can be used to measure the effectiveness of a marketing plan.

You have just been appointed marketing manager for Apollo Tracksuits Pty Ltd. One of your first tasks is to analyse total industry sales and product line sales revenue breakdown, as shown in tables 9.3 and 9.4. Then complete questions 16 to 18.

TABLE 9.3 Apollo Tracksuits Pty Ltd — company sales and total industry sales, 2016–2020

Year	Apollo sales ($ millions)	Industry sales ($ millions)	Apollo market share (%)
2016	5	38	
2017	7	44	
2018	10	81	
2019	9	70	
2020	12	89	

TABLE 9.4 Apollo Tracksuits Pty Ltd — product line sales, 2017

Product	Sales quota ($ millions)	Actual sales ($ millions)	Difference ($)	(%)
Techno Tracks	2	1		
Weekenders	3	1.5		
Sports Plus	2	2		
Image Track	2	2.5		
No Sweat Tops	3	3		

16. Calculate a market share analysis by completing table 9.3. **Create** a report on your results.
17. The actual sales and sales quota figures for each product are shown in table 9.4. Complete the table. **Deduce** what these figures indicate.
18. **Determine** what suggestions you would make to improve the actual sales performance.

9.7 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q16

A bathroom products business cannot sustain the production of their current range. A consultant has advised the business to reduce the product range.

The actual and planned results for the entire year are shown.

Bathroom product	Actual results Jan–Jun (units)	Planned results Jan–Jun (units)	Actual results Jul–Dec (units)	Planned results Jul–Dec (units)
Coconut Handwash	7 500	7 500	10 000	9 000
Lavender Bodywash	8 000	8 500	8 500	9 500
Blueberry Handcream	7 000	6 000	7 500	8 000
Peppermint Bath Salts	8 000	7 000	8 500	10 000

By comparing actual and planned results, which product should be deleted?

A. Coconut Handwash
B. Lavender Bodywash
C. Blueberry Handcream
D. Peppermint Bath Salts

Question 2 (5 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q22a & b

A business develops video games. It had three different games for sale last year. The table shows forecast and actual sales for each game.

	Forecast sales ($)	*Actual sales* ($)
Game A	500 000	495 000
Game B	200 000	100 000
Game C	300 000	800 000

A. Why is this information an important part of the marketing process? **(2 marks)**
B. With reference to the information, recommend a strategy for promoting game *B*. **(3 marks)**

Question 3 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q19

The following is an extract from the end of year marketing report for a business.

	Planned sales ($)	*Actual sales* ($)	*Variance from target* %
Region *A*	1 200 000	1 00 000	
Salesperson 1			25
Salesperson 2			-50
Salesperson 3			-25
Region *B*	1 00 000	1 00 000	
Salesperson 4			50
Salesperson 5			50
Salesperson 6			-75
Region *C*	800 000	1 000 000	
Salesperson 7			33
Salesperson 8			50
Salesperson 9			0

Which of the following is suggested by the data?
A. Salesperson 1 is the least successful salesperson in the least successful region.
B. Salesperson 4 is the most successful salesperson in the least successful region.
C. Salesperson 7 is the least successful salesperson in the most successful region.
D. Salesperson 8 is the most successful salesperson in the most successful region.

Question 4 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q18

Use the following information to answer the question.

Extract from marketing report for Star Car Pty Ltd

	Star Car Sales in each country ($)		*Star Car's % of the car market in each country*	
	2010	*2011*	*2010*	*2011*
Country A	10 million	12 million	10	12
Country B	10 million	12 million	10	10
Country C	10 million	10 million	10	8
Country D	10 million	8 million	10	6

Note: The price of the cars remained unchanged from 2010 to 2011.

In 2011 Star Car Pty Ltd's main marketing objective was to take sales away from its competitors. In which country was this objective least effective?

A. Country A
B. Country B
C. Country C
D. Country D

Question 5 (1 mark)

Source: HSC 2002 Business Studies Exam, Section I, Q9

What is the function of management that involves comparing sales figures for a financial period to the forecast of sales for the same period?

A. Collecting market research data
B. Comparing cash and credit sales
C. Implementing financial plans
D. Monitoring the achievement of marketing plans

More exam questions are available in your learnON title.

9.8 Review

9.8.1 Summary

Situational analysis

- A marketing plan gives a purpose and direction to all the business's activities.
- The steps involved in the marketing process are:
  - situational analysis
  - market research
  - establishing marketing objectives
  - identifying target markets
  - developing marketing strategies
  - implementation, monitoring and controlling.
- A situational analysis provides a precise understanding of the business's current position and where it is heading.
- A SWOT (strengths, weaknesses, opportunities and threats) analysis provides the information needed to complete the situational analysis and assesses the business's position compared with its competitors.
- The product life cycle consists of the stages a product passes through: introduction, growth, maturity and decline.
- At each stage of the product's life cycle a different marketing strategy is necessary.

Market research

- Market research is the process of systematically collecting, recording and analysing information concerning a specific marketing problem.
- To obtain reliable and accurate information, marketers follow a three-step approach.
  - Step 1: Determining information needs. The problem is clearly stated to determine what needs to be measured and the issues involved.
  - Step 2: Collecting data from primary and secondary sources. Data are collected by mail, telephone and personal surveys, personal observation or from private data sources.
    - Primary data: information from original sources. Example: interviews and surveys
    - Secondary data: information collected by other organisations. Example: reports and Australian Bureau of Statistics
- Step 3: Data analysis and interpretation. Determine what the data means.
- Statistics are processed to determine if responses show trends or patterns that can be used in the business.

Establishing market objectives

- Marketing objectives are the realistic and measurable goals to be achieved through the marketing plan.
- The marketing objectives should be more customer-oriented than the goals for the entire business, and should include specific targets to be met — for example, 'Increase market share by 5 per cent over 12 months'.
- Marketing objectives include:
  - Increase market share. Market share refers to the business's total share of the total industry sales for a particular market.
  - Expand the product range. Product mix is the total range of products offered by a business.
  - Maximise customer service. Customer service means responding to the needs and problems of the customer.

Identifying target markets

- A target market is a group of present and potential customers to which a business intends to sell its product.
- Sometimes a business may be able to identify a primary and a secondary target market.
- A business identifies and selects a target market so it can direct its marketing strategies to that group of customers.

- Businesses can choose one of three approaches to identifying and selecting a consumer target market:
  - mass marketing approach — the seller mass-produces, mass-distributes and mass-promotes one product to all buyers
  - market segmentation approach — the total market is subdivided into groups of people who share one or more common characteristics
  - niche market approach — a narrowly selected target market segment.

Developing marketing strategies

- Marketing strategies are actions undertaken to achieve the business's marketing objectives through the marketing mix.
- The marketing mix refers to the combination of the four Ps — product, price, promotion and place/distribution.
- Once the four Ps have been established, the business must then determine the emphasis it will place on each of the variables.
- A business may vary its marketing mix when it wants to reach different target markets.
- A product is a good or service that can be exchanged for money.
- The price is the amount of money a customer is prepared to offer in exchange for a product. It refers to the method or strategy the business uses to decide their prices.
- Promotion describes the methods used to inform, persuade and remind customers about a business's products.
- Place is the element of the marketing mix that deals with the channels of distribution: the ways of getting the product to the customer.

Implementation, monitoring and controlling

- Implementing the marketing plan means putting the marketing strategies into operation.
- Once the marketing plan has been implemented, it must be carefully monitored and controlled.
- Monitoring means checking and observing the actual progress of the marketing plan.
- Controlling involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained.
- When evaluating alternative marketing strategies, a business must develop a financial forecast that details the costs and revenues for each strategy.
- Developing a financial forecast requires two steps.
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- Three key performance indicators used to measure the success of the marketing plan are:
  - sales analysis
  - market share analysis
  - marketing return on investment (ROI).
- The marketing plan can be revised by:
  - changes in the marketing mix
  - new product development
  - product deletion.

9.8.2 Key terms

controlling involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained
customer service how well a business meets and exceeds the expectations of customers in all aspects of its operations
financial forecast the business's predictions about the future
implementation process of putting marketing strategies into operation
market research the process of systematically collecting, recording and analysing information concerning a specific marketing problem
market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics
market share the business's share of the total industry sales for a particular product
marketing data the information relevant to the defined marketing problem
marketing mix refers to the combination of the four elements of marketing, the four Ps — product, price, promotion and place — that make up the marketing strategy
marketing objectives the realistic and measurable goals to be achieved through the marketing plan
marketing ROI measures how much revenue a marketing campaign is generating compared to the cost of running that campaign
marketing strategies actions undertaken to achieve the business's marketing objectives through the marketing mix
mass marketing approach a marketing approach that seeks a large range of customers
monitoring the process of measuring actual performance against planned performance
primary data the facts and figures collected from original sources for the purpose of the specific research problem
primary target market the market segment at which most of the marketing resources are directed
product deletion the elimination of some lines of products
product life cycle the stages a product passes through: introduction, growth, maturity and decline
product mix the total range of products offered by a business
sales analysis the comparing of actual sales with forecast sales to determine the effectiveness of the marketing strategy
secondary data information that has already been collected by some other person or organisation
secondary target market a smaller and less important market segment than the primary target market
statistical interpretation analysis the process of focusing on the data that represents average, typical or deviations from typical patterns
survey the gathering of data by asking or interviewing people
SWOT analysis involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment
target market a group of present and potential customers to which a business intends to sell its product

on Resources

Digital documents	Key terms glossary (doc-35666) Chapter crossword (doc-36216)
Interactivity	Chapter crossword (int-7161)
Exam question booklet	Chapter 9 Exam question booklet (eqb-0031)

9.8 Activities

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Exercise 1: Multiple choice questions

1. Which of the following is NOT an example of secondary data?
   - **A.** Focus group
   - **B.** Government report
   - **C.** Financial data and statistics
   - **D.** Report from the Australian Bureau of Statistics

2. Which step is the implementation, monitoring and controlling stage of developing a marketing plan?
   - **A.** The final step of the process and involves conducting a SWOT analysis
   - **B.** The final step of the process and includes revising the marketing strategy to check that it is working
   - **C.** The fifth step of the process and involves consideration of who the business is planning to sell to
   - **D.** The final step in an ongoing cycle, which focuses on how the business will achieve its business objectives

3. A SWOT analysis is an important tool for a business to use to understand internal and external factors that affect the business. What does the internal assessment of the SWOT analysis include?
   - **A.** Strengths and weaknesses; for example, past failures
   - **B.** Opportunities and threats; for example, how new regulations will affect the business
   - **C.** Strengths and weaknesses; for example, how new technology affects the business
   - **D.** Opportunities and threats; for example, how strong the business's current financial situation is

4. What stage of the product life cycle is price skimming usually associated with?
   - **A.** Decline
   - **B.** Introduction
   - **C.** Growth
   - **D.** Maturity

5. What is the best approach to obtaining reliable information on a specific marketing issue?
   - **A.** A SWOT analysis, which includes investigating strengths, weaknesses, opportunities and threats
   - **B.** Market research, which includes determining information needs, and collecting and analysing data
   - **C.** A product life cycle analysis, which is used to determine the stage of the product and the most appropriate marketing strategies to match it
   - **D.** Development of a marketing plan, which includes situational analysis, establishing market objectives and developing market strategies

6. Paulo's Pies is using taste-testing sessions to find out what people think of their pies. What is the information gained during this process an example of?
   - **A.** Secondary data, through internal sources
   - **B.** Primary data, through the observation method
   - **C.** Secondary data, through external sources
   - **D.** Primary data, through the survey method

7. Which of the following would BOTH form part of a situational analysis?
   - **A.** SWOT and product life cycle
   - **B.** SWOT and business life cycle
   - **C.** Business life cycle and SWAT
   - **D.** Product life cycle and business life cycle

8. Which of the following are the three steps of the market research process in the correct order?
   - **A.** Determine information needs, data collection, data analysis and interpretation
   - **B.** Data collection, determine information needs, data analysis and interpretation
   - **C.** Data collection, data analysis and interpretation and prepare a report analysing results
   - **D.** Determine information needs, data analysis and interpretation, prepare a report analysing results

9. As a result of a SWOT analysis, a café owner discovers that a new restaurant is opening nearby. The owner of the café then decides to extend their opening hours and alter their menu. The aim of this strategy is to use
   A. a strength to overcome a threat.
   B. a strength to overcome a weakness.
   C. an opportunity to overcome a threat.
   D. an opportunity to overcome a weakness.

10. Pampered Pooches makes specialised dog products, mostly for injured or older dogs, such as dog strollers and portable stairs to help dogs climb into cars. What would be the best marketing strategy to appeal to their target market?
   A. Mass marketing approach
   B. Market segmentation approach
   C. Niche market approach
   D. Secondary target market approach

Exercise 2: Exam practice questions

Question 1 (2 marks)
Identify TWO possible market objectives.

Question 2 (4 marks)
Outline TWO strategies businesses can use to monitor and control their marketing process.

Question 3 (2 marks)
Explain why it's important for businesses to identify and select a target market.

Question 4 (2 marks)
Identify one stage of the product life cycle and **recommend** an appropriate marketing strategy for a business in that stage.

Question 5 (2 marks)
Distinguish between the mass marketing and market segmentation approaches.

Question 6 (4 marks)
Assess why it is crucial for a business to conduct market research.

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10 Marketing strategies

10.1 Overview

LEARNING SEQUENCE

10.1 Overview
10.2 Market segmentation
10.3 Product and service differentiation and positioning
10.4 Products — goods and services
10.5 Price
10.6 Promotion
10.7 Place and distribution
10.8 People, processes and physical evidence
10.9 E-marketing
10.10 Global marketing
10.11 Review

There are a variety of marketing strategies businesses can adopt to satisfy the needs and wants of target customers. The main goal of a marketing manager is to develop and maintain a marketing mix that matches the needs of customers in the target market.

The main marketing strategies are the marketing mix, which consists of four elements: product, price, promotion and place (as mentioned in chapter 9). Reference was also made to the three Ps of marketing — which when combined with the original four Ps creates the **extended marketing mix**. Together, these seven Ps make up the main strategies of marketing and become the centrepiece of the marketing plan (see figure 10.1).

extended marketing mix the combination of people, processes and physical evidence with the four main elements of the marketing mix

FIGURE 10.1 The seven Ps of the extended marketing mix. The marketing mix may be varied when a business wants to reach different target markets.



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Digital document Key terms glossary (doc-35641)
Exam question booklet Chapter 10 Exam question booklet (eqb-0032)

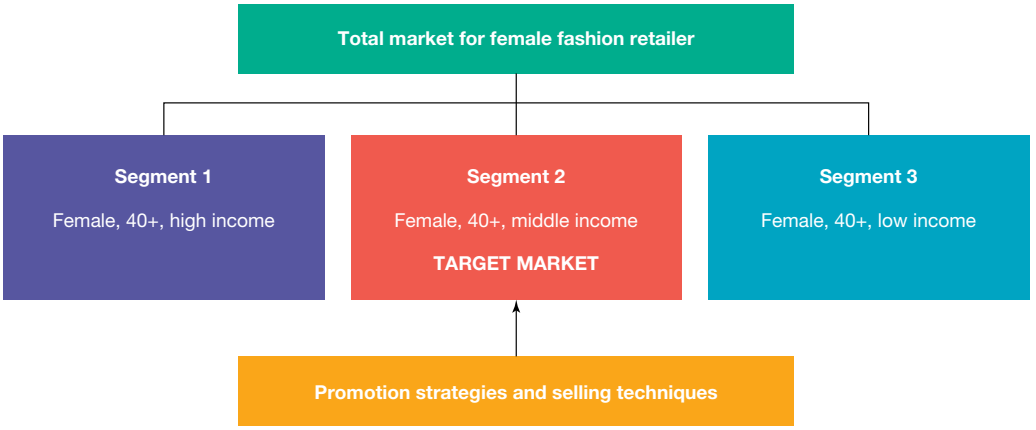
10.2 Market segmentation

SYLLABUS LINK In this subtopic you will learn about market segmentation as a marketing strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

As was outlined in chapter 9, **market segmentation** involves dividing the total market into groups of people who share one or more common characteristics. Once the market has been segmented, the marketing manager selects one of these segments to become the target market (see figure 10.2). Often a business will implement a specific marketing mix to each target market that the business wants to sell to.

FIGURE 10.2 Selecting a market segment to be the target market is important. In this example, the fashion retailer makes clothes for women over 40 years of age. The clothes are of a reasonable quality but would not be classed as 'designer' clothes. In this business, female middle-income earners are the main target market.



The ultimate aim of market segmentation is to increase sales, market share and profits by better understanding and responding to the desires of the different target customers.

market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics

segmentation variable a characteristic of an individual or group that is used by marketing managers to divide a total market into segments

10.2.1 Segmenting consumer markets

A **segmentation variable** is a characteristic of an individual or group that is used by marketing managers to divide a total market into segments. The consumer market can be segmented according to four main variables: demographic, geographic, psychographic and behavioural (see table 10.1).

TABLE 10.1 Common variables for segmenting customer markets

Demographic	Geographic	Psychographic	Behavioural
• Age • Gender • Education • Occupation • Income • Social class • Religion • Ethnicity	• Region • Urban • Suburban • Rural • City size • Climate • Landforms	• Lifestyle • Personality • Motives • Socioeconomic group • Consumer opinions and interests	• Purchase occasion • Benefits sought • Loyalty • Usage rate • Price sensitivity

Demographic segmentation

Demographic segmentation is the process of dividing the total market according to particular features of a population, including the size, age, sex, income, cultural background and family size. Due to the ease with which these demographic variables can be measured, their use is widespread amongst marketers.

Age and gender are two of the most widely used demographic variables for segmentation purposes. The marketing of sparkling and still beverages is typical of this. Coca-Cola, for example, targets 15- to 35-year-old males with the energy drink Mother. The more health-conscious adult market is served with Diet Coke, Deep Spring Natural Mineral Water or Fuze Iced Tea. The primary target market for Fanta is 13- to 16-year-olds. Mount Franklin is aimed at younger females and families, whereas for Powerade and Pump, the core market is 18- to 24-year-old males who are engaged in athletics — the 'active consumer'.

demographic segmentation the process of dividing the total market according to particular features of a population, including the size of the population, age, sex, income, cultural background and family size

geographic segmentation the process of dividing the total market according to geographic locations

FIGURE 10.3 Nike segments the market using mainly demographic variables. Nike primarily targets consumers aged between 15 and 45. In recent years, the company planned to grow the business further by focusing on three key demographics: women, young athletes and runners. Nike expanded women's apparel and product lines and invested in sponsorships of local clubs and partnerships with professional athletes to appeal to the younger demographic.



Geographic segmentation

Since people in different locations are bound to display different characteristics and have a variety of wants and needs, geographic segmentation can be important. **Geographic segmentation** is the process of dividing the total market according to geographic locations. This type of segmentation is based on the geographic units themselves (countries, states, cities, etc.), but also on various geographic factors, such as climate, cultural preferences, populations and more.

Businesses may divide the consumer market into regions because consumers in different geographical locations have different needs, tastes and preferences. Consequently, the marketing mix may differ from one geographic region to another. For example, McDonald's serves beer in their German restaurants, but not in the US. This reflects the difference in drinking preferences between the two cultures. They've also incorporated local foods on their menu in some locations — the McArabia in the Middle East, banana pie in Brazil and the McVeggie salsa bean burger in India. Although most of its marketing mix elements will be common across all locations, regional variations require modifications to suit the particular local culture.

Sometimes the size of the city can be an important segmentation variable. One franchise fast-food business will not locate in cities of less than 25 000 people. Climate also has an impact on segmenting markets for businesses selling heating and cooling systems as well as clothing. Consumers in Jindabyne will need snow chains and heavy outdoor clothing, but consumers in Port Macquarie are more interested in lightweight clothing.

psychographic segmentation
the process of dividing the total market according to personality characteristics, motives, opinions, socioeconomic group and lifestyles

Psychographic segmentation

Personality and self-concept have been found to influence the clothes, hair styles, make-up, entertainment and motor vehicles that individuals will purchase. **Psychographic segmentation** is the process of dividing the total market according to personality characteristics, motives, opinions, socioeconomic groups and lifestyles. When segmenting a market according to psychographic variables, a business would research a consumer's brand preferences, favourite music, radio and television programs, reading habits, personal interests and hobbies, and values.

FIGURE 10.4 Blackmores' target market is predominantly women aged 20 to 49. This group is then further segmented according to their primary areas of interest and motives: general wellbeing, weight, pregnancy and fitness. Blackmores' strategy is to produce a highly-targeted creative marketing campaign for each of these segments.



Psychographic variables focus on why people behave the way they do. An average Toyota Corolla owner compared with an average Porsche Cayman S owner, for example, will respond quite differently about the cost of vehicle maintenance, insurance and accessories.

Psychographic variables can be used by themselves to segment a market, or they can be combined with other types of segmentation variables. However, unlike demographic variables, psychographic variables can sometimes be difficult to accurately measure, especially personality characteristics and lifestyle.

BizFACT

The shampoo industry uses psychographics to segment the market. The attitudes and values of customers are important when segmenting the market and many companies develop specific products to target certain lifestyles as well as satisfying different needs; for example, anti-dandruff, detangler, volumising, moisturising.

Behavioural segmentation

Behavioural segmentation is the process of dividing the total market according to the customers' relationship to the product. This includes customers' knowledge of, attitude towards, use of, or benefits sought from the product. A total market, for example, may be divided into users and nonusers. Users can then be classified as heavy, moderate or light. To encourage light and moderate users to purchase more of its products, a business may have to redesign the product, set special prices and implement special promotion activities.

behavioural segmentation the process of dividing the total market according to the customers' relationship to the product

FIGURE 10.5 The loyalty of the customer can also be used for behavioural segmentation. The best example of this is in the hospitality industry where hotels, restaurants and airlines provide their best service to their most loyal customers. For example, the Qantas Club is a membership program that gives members access to Qantas Club Lounges in Australia, as well as international lounges at airports around the world.



Identifying what the customers want from the product — the benefits sought — is an important aspect of behavioural segmentation. By determining the benefits desired, marketers can design products that directly satisfy these desires.

SNAPSHOT

Case study: The six buyer segments in the property market

Our demographic shape is changing; there are six distinct buyer segments in the Australian property market:

1. Young renters
2. First home buyers
3. Upgraders
4. Downsizers
5. Retirees
6. The aged care market.

Looking ahead, the demand from young renters and upgraders is set to decline; while that from aged care will likely remain steady.



The stand out groups (those set to be the main drivers of Australia's housing demand over the next ten years) are first home buyers, those downsizing and retirees.

It may surprise some, but first home owners are generally aged 35 to 44 years.

This group is projected to take up 20 per cent of our total new housing demand over the next decade.

What first home buyers are looking for in a property is the room to grow and the opportunity for property improvement. And naturally, affordability is a big consideration.

Preferred housing options for first home buyers vary, depending upon the location.

Some first home buyers opt for inner city apartments; some look to townhouses/duplexes and small houses in middle suburbs; and some prefer larger detached and dual-income homes in outer suburbs.

The downsizer demographic refers to those aged 60 to 74 years.

Almost all of this group (92 per cent) have no children living at home; while just on three-quarters are couples or live alone.

Downsizers are projected to take up 32 per cent of total new housing demand over the next decade.

Their preference is to remain in the same neighbourhood, close to friends, family and established ties.

What they are looking for is low maintenance, convenience, like-minded residents and small projects.

Some from this group are looking to experience inner city living — their preference is for spacious, well-priced, quality apartments.

This group also prefers compact housing like townhouses; villas and dual-income homes in both middle-ring and outer-ring suburbs.

Understanding Australia's real underlying housing need is more than just a matter of calculating population growth and average number of people per household.

Demographics will determine our future

It's our demographic profile — the change in our household formation — that will best determine future housing need.

But the right housing will need to be built; and importantly, at the right prices, in order to encourage key buyer groups to purchase.

At issue is lack of diversity in Australia's housing stock, and the ability for most to afford their housing preference.

Source: https://nakedrealestate.com.au/blog/the-six-buyer-segments-in-the-property-market, 3 May 2017.

KEY IDEAS

- The main goal of a marketing manager is to develop and maintain a mix of marketing strategies that matches the needs of customers in the target market.
- Marketing segmentation involves dividing the total market into segments.
- A business selects one of these segments to become the target market.
- The ultimate aim of market segmentation is to increase sales, market share and profits by better understanding and responding to the desires of the different target customers.
- The consumer market can be segmented according to four main variables:
  - demographic — features of a population
  - geographic — urban, regional and rural locations
  - psychographic — personality characteristics
  - behavioural — customers' relationship to the product.

10.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.2 Quick quiz on	10.2 Exercise	10.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 6, 7, 8	9, 11	5, 10

10.2 Exercise

Revision

1. **Identify** the seven marketing elements that make up the marketing mix.
2. **State** the link between market segmentation and target market.
3. **Recall** the ultimate aim of marketing segmentation.
4. **Summarise** the four main ways of segmenting consumer markets.
5. Here are five different market segments:
   - **a.** young married couple, no children
   - **b.** female teenager, part-time worker
   - **c.** older single person, female, retired
   - **d.** younger single person, male, working
   - **e.** male teenager, full-time student.

   Listed below are 10 products/services. Copy the list into your notebook and, beside each item, **determine** the most appropriate market segment letter (a–e) for that product/service. In some cases, you may want to write more than one letter. Compare your answers with those of the rest of the class.
   - **i.** Financial advice _____
   - **ii.** Ballet tickets _____
   - **iii.** Bus tour _____
   - **iv.** Dolly magazine _____
   - **v.** Health insurance _____
   - **vi.** Apple iPad _____
   - **vii.** Rover lawnmower _____
   - **viii.** School textbook _____
   - **ix.** Smartphone _____
   - **x.** Furniture _____

Read the 'The six buyer segments in the property market' case study and answer questions 6 to 9.

6. **Identify** the variables the property market uses to segment the market.
7. **Identify** the six distinct buyer segments in the Australian property market.
8. **Outline** the characteristics of the first home-buyer and downsizer segments.
9. **Explain** which segments are predicted to increase and decrease.

Extension

10. **Determine** why the mass marketing approach has declined in recent years. Discuss whether this means there is no place for mass marketing. Justify your answer.
11. Once the total market is segmented, a business selects a target market. **Demonstrate** the different ways in which a market may be segmented. **Why** does having a clear understanding of the target market improve the efficiency of the marketing plan?

10.2 Exam questions

Question 1 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q15

A gym has fitness-conscious office workers as its target market.

What type of market segmentation is this?

A. Geographic and behavioural
B. Geographic and demographic
C. Psychographic and behavioural
D. Psychographic and demographic

Question 2 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q7

A global pizza company changes the pizza sizes and toppings for each country in which it operates.

What is this an example of?

A. Differentiation
B. Standardisation
C. Global branding
D. Global consumers

Question 3 (1 mark)

Source: HSC 2010 Business Studies Exam, Section I, Q4

A manufacturer of dog biscuits would like to segment the market. Which of the following is a segmentation strategy that the manufacturer could implement?

A. Sourcing cheaper raw materials
B. Promoting to high income consumers
C. Changing the colour of the packaging
D. Rounding prices to the nearest fifty cents

Question 4 (1 mark)

Tyro Total Care has decided to market its health care service to the aged. Which term best describes this marketing strategy?

A. Research
B. Setting objectives
C. Situation analysis
D. Segmentation

Question 5 (3 marks)

A marketing consultant has advised a business to segment the market. Define the phrase 'segment the market' and describe the advantages of this strategy.

More exam questions are available in your learnON title.

10.3 Product and service differentiation and positioning

SYLLABUS LINK In this subtopic you will learn about product/service differentiation and positioning as a marketing strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Walk into any supermarket to buy a loaf of bread and you are faced with a wide selection from which to choose: white, wholemeal, sliced, unsliced, gluten-free, vitamin enriched, thick for toasting and so on. Providing so many different types of breads is a deliberate marketing strategy and is an example of **product/service differentiation**. This occurs when products that are the same or similar are made to appear different from and/or better than those of their competitors. By achieving this, the seller is able to gain a little more control in the marketplace, especially with price.

10.3.1 Points of differentiation

The difference could be as simple as changes to the packaging or labelling; or more complex, such as offering top-quality service, greater convenience, more features and better **value for money**, or products or services that are environmentally friendly. These factors all play a part in persuading consumers to perceive the product or service as being superior to all similar products or services and, therefore, influencing them to buy it. Examples include jeans with designer labels, washing detergent with brightener additives and an exclusive restaurant that offers full table service.

Four important points of differentiation are customer service, environmental concern, convenience, and social and ethical issues.

Customer service

Market research shows that consumers:

- *desire 'personalised' service:* products that are tailored to their individual needs and wants. Customers may require many different services before, during and after the purchase
- *require 'caring' service:* to be treated honestly, courteously and efficiently
- *want high quality and value:* a business needs to establish favourable conditions for service by offering fair prices and high-quality products.

Customer service can be a powerful marketing tool and a true point of differentiation in today's business environment.

Consumers expect a high level of customer service. Pre-sales and after-sales service are very important to consumers purchasing expensive items such as cars or electrical appliances.

Failing to provide excellent customer service will result in lost sales and damage the business's competitive position. Customer service should be the main feature to position a business head and shoulders above its competition. Simply meeting basic customer needs is not considered enough in today's marketplace. Businesses should always strive to exceed customer expectations.

Customer service may also include the presentation of the premises, the atmosphere, or the range of products that set a business apart and capture the consumer's interest.

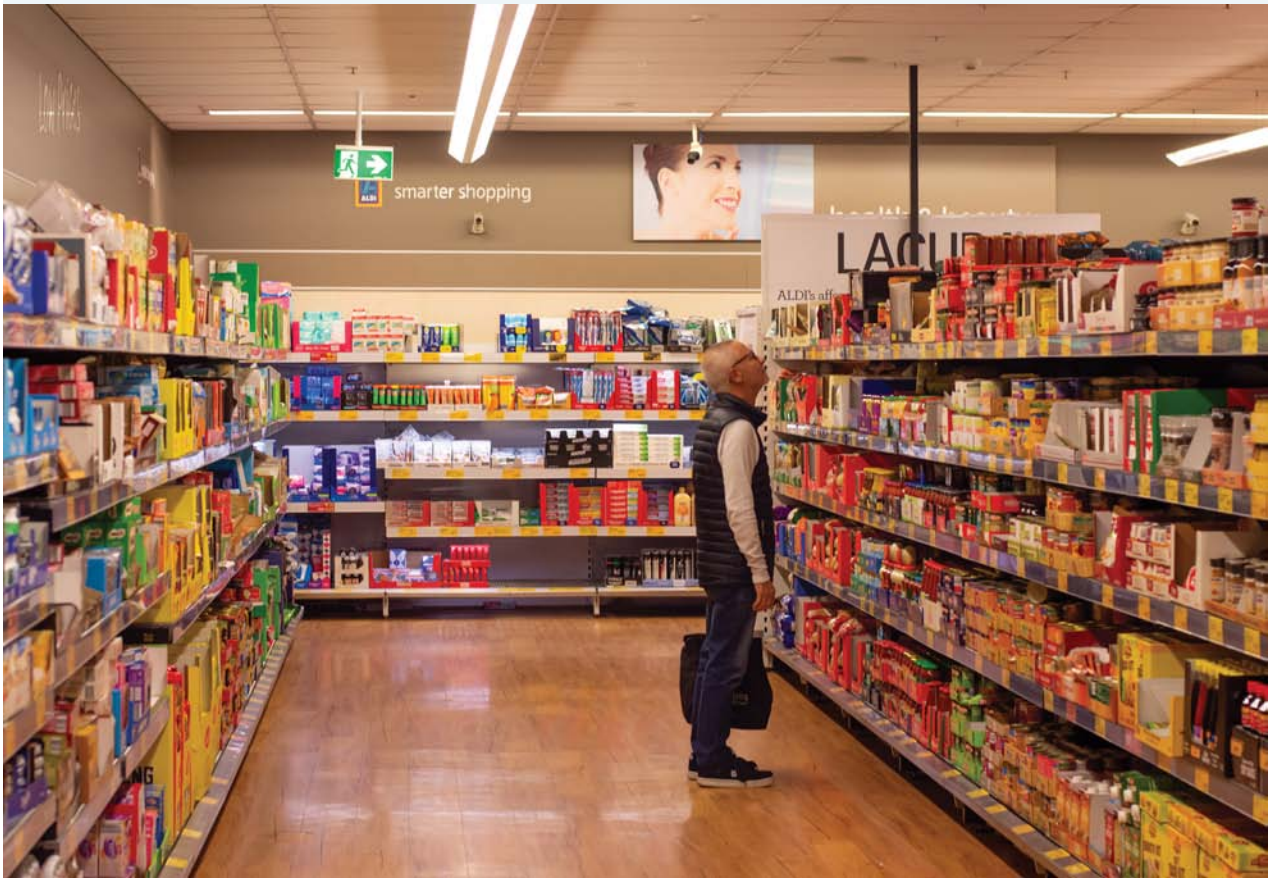
product/service differentiation the process of developing and promoting differences between the business's products or services and those of its competitors

value for money the desire to obtain the best quality, features and performance for a given price of a product

Environmental concerns

People are becoming more concerned with 'quality of life' issues, especially the physical environment. Businesses that create pollution may risk losing customers; whereas businesses that adopt a 'green' philosophy and produce environmentally friendly products may see their sales increase.

FIGURE 10.6 ALDI have made a strong commitment towards being environmentally sustainable. Their goals for 2025 are to ensure that all their packaging is reusable, recyclable or compostable, and to reduce packaging material on all products by 15 per cent. All of ALDI's consumable packaging includes a How2Recycle label that lets people know how to recycle each item and they have made their own private-label product packaging that's easier for customers to reuse.



Convenience

Because today's consumers are busy, they will often select products that are convenient to use. For example, many consumers do not have a lot of time for meal preparation. In response, food manufacturers have developed a range of convenience food products. The packaging and cooking requirements are designed to make the preparation as convenient as possible.

BizFACT

Woolworths has responded to people's need for businesses to cater to their busy, on-the-go lifestyles with a new "Pick up Drive thru" service. Their dedicated drive-throughs are one of the newest conveniences the supermarket has added. Supermarkets nowadays are all about speed, convenience and helping customers shop more easily. The old strategy of hiding milk at the back of the store has been replaced with strategies to make shopping more convenient.

Social and ethical issues

A growing number of consumers are becoming more ethically minded and will actively purchase products or brands that they believe do not exploit workers, producers or the environment. These consumers want to know more about the way goods are made, including the conditions in the factories and where they come from.

Ethical consumerism provides businesses with opportunities to satisfy the demands of this growing number of consumers. For example:

- In response to the dislike of genetically modified (GM) foods by some consumers, various producers are labelling their products as GM-free.
- The **Fair Trade movement** is gaining in influence, with consumers increasingly prepared to pay more for guarantees of fair labour practices and sustainable, organic products. The FAIRTRADE Mark, which represents an independent certification system, is one example of assuring fair labour practices.
- Many businesses are producing products using non-animal alternatives or methods associated with good animal welfare. For example, the cosmetic industry is delivering more natural products, not tested on animals.

FIGURE 10.7 The Iconic has developed a Considered Edit, a range of clothing, footwear and accessories that are made using a material or process that benefits humans, animals or the environment, or made by a brand that is positively contributing to the community around us. They've introduced values-based filters consumers can shop by, e.g. fair production or sustainable materials. Each considered item has to meet at least one of the five sustainability credentials, which is highlighted on the product page.



10.3.2 Product/service positioning

Closely tied to product/service differentiation is the practice of **product/service positioning**. This refers to the technique in which marketers try to create an image or identity for a product/service compared with the image of competing products or services.

Product/service positioning is something that is done in the minds of the target market: it is how potential buyers perceive the product. Some brand names, such as Rolex, Ferrari, Woolworths Essentials and Cotton On, can immediately evoke an image of the product's quality. This image gives the product its position within the market.

In highly competitive markets, sales may be difficult to secure. For this reason, a business will attempt to create an image that differentiates its product/service from the others. Many businesses invest considerable resources in the positioning of their product/service. The business will decide on the image it wishes to create for a product/service and will use other elements of the marketing mix to shape and maintain this image.

Whenever a new product is launched, the marketing manager needs to have clearly determined the desired positioning of the product/service. This will be achieved through the product/service's name, price, packaging, styling, promotion and channels of distribution. Combined, these individual characteristics create the image of the product/service.

Many companies have made a strategic decision to reposition themselves in their market (see figure 10.8 and the following case study). Repositioning focuses on changing what customers associate with the brand and sometimes competing brands. Some reasons companies reposition themselves include changing market conditions, decline in sales, desire to focus on a new target market, new competition and to overcome negative customer perceptions of the brand.

ethical consumerism involves buying products that are not harmful to the environment, animals and society

Fair Trade movement an alternative method of international trade that promotes environmentalism, fair wages, alleviation of global poverty and a fair price for farmers and workers

product/service positioning the technique in which marketers try to create an image or identity for a product compared with the image of competing products

FIGURE 10.8 Given the changing nature of entertainment and their struggles connecting with customers, Optus realised they would need to reposition themselves from simply delivering telecommunications to delivering a full experience of digital engagement. 'Yes' was an enduring part of the Optus brand since the 90s, but over time it lost meaning. In 2015 Optus rebranded and decoupled 'Yes' from their logo and created a standalone mark representing the voice of the customer: it's the customer response when Optus makes 'Yes Moments' happen.



SNAPSHOT

Case study: Zara — repositioning the brand in a move towards luxury



In order to reposition themselves as a premium brand, Zara hired an advertising agency to redesign their logo in 2019. This rebrand needed to align with Zara's new positioning and strategy of offering a wide range of products that look like popular higher-end fashion brands. The company wanted to be perceived as a luxury brand but also remain accessible to mainstream customers.

Zara's original 1975 logo was more spaced out and used a bold minimalist sans serif font to express their previous positioning of selling semi-premium products at lower prices. While the new logo still features a serif font and block capital letters, it shares a similarity to high-end brands such as Gucci, Cartier and Bulgari. The new design features a bolder serif, reduced spacing, accentuated curves to the 'Z' and 'R', elongated letters and a more complex overlapping design of letters to imitate the style of luxury fashion brands.

This new logo design imitates the style of other high-end labels and signals Zara's ambition to reposition themselves among these luxury brands. The new design attracted criticism from some designers, particularly typographers, who described the design and merging letters as 'claustrophobic', crowded and difficult to read. While it's not clean and simple, it was designed in this way to appeal to people's subconscious, which naturally connects complexity to luxury.

on Resources

Weblink Fair Trade

KEY IDEAS

- Product/service differentiation, in its broadest sense, is the process of developing and promoting differences between the business's products or services and those of its competitors.
- Four important points of differentiation are customer service, environmental concerns, convenience, and social and ethical issues.
- Product positioning refers to the technique in which marketers try to create an image or identity for a product/service compared with the image of competing products/services.

10.3 Activities

learnON

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10.3 Quick quiz on | **10.3 Exercise** | **10.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 11	3, 4, 5, 6, 7, 8, 9	10

10.3 Exercise

Revision

1. **Outline** the purpose of product/services differentiation.
2. For two specific products/services with which you are familiar, **describe** how they are differentiated from their competitors.
3. **How** can a business use customer service as a point of differentiation?
4. 'Environmentally friendly products are just a clever promotional strategy to make purchasers feel good.' **Justify** whether you agree or disagree with this statement.
5. Use the **Fair Trade** weblink to **examine** the ways the Fair Trade movement is committed to selling and production practices that are ethically responsible.
6. In small groups, choose a product/service with which you are familiar and **demonstrate** the types of positioning strategies used to promote it. Share your answer with the rest of the class. You may wish to prepare this as a PowerPoint presentation.

Read the 'Zara— repositioning the brand in a move towards luxury' case study and answer questions 7 to 9.

7. **Why** did Zara design a new logo?
8. **Explain** how the new logo aligns with their new positioning.
9. **Compare** Zara's previous positioning with their current one.

Extension

10. **Create** an A4 print advertisement for a new model mobile phone that highlights its 'exclusive' features. You may wish to use desktop publishing software to present the advertisement with text and graphics.
11. Research and **identify** four different businesses that have differentiated themselves in relation to either customer service, environmental concerns, convenience or social and ethical issues. For each business, explain how this differentiation has led to a competitive advantage.

10.3 Exam questions

Question 1 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q12

A car company advertises its new luxury car as more exciting and fun to drive than its competitors' cars.

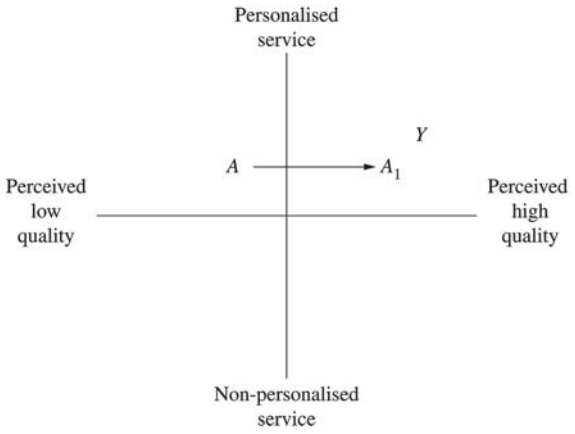
What strategy is the car company using?

A. Opinion leader
B. Personal selling
C. Positioning
D. Public relations

Question 2 (1 mark)

Source: HSC 2008 Business Studies Exam, Section I, Q11

The diagram shows the market position of Product *A* and of its competitor Product *Y*.



The marketing manager for Product *A* wishes to move the product from its current position at *A* to *A*1.

The marketing manager for Product *Y* would like to maintain Product *Y*'s current market positioning and customers.

Which strategy would best achieve this?

A. Reducing the price
B. Using intensive distribution
C. Developing a loyalty scheme
D. Advertising weekly in free local newspapers

Question 3 (1 mark)

Source: HSC 2001 Business Studies Exam, Section I, Q2

Positioning is a part of which business function?

A. Accounting
B. Finance
C. Marketing
D. Operations

Question 4 (4 marks)

Assess the role of positioning in the development of marketing strategies.

More exam questions are available in your learnON title.

10.4 Products — goods and services

SYLLABUS LINK In this subtopic you will learn about the branding and packaging of products — goods and/or services — as a marketing strategy.

You will also learn to explain why goods and/or services are central to both marketing and operations.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

When you buy a book or new phone you are purchasing a good. They are real, physical objects that can be touched and owned; they are *tangible*. Financial advice, television programs and sporting events provide an *intangible* service for our use or enjoyment, not for our ownership. However, services are products just the same. **Products** are goods or services that can be offered in an exchange for the purpose of satisfying a need or want.

It is convenient to group products as tangible goods or intangible services. In reality, it is not quite so simple. Most products are combinations of tangible and intangible components. Dinner at an expensive restaurant, for example, provides tangible elements (food and drinks) and intangible elements (efficient service, live music and a pleasant atmosphere). Consequently, when customers purchase products, they buy both the tangible and intangible benefits (attributes) — a **total product concept**. In other words, a product is a 'collection of satisfactions', which might include a variety of things such as the package, the brand name, the warranty and the after-sales service.

The term 'product', therefore, is a much broader concept than most people understand. Usually when people talk about products, they refer to what a company produces, such as motor vehicles or entertainment. And yet the intangibles that come with these products are also important. They can be used to differentiate one business's product from that of its competitor.

Often, with mass-produced products, it is on the differences in the intangible benefits that product competition is based. For example, cars are basically a means of transportation used to get from one place to another. If this was all they were, then there would be only one model. But a car contains a vast array of intangibles that are used to differentiate each model, such as image, reputation, style and safety record. Viewing the car in terms of a total product concept clearly shows that no two cars are exactly the same (see figure 10.9). All products, then, are a combination of tangible and intangible attributes.

products goods or services that can be offered in an exchange for the purpose of satisfying a need or want

total product concept the tangible and intangible benefits (attributes) a product possesses

FIGURE 10.9 Many Australians buy luxury cars because it not only satisfies their needs and wants, but also provides intangible benefits such as a feeling of prestige, importance or influence. Mercedes-Benz is currently the leading luxury vehicle brand in Australia.



10.4.1 Branding

Read the list of brand names in figure 10.10 and test yourself: what products do you associate with each brand name? Your score was probably 20 out of 20. You have just experienced the power of *brand name recognition*. The 20 businesses that market these brands have spent a lot of money making sure customers instantly recognise their brand name and the products associated with them. A **brand** is a name, term, symbol, design or any combination of these that identifies a specific product and distinguishes it from its competition. A **brand name** is that part of the brand that can be spoken. It may include letters (BMW motor vehicles); numbers (4711 perfume); numbers and letters (3M tapes); or pronounceable symbols, such as the ampersand (&) in Johnson & Johnson.

brand a name, term, symbol, design or any combination of these that identifies a specific product and distinguishes it from its competition

brand name that part of the brand that can be spoken

FIGURE 10.10 Examples of brand names

Apple	Kellogg's	McDonald's	Coca-Cola	Instagram
Uncle Tobys	Arnott's	Samsung	Google	Netflix
Toyota	Sorbent	Telstra	KFC	Speedo
Colgate	Cadbury	Qantas	Nike	Sony

BizFACT

According to Forbes' annual list of the World's Most Valuable Brands, the top five most valuable brands in the world in 2019 (in order) were Apple, Google, Microsoft, Amazon and Facebook. The top five companies that showed the biggest gains since last year's list were Netflix, Chanel, Amazon, Microsoft and PayPal.

Benefits of branding

Branding provides benefits for both buyers and sellers. Branding helps consumers:

- identify the specific products that they like. Without branding, a consumer selection would be quite random because buyers could have no guarantee that they were purchasing what they preferred
- evaluate the quality of products, especially when a consumer lacks the expertise to judge a product's features
- reduce their level of perceived risk of purchase. A respected and trusted brand will provide reassurance that the consumer is making the right choice
- gain a psychological reward that comes from purchasing a brand that symbolises status and prestige.

FIGURE 10.11 McDonald's proves their brand strength with their blurry ad campaign. These ads currently on display in some nations on billboards and social media are deliberately blurry and illustrate the strength of the McDonald's brand. Titled 'Say No More', this campaign celebrates how their red and yellow colour scheme and products are so iconic that people can still recognise blurred images of key menu items.



Branding helps businesses:

- gain repeat sales because consumers recognise the business's products
- introduce new products onto the market because consumers are already familiar with the business's existing brands
- with their promotional activities because the promotion of one product indirectly promotes all other similarly branded products
- encourage customer loyalty. This has the added benefit to the business of being able to charge a higher price for the product.

For these reasons, a brand name can be a powerful marketing tool. It is also why businesses spend a great deal of time, money and effort creating and protecting their brand name. McDonald's, for example, is one business that aggressively protects its brand name — which is a registered **trademark** — against infringement. It has brought legal proceedings against a number of businesses with 'Mc' names because it fears that the use of the 'Mc' will give consumers the impression that these businesses are owned or endorsed by McDonald's. The symbols ©, TM or R at the end of a brand name signify that the name or symbol is copyright protected or a registered trademark.

trademark signifies that the brand name or symbol is registered and the business has exclusive right of use

brand symbol or **logo** a graphic representation that identifies a business or product

BizFACT

In 2018 Dunkin' decided to drop the word 'Donuts' from the Dunkin' Donuts' brand name. 'Donuts' was dropped to reflect the fact that the chain is first and foremost a coffee chain, as opposed to a bakery. It also highlights the company's future, which is in coffee and beverages.

Branding — symbols and logos

A **brand symbol** or **logo** is a graphic representation that identifies a business or product.

Logos can be categorised into five basic types. Figure 10.12 demonstrates an example of each type in order:

- *Brandmark logo*: a solitary graphic that is not expressed in words. It is a pictorial mark with no text. Some businesses encourage the instant recognition of their brand symbol rather than their brand name, e.g. Apple.
- *Wordmark logo*: where the logo is literally the name of the business. Since there's no imagery, these logos rely heavily on typography to stand out, e.g. Coca Cola.
- *Lettermark logo*: a typography-based logo that's comprised of a few letters, usually a company's initials, to represent the brand, e.g. Hewlett Packard.
- *Combination mark logos*: contain a combination of a brandmark and a wordmark, e.g. Pepsi.
- *Emblem*: similar to combination mark logos, these logos combine images with text. The difference is that emblem logos encapsulate these design features within a frame or border, e.g. Starbucks.

FIGURE 10.12 Brand symbols or logos assist in the easy recognition of a product. Each of these logos represents one of the five basic types of logo.



BizFACT

Brand counterfeiting is especially detrimental because the usually inferior counterfeit product weakens consumers' trust in the brand and their loyalty to it.

Branding strategies

Brands are usually classified according to who owns them. When a manufacturer owns a brand name it is referred to as a **manufacturer's brand** or **national brand**. Common examples of manufacturer's brands include Sunbeam appliances, Kraft foods and Billabong clothing. These brands have high appeal with customers because they are recognised across the country, are widely available and offer reliability with constant quality.

A **private** or **house brand** is one that is owned by a retailer or wholesaler. These products are often cheaper because the retailer or wholesaler can buy at lower costs. For example, Myer sells products from its own label, including Reserve, Basque, Urbane, Blaq, Soho, Vue and Miss Shop.

Generic brands are products with no brand name at all. Carrying only the name of the product and in plain packaging; these generic brands have been available in supermarkets since the mid 1970s. Examples include Black and Gold (IGA), Essentials and Macro (Woolworths), Coles Finest (Coles) and SimplyNature (Aldi).

manufacturer's brand or **national brand** a brand owned by a manufacturer

private or **house brand** a brand that is owned by a retailer or wholesaler

generic brands products with no brand name at all

packaging the development of a container and the graphic design for a product

10.4.2 Packaging

Packaging involves more than simply putting the product in a container or placing a wrapper around it. **Packaging** involves the development of a container and the graphic design for a product.

To assist sales, the packaging of a product is sometimes as important as the product itself. Well-designed packaging will give a positive impression of the product and encourage first-time customers. For example, tasteful packaging can create an image of luxury, sensuality and exclusiveness, helping to promote the product. In addition, packaging:

- preserves the product
- protects the product from damage or tampering
- attracts consumers' attention
- divides the product into convenient units
- assists with the display of the product
- makes transportation and storage easier.

FIGURE 10.13 In 2014 Aldi expanded its private brand offering and joined Coles and Woolworths by developing an organic product range to sell under a new generic brand. ALDI debuted its 'SimplyNature' store brand, which features organic and natural products made with only all-natural or organic ingredients.



Apart from performing these practical functions, packaging also acts as a form of communication. Consumers see certain colours and draw conclusions about the product even before they read the label. For example, a red soft-drink can means cola; green means lemon-lime. Dishwashing liquid in a yellow container is considered 'lemony' and a household cleaner in a green package is associated with an environmentally-friendly product. Many products packaged in black or gold portray an image of luxury and sophistication.

Sometimes, the shape of the packaging can become part of the product itself. That is, consumers readily associate a unique shape with a specific product. For example, one of the most easily recognised shapes in the soft-drink market is the distinctive 'pinched in at the waist' Coke bottle. In 1977, Coca-Cola gained trademark protection by the United States Patent Office. Coca-Cola argued that the 'distinctively shaped contour' had become so well known it had taken on trademark status. Coca-Cola is also the registered owner of a number of Australian trademarks for its famous Contour Bottle. Due to the strong consumer association with the unique bottle design, Coca-Cola has aggressively protected its trademark shape.

FIGURE 10.14 Cadbury has recently trialled new 100 per cent sustainably sourced recyclable paper wrapping on a small selection of chocolates in New Zealand. The company is committed to phasing out plastic packaging within five years if this trial is successful. Many paper-based food wraps have a thin plastic film to protect the product; however, the Cadbury packaging paper acts as the barrier to protect food and ensure freshness.



BizFACT

The Root Glass Company of Indiana created the famous Coca-Cola contoured bottle in 1915. It was designed to help Coca-Cola stand out from other drinks at the time, and the design brief was to ensure that the bottle was recognisable even in the dark.

SNAPSHOT

Case study: The impact of packaging



We may think our eating decisions are mainly driven by rational factors such as weighing up the different attributes of products — for example, prices and content. But research shows we are strongly influenced by environmental factors that nudge us into making different decisions.

Designs of packages, brands or claims on food products also influence how we value and consume them. These influences are of course extensively used by companies to affect consumers' choices.

Companies make use of bright colours, and well-known characters from movies or other celebrities to distinguish their products from others. These visual properties act as signals that influence the way we value products and make people more likely to be attracted to certain items over others.

Some studies in children show food-directed commercials influence the amount of calories they consume, with this effect especially pronounced in overweight children.

But the fact contextual factors play a strong role in the perception of foods can also be used to help consumers in their choices.

We conducted a study in school children where we presented the same cereals in different packages. One of these was especially designed to be more appealing to children — we created cartoon characters and placed them on the package.

The same cereal not only tasted better when it was in the more appealing package, but children were also willing to make more effort to receive it (by more strongly pressing on a specially designed hand lever).

This influence of marketing on the actual taste experience has also been referred to as the marketing placebo effect. Expectations consumers may have about a known brand or a nice design can lead to actual differences in taste and consumption patterns, probably by acting on the human reward circuitry and raising the subjective pleasure of the taste experience.

Source: Bernd Weber, 'Junk food packaging hijacks the same brain processes as drug and alcohol addiction', *The Conversation*, 8 May 2017.

Labelling

Another important part of a product's package is labelling. **Labelling** is the presentation of information on a product or its package. A **label** is that part of the package that contains this information. Marketers can use labels to promote other products or to encourage proper use of products and therefore greater consumer satisfaction with products. Usually the label will provide information about ingredients, operating procedures, shelf life, package size or country of origin (see figure 10.15).

labelling the presentation of information on a product or its package

label that part of the package that contains information

FIGURE 10.15 All packaged food must have details of ingredients on the packaging. Food labels must identify the:

- name or description of the food
- batch number
- name and Australian address of the supplier
- list of ingredients
- date mark
- nutrition information panel
- country of origin
- warning and advisory statements.



BizFACT

To help reduce confusion among consumers regarding country of origin labelling, the Australian Government introduced new food labelling requirements in 2016 to make it clearer where products are produced, grown, made or packed. The labels also tell consumers what percentage of the ingredients come from Australia.

All labels must be truthful. In Australia, there are number of statutes (laws) and government regulations specifying information that *must* be included in the labelling for certain products (see the BizFact above).

These regulations are aimed at protecting the consumer from misleading or deceptive claims and the unsafe use of products. They also make it easier for consumers to compare products.

10.4.3 Explain why goods and/or services are central to both marketing and operations

The good or service is the central point on which both marketing and operations must focus. Operations managers need to determine how to make the product or provide the service and then marketing plays a key role in determining the appearance of the product and its functions, as well as communicating with the market.

The operations function is central to any business because it produces the goods and/or services; without a good or service, the business would not exist. Simply producing a product, however, doesn't necessarily result in sales. The operations department therefore relies on the marketing department to carry out market research so they can produce a product that will satisfy customers' needs. Operations also rely on marketing to inform the market, distribute products, determine a price and persuade people to purchase the products.

on Resources

Weblinks Australian Institute of Packaging
Australian Made

KEY IDEAS

- A product is a good or service that can be offered in an exchange for the purpose of satisfying a need or want.
- Most products are combinations of tangible and intangible benefits — the total product concept.
- With mass-produced products, competition is often based on the differences in the intangible benefits.
- A brand is a name, term, symbol, design or any combination of these things that identifies a specific product and distinguishes it from its competition.
- A brand name is that part of the brand that can be spoken.
- Logos can be categorised into five basic types: brandmark logos, wordmark logos, lettermark logos, combination mark logos and emblems.
- To guard against other businesses using its brand name or symbol, a business can apply to have the name registered.
- Manufacturer's or national brands are those owned by a manufacturer.
- A private or house brand is one that is owned by a retailer or wholesaler.
- Generic brands are products with no brand name at all.
- To assist sales, the packaging of a product is sometimes as important as the product itself.
- Marketers can use labels to promote other products or to encourage proper use of products and therefore greater consumer satisfaction with products.

10.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.4 Quick quiz on	10.4 Exercise	10.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 5, 7, 9, 15	2, 3, 4, 6, 10, 11, 12, 14, 16, 17, 19	8, 13, 18, 20

10.4 Exercise

Revision

1. Think of a product you have recently purchased. **Identify** the tangible and intangible benefits you gained from the product.
2. **Why** do marketing managers prefer to use the term 'total product concept' rather than simply 'product'?
3. **Explain** what is meant by imagining a product as a 'collection of satisfactions'.
4. **Why** do businesses spend so much money attempting to establish a brand name and brand symbol?
5. Create a 'T' table to **summarise** the benefits of branding for (a) consumers and (b) businesses. The 'T' table has been started for you.

Benefits of branding	
Consumers • Identify favourite products	Businesses

6. Identify which benefit of branding you consider to be the most important for the (a) consumer and (b) business. **Justify** your selection.
7. When deciding on a brand name and brand symbol, **outline** some of the considerations that a marketer must take into account.
8. **Evaluate** each of the following brand names. Indicate the strong points of each name.
   a. Uber
   b. KFC
   c. Facebook
9. **Summarise** the different types of branding strategies a business can use. Provide an example of each.
10. **Explain** why packaging is critical to the success of a product.
11. Select three differently packaged goods and **explain** why you think the manufacturers chose to package the goods in such a way.
12. **How** can packaging and labelling be used as marketing strategies?
13. Find examples of packaging awards winners. The **Australian Institute of Packaging** website is a useful starting point. **Analyse** two of the designs and, for each one, write a 150-word paragraph on how these address a marketing plan.
14. Using an example, **explain** why goods and/or services are central to both marketing and operations.

Read the case study 'The impact of packaging' and answer questions 15 to 17.

15. **Identify** a range of factors that influence our eating decisions.
16. **Explain** how companies affect consumer choices.
17. **How** does packaging influence consumer expectations about products?

Extension

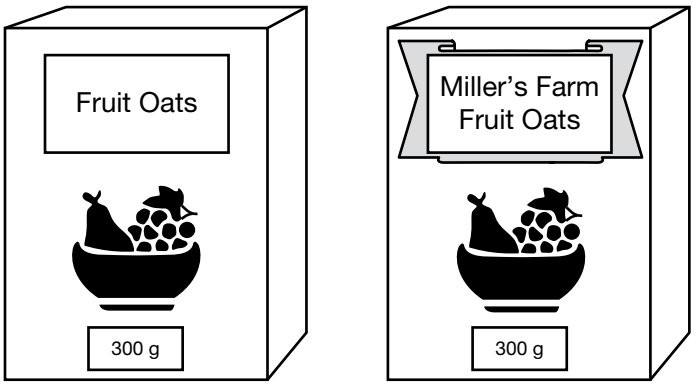
18. 'With mass-produced products, it is often on the differences in the intangible benefits that product competition is based.' **Evaluate** the accuracy of this statement. Provide examples to support your answer.
19. **Distinguish** between Product of Australia, Australian Made and Grown in Australia.
20. 'Branding, packaging and labelling combine to create a powerful set of marketing strategies.' Use examples to **evaluate** the accuracy of this statement.

10.4 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q8

Two boxes of oats are shown.



Product A Product B

Which strategy is being used by Product B that is not being used by Product A?

A. Branding
B. Labelling
C. Packaging
D. Trademarking

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q5

A landscaping business includes an image of a large purple coloured tree on its website and its vehicles.

Which of the following is the most likely reason for this?

A. Sales promotion
B. Niche marketing
C. Product branding
D. Competitive positioning

Question 3 (4 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q21c

A producer of gourmet ice-creams chooses selective distribution for her products.

Recommend ways that packaging could be used to maximise sales of the products.

Question 4 (2 marks)

Source: HSC 2008 Business Studies Exam, Section II, Q21a

A business sells a perfumed hair gel under the *KoolTop* brand. It now wants to market a cheaper non-perfumed hair gel.

Define *branding*.

Question 5 (1 mark)

Source: HSC 2006 Business Studies Exam, Section I, Q2

A soft drink company has designed a multicoloured bottle to market its new drink.

Which marketing strategy is being used by the company?

A. Place
B. Price
C. Product
D. Promotion

More exam questions are available in your learnON title.

10.5 Price

SYLLABUS LINK In this subtopic you will learn about price including pricing methods — cost, market, competition-based.

You will also learn about price and quality interaction and different pricing strategies — skimming, penetration, loss leaders, price points.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Price refers to the amount of-money a customer is prepared to offer in exchange for a product. Many businesses have difficulty selecting the 'correct' price for their products. A price set too high could mean lost sales unless superior benefits are offered. A price set too low may give customers the impression that the product is 'cheap and nasty'. Somewhere between these extremes is a correct price for a product.

In any market, businesses will attempt to gain some control over the price by differentiating their products. Once this happens, the business has more leverage over the price. For example, clothes with designer labels, such as Nike, Tommy Hilfiger, Polo Ralph Lauren and Witchery, are the result of product differentiation strategies. These labels can set higher prices for their garments than clothing sold under the Target or Kmart brand labels.

price the amount of money a customer is prepared to offer in exchange for a product

FIGURE 10.16 Woolworths has moved most of its prices to round numbers, turning their back on the age-old practice of adding .99 to a price in the belief consumers put more weight on dollar figures. Round prices will make it easier for customers to add up and compare prices. Since stores such as Kmart have conditioned customers to think that neat, whole numbers must have been marked down at some point, this everyday low-price philosophy is a psychological pricing strategy to convince shoppers they are actually paying less.



10.5.1 Pricing methods

Overall, a business's pricing decisions are influenced by a variety of internal and external factors. As a starting point, the business's marketing objectives and costs of production provide an indication of what it should charge for its products. Then, the business must consider such factors as the amount of competition in the marketplace, government regulations, the location of the product on its life cycle and the level of economic activity.

There are three main pricing methods: cost-based, market-based and competition-based. These pricing methods provide a 'basic' price for each product. Pricing strategies are then used to adjust the basic price, depending on the marketing objectives and conditions within the marketplace.

Cost-based pricing

Cost-based pricing is the simplest of the three methods. As a starting point, the business determines the total cost of producing (or purchasing) one unit of the product. The business then adds an amount to cover additional costs (overheads such as interest payments, insurance, transport) and to also provide an adequate profit margin. That amount is referred to as the **mark-up** and is usually expressed as a percentage. The total of the cost plus the mark-up is the selling price of the product. The formula is as follows:

$$\text{Cost} + \text{Cost} \times \text{Mark-up percentage} = \text{Price}$$

For example, if a manager of a clothing store buys 100 blouses at $50 each and applies an 80 per cent mark-up on cost, the price to the consumer will be $90 per item. This same percentage mark-up might be applied to all products in the store.

BizFACT

A breakeven analysis can assist a marketing manager to determine the appropriate mark-up percentage.

Cost-based pricing is a very simple and straightforward pricing policy and is used mainly by wholesalers and retailers. However, it has two major drawbacks.

1. Difficulty in accurately determining an appropriate mark-up percentage. If the percentage is too high, the product will be overpriced and possibly not sell. If the mark-up is too low, the business is losing profit they could have easily obtained.
2. The product is priced after production and associated costs are incurred without taking into account the other elements of the marketing mix or the state of the market.

Market-based pricing

Instead of using costs to determine price, businesses sometimes set prices according to the level of **supply** and **demand** — whatever the market is prepared to pay. **Market-based pricing** is a method of setting prices according to the interaction between the levels of supply and demand. When demand for a product is greater than its supply, there will be a *shortage* in the market. This will force up the price of the good. For example, if 100 prospective buyers attend an art auction but there is only one particular type of painting (product) offered for sale, the price will rise. As the price rises, buyers will progressively drop out of bidding until the final buyer is successful. Conversely, when the supply of a product is greater than its demand, a *surplus* will exist in the market. The price of the product will consequently fall. This is why bananas are cheaper, for example, during the summer months.

cost-based pricing a pricing method derived from the cost of producing or purchasing a product and then adding a mark-up

mark-up a predetermined amount (usually expressed as a percentage) that a business adds to the cost of a product to determine its basic price

supply the quantity of a product businesses are willing to offer for sale at a particular price

demand the quantity of a product consumers are willing to purchase at a particular price

market-based pricing a method of setting prices according to the interaction between the levels of supply and demand — whatever the market is prepared to pay

The prices of products, therefore, are constantly changing in relation to fluctuations in the levels of supply and demand. Market-based pricing is critically important not only as a pricing method in itself, but also as a basis for the other pricing methods. However, this method can be difficult to apply because the levels of supply and demand will constantly change. (Refer to figure 10.17.)

Competition-based pricing

Most products are available from more than one business. When making a major purchase, many consumers compare prices. Businesses, therefore, need to consider the competition when making their pricing decisions. **Competition-based pricing** is where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to the competitor's price.

Competition-based pricing is often used when there is a high degree of competition from businesses producing similar products. Once a business has established a base price, it can then decide to choose a price either:

- below that of competitors. This policy of undercutting the competition is often used as a way of breaking into an established market.
- equal to that of competitors. Following the price established by a **price leader** is an easy option for a business because it avoids having to undertake market research to find out what the consumer would actually pay. As well, it also avoids the risks of price competition/war.
- above that of competitors. This is a favoured practice by businesses who wish consumers to perceive the product as superior, which appeals to the status-conscious buyer.

FIGURE 10.17 Have you ever tried to buy tickets for an event and the price changes each time you check? Many event ticketing companies such as Ticketmaster use market-based pricing. This means that ticket prices and fees change based on demand. You may notice that ticket prices go down closer to the event date because fewer people are buying tickets. On the other hand, popular events will be priced very high. Companies use this strategy to boost revenue, especially when they know that demand for tickets will fluctuate.



10.5.2 Pricing strategies

Once the basic price has been set using the preferred pricing method(s), the business then fine-tunes this price in line with its pricing strategy. Various pricing strategies can be used, and it is common for a business to use several at once, even for the same product. The extent to which a business uses any of the following strategies depends primarily on:

- its marketing objectives
- the life cycle of the product
- the market for the product
- the degree of product differentiation
- the level of economic activity.

competition-based pricing where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to the competitor's price

price leader a major business in an industry whose pricing decisions heavily influence the pricing decisions of its competitors

Of course, as with all areas of business, the pricing strategies used by marketers will have to be modified depending upon changes within the external business environment, especially the influence of technology. For example, the growing influence of the internet and the expansion of e-commerce have weakened some business's control over prices. Consequently, marketers have been forced to modify their traditional pricing strategies. One example is the widespread use of **bundle pricing** common with the telecommunications businesses, as evidenced by the advertisements from mobile phone companies, internet providers and cable television operators offering all kinds of packages.

Price skimming

Price skimming occurs when a business charges the highest possible price for the product during the introduction stage of its life cycle. Some consumers are willing to pay a high price for a product's novelty features because of the prestige or status that ownership gives. Early purchasers (adopters) of innovative electronic equipment fall into this category. The business essentially 'skims the cream' off the market. The objective is to recover the costs of research and development as quickly as possible, before competition enters the market.

bundle pricing where customers gain a 'package' of goods and services in addition to the tangible good they purchased

price skimming when a business charges the highest possible price for the product during the introduction stage of its life cycle

BizFACT

Whenever Sony launches a new and innovative product, they use the price skimming strategy. They set the price high when a product is first launched to make as much money as they can from those customers who will pay almost any price to get the latest gadget and then they decrease the price gradually over time.

Apple is a very good example of a price-skimming brand. Historically, new Apple products launch with a premium price attached. Read the following case study which illustrates why Apple has been so successful with this strategy.

SNAPSHOT

Case study: Apple — skimming their way to the top



Marketing isn't just about promotion. A business's pricing strategy is also hugely important. This is especially true when a business is selling a 'prestige' product. Take for instance Apple, whose business model has attracted a lot of attention. While their promotional strategies and innovative products have had a significant impact on their success, their pricing strategy is also an important factor.

Apple has always focused on the high-end smartphone market, which put them in an ideal position to pursue the skimming pricing strategy. Let's focus on the iPhone. Before each new iPhone comes out, Apple has already stirred up consumers' curiosity and expectations with their marketing strategies. In most cases, when a new product is first launched, a high price would deter many consumers from purchasing the product. So why are there always queues outside Apple stores when new phones are released?

With iPhone sales gradually slowing down, Apple needed to look for other ways to increase revenue and the most obvious way to do that was to raise the price of their phones. Therefore, over the past few years, Apple has successfully made buying their latest and greatest phones more expensive.

There are a few reasons why Apple has chosen to adopt price skimming:

1. High price = higher revenue
   Development of new products at higher prices means the company is able to obtain a larger profit and get a faster return on their initial investment of new products. This extra profit enables the business to further invest in expanding and creating more innovative products.
2. Positioning
   Since Apple's target market is the high-end consumer, this market position will be supported by the higher prices. Their primary target market is not price sensitive and these higher prices signal the higher quality of their new product.
3. Suppress competition
   The new highly priced phones could prevent new competitors from entering the market.
4. Branding
   Apple has developed a very strong brand reputation and has a huge number of customers who perceive the brand as attractive, which enables them to support these higher prices.

This price skimming strategy has been so successful that, despite a zero per cent change in iPhone sales over the past few years, Apple has ended up with a significant increase in revenue in its smartphone division.

In fact, despite global smartphone sales dropping 20.4 per cent in the second quarter of 2020, Apple was the only company that remained relatively stable this quarter, while other manufacturers saw double digit declines year after year. The higher price tag has been successful enough to significantly increase the iPhone's average selling price and therefore generate the majority of Apple's recent revenue growth. This price skimming strategy is pretty remarkable considering that it will help keep Apple's revenue growing, even if iPhone sales don't increase in terms of numbers.

Price penetration

At the opposite extreme to price skimming is price penetration. **Price penetration** occurs when a business charges the lowest price possible for a product. The strategy aims to quickly achieve a large market share for a product — sometimes called 'mass-market pricing'. The objective is to sell a large number of products during the early stages of the life cycle and thus discourage competitors from entering the market or from taking market share from existing businesses. The main disadvantage of this strategy is that it is more difficult to raise prices significantly than it is to lower them. Consequently, a business may be locked into a low sales revenue until it substantially modifies the product at a later stage.

price penetration when a business charges the lowest price possible for a product or service so as to achieve a large market share

loss leader a product sold at or below cost price

Loss leader

A **loss leader** is a product sold at or below cost price. For a special promotion, many businesses, especially retail stores, deliberately sell a product at a loss to attract customers to the shop. Although the business makes a loss on this product, it hopes that the extra customers will buy other products as well. The psychology behind this strategy is that once the consumers are in the store, they will usually buy other products and spend on more than what attracted them into the store to begin with. The business can recover the loss on the low-price item from the sale of the other items or services that the consumer buys.

FIGURE 10.18 Supermarkets frequently use the loss leader pricing strategy as evidenced by the promotion of weekly specials. Often these heavily discounted items are located next to higher priced, more appealing products or at the end of the aisles with the lower prices clearly displayed.



This successful pricing strategy is often used when the business:

- is overstocked or a product is slow to sell
- wants to increase the traffic flow in the expectation of gaining new customers
- wants to build a reputation of having low prices.

However, the main danger of this practice is that if it is done incorrectly the business can actually lose money.

Price points

Price points (or **price lining**) is selling products only at certain predetermined prices. This pricing strategy is used mainly by retailers, especially clothing stores and boutiques. The business chooses a limited number of key prices or price points for selected product lines. For example, a jeweller may offer a line of watches priced at $55, $75 and $95 regardless of how much they cost at wholesale. In practice, this means the store would not apply a fixed mark-up to the products.

Using this pricing strategy makes it easier for the customer to find the type of product they need. It also makes it easier for the business to encourage the customer to 'trade up' to a more expensive model.

10.5.3 Price and quality interaction

You have probably heard the expression 'You get what you pay for'. To marketing managers, this saying describes the price–quality relationship. Normally, products of superior quality are sold at higher prices. This is usually due to the higher manufacturing cost involved in producing them.

This perceived price–quality relationship helps determine the image customers have of products or brands. Therefore, if a business charges a low price for a product, customers may perceive the product as 'cheap'. Charge a high price and the product develops an aura of quality and status (see figure 10.19). This pricing strategy is referred to as **prestige** or **premium pricing** and is designed to encourage status-conscious consumers to buy the product. Premium or prestige pricing is based on the tendency for consumers to assume that expensive products are of superior quality and distinction. If a business that uses premium pricing lowered their prices dramatically, it would damage their reputation because it is inconsistent with the perceived images of such products.

BizFACT

Premium pricing is common for service industries, where the consumer cannot see the product in advance and relies on price to indicate its quality.

This price–quality relationship does not apply to all products. Usually, high-priced and infrequently purchased items such as cars, homes and furniture display a stronger price–quality relationship than frequently purchased products such as grocery items. As well, consumers may believe that high prices reflect either expensive packaging or market exploitation. This may lead to a reduction in sales because the consumer perceives there to be little actual difference between the quality of a low- and high-priced item. Sometimes, a premium price is set artificially high to imply a prestigious or quality image when, in reality, the quality may not be much superior to cheaper alternatives.

price points (or **price lining**) selling products only at certain predetermined prices

prestige or **premium pricing** a pricing strategy where a high price is charged to give the product an aura of quality and status

FIGURE 10.19 Louis Vuitton is an example of a retailer with a prestige pricing strategy. Products are priced at a high level in order to denote exclusivity, high quality and luxury. The French fashion house implements premium pricing on all its products; it doesn't conduct sales, nor does it have any outlet stores.



KEY IDEAS

- Price refers to the amount of money a customer is prepared to offer in exchange for a product.
- There are three main pricing methods:
  - Cost-based (mark-up) pricing is a pricing method derived from the cost of producing or purchasing a product and then adding a mark-up.
  - Market-based pricing is a method of setting prices according to the interaction between the levels of supply and demand.
  - Competition-based pricing is where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to competitors' prices. A business can select a price that is below, equal to or above those of competitors.
- Once the basic price has been set using the preferred pricing method, the business then fine-tunes this price in line with its pricing strategy.
- The four main pricing strategies include:
  - price skimming, which occurs when a business charges the highest possible price for the product during the introduction stage of its life cycle
  - price penetration, which occurs when a business charges the lowest price possible for a product or service to achieve a large market share
  - loss leader, which is a product sold at or below cost price. Although the business makes a loss on this product, it hopes that the extra customers will buy other products as well.
  - price points (or price lining), which is selling products only at certain predetermined prices.
- Normally, products of superior quality are sold at higher prices.
- Prestige or premium pricing is a pricing strategy where a high price is charged to give the product an aura of quality and status.

10.5 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.5 Quick quiz on | **10.5 Exercise** | **10.5 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 6, 8, 11, 12, 14, 19, 25	3, 5, 7, 9, 10, 13, 15, 16, 17, 18, 20, 24	21, 22, 23

10.5 Exercise

Revision

1. Complete the following sentences by **recalling** the correct term from the list below.

exchange	correct	high	low
money	customers	selecting	sales

Price refers to the amount of ———— a customer is prepared to offer in ———— for a product. Many businesses have difficulty ———— the 'correct' price for their products. A price set too ———— could mean low ———— unless superior benefits are offered. A price set too ———— may give ———— the impression that the product is 'cheap and nasty'. Somewhere between these extremes is a ———— price for a product.

2. **Identify** the three main pricing methods.
3. **Why** are retailers likely to adopt the cost-based method to pricing?
4. **State** the formula used to calculate the price using the cost-based method.
5. As the manager of a furniture store, you have just received a shipment of new media units. The units cost you $385 each and your usual mark-up is 75 per cent.
   a. **Calculate** the final selling price.
   b. **Explain** what you would do to the price if your business has exclusive distribution of this highly fashionable product.
6. **Outline** the two major drawbacks of cost-based pricing.
7. **How** is market-based pricing determined?
8. **Recall** the three alternatives that are available to businesses that adopt the competition-based method of pricing.
9. **Explain** why a business would use competition-based pricing.
10. **Why** do some businesses use bundle pricing?
11. **State** what motives might lead a business to adopt a price skimming strategy.
12. **Identify** a possible problem with using price skimming.
13. **Deduce** under what conditions a phone manufacturer would adopt (a) a price skimming approach and (b) a price penetration approach for a new product.
14. **Recall** the main disadvantage of price penetration.
15. **Account** for why a business would use the loss leader pricing strategy.
16. **How** might buyers' perceptions of price influence pricing decisions?
17. **Discuss** whether you agree with the statement 'You get what you pay for'. Provide examples to **justify** your answer.

18. Imagine you are a marketing consultant. A client has asked you to make recommendations regarding the price of five, as yet, unbranded new products. You are trying to decide whether to recommend price skimming, price penetration, loss leader or price points pricing strategies. Complete the following table and **justify** your recommendation.

Unbranded new product	Recommended pricing strategy	Justification for this strategy
1. Imported leather lounges		
2. A range of costume jewellery		
3. Bottled water		
4. Mobile phone		
5. T-shirts		

Read the 'Apple—skimming their way to the top' case study and answer questions 19 to 21.

19. **Outline** Apple's positioning in the market.
20. **Why** are Apple able to charge higher prices?
21. **Assess** the effectiveness of this price skimming strategy for Apple.

Extension

22. Define the term 'non-price competition'. Compare the characteristics of price and non-price competition. **Predict** under what conditions a business would be most likely to use non-price competition.
23. Explain why some customers are prepared to pay a high price for a product, although other customers would not buy the product even if the price was low. **Extrapolate** what this tells you about the relationship between price and customer tastes and preferences.
24. **Why** do many department stores use a mark-up of about 50 per cent, when some discount variety stores operate on a mark-up of 20 per cent?
25. Compare the prices of five identically branded electronic products in three competing stores.
    a. **State** whether the prices are the same or different.
    b. Account for the similarities and/or difference.

10.5 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q6

A biscuit manufacturer reduces the price of its biscuits to below cost in order to attract more customers.

Which of the following identifies this approach?

A. Skimming
B. Loss leader
C. Price points
D. Production leader

Question 2 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q7

When pricing a potential job, a plumber considers how long the job will take and how difficult it will be.

Which pricing method is being used?

A. Cost-based
B. Market-based
C. Customer-based
D. Competition-based

Question 3 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q9

What is the main reason for a business using penetration pricing?

A. To maximise profit per unit
B. To gain short-term market share
C. To develop a reputation for quality
D. To take advantage of a lack of competition

Question 4 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q9

What is the most likely reason that a business would use price skimming?

A. To encourage export sales
B. To achieve market share quickly
C. To gain high profits when demand is strong
D. To reverse the decline stage of the product life cycle

Question 5 (4 marks)

Source: HSC 2012 Business Studies Exam, Section I, Q17

A fast food outlet advertises a large soft drink for only 20 cents, knowing that customers will also buy additional items from the menu once they are in the store.

What pricing strategy is this?

A. Loss leader
B. Penetration
C. Price points
D. Skimming

More exam questions are available in your learnON title.

10.6 Promotion

SYLLABUS LINK In this subtopic you will learn about:

- the elements of the promotion mix — advertising, personal selling and relationship marketing, sales promotions, publicity and public relations
- the communication process — opinion leaders, word of mouth.

You will also learn to assess why a mix of promotional strategies is important in the marketing of goods and services.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

To sell more of its products, a business has to change customers' behaviour through information or persuasion. This is achieved through promotion. **Promotion** describes the methods used by a business to inform, persuade and remind a target market about its products.

Promotion attempts to:

- attract new customers by heightening awareness of a particular product
- increase brand loyalty by reinforcing the image of the product
- encourage existing customers to purchase more of the product
- provide information so customers can make informed decisions
- encourage new and existing customers to purchase new products.

promotion the methods used by a business to inform, persuade and remind a target market about its products

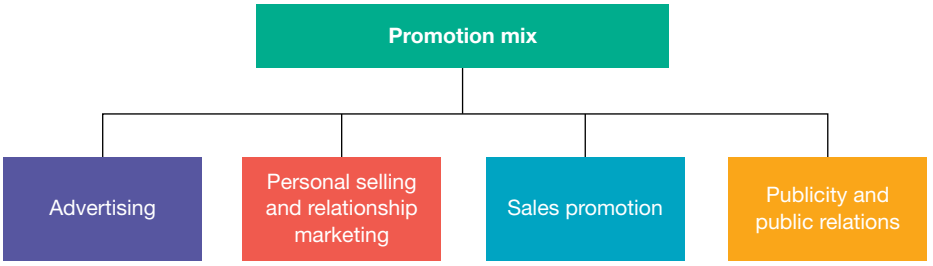
promotion mix the various promotion methods a business uses in its promotional campaign. Methods include:

- advertising
- personal selling and relationship marketing
- sales promotions
- publicity and public relations.

10.6.1 Elements of the promotion mix

Many people confuse promotion with advertising because of its visibility and frequency. However, advertising is just one of the four elements of the promotion mix. A **promotion mix** is the various promotion methods a business uses in its promotional campaign (see figure 10.20).

FIGURE 10.20 Depending on the type of product and target market involved, two or more of these elements are combined to form the promotion mix.



Advertising

Which current advertisement has most impressed you? What product is it advertising: soft drink, food, clothes, a car or something else? Why did it impress you? You can probably answer these questions without too much thought. This is because you have been influenced by advertising. Everywhere you look businesses are trying to sell consumers their products.

advertising media refers to the many forms of communication used to reach an audience

As previously explained, advertising is a paid, non-personal message communicated through a mass medium. Because of the myriads of products available, advertising is an essential tool for successful marketing. An effective advertising campaign can result in increased sales and profit for a business. The form and presentation of advertisements have changed over time (see figure 10.21), but the purpose of advertising — to inform, persuade and remind — has remained constant.

The main advantage of advertising is that it provides businesses with the flexibility to reach an extremely large audience or to focus on a small, distinct target market segment.

FIGURE 10.21 Video marketing is one of the fastest growing forms of advertising, with about 87 per cent of businesses now using video as a part of their marketing strategies. Ryan ToysReview is one of the most popular YouTube channels, with billions of views and more than 23 million subscribers. The videos feature an excitable eight-year-old named Ryan unpackaging toys and playing with them and going on kid-friendly adventures. The channel, run by Ryan's parents, Shion and Loann Kaji, was YouTube's top earner in 2019, according to Forbes, bringing in US$26 million. Nearly all of his money comes from pre-roll advertising on his channels.



Advertising media

Advertising may take many forms, from buying time on national television, to inexpensive leaflets or posters, to internet banner advertisements. All businesses need to develop the most cost-effective means to advertise their products. **Advertising media** is a term for the many forms of electronic and print communication used to reach an audience.

There are many different types of advertising media, such as:

- *Print publications* — advertisements in newspapers and magazines
- *Television advertising* — television has an extensive reach and caters to a large market in a large area
- *Radio advertising* — where advertisements are broadcasted from different stations

- *Outdoor advertising* — where messages are printed on billboards, posters, electric displays, neon signs, sky writing, painted signs or different forms of public transport
- *Direct mail* — where catalogues, brochures or leaflets are mailed to individual households
- *Window display* — usually undertaken by retailers who display their products in shop windows in order to attract customers
- *Internet advertising* — the use of the internet to deliver advertising messages
- *Telemarketing* — the use of the telephone to personally contact a customer.

Which type of advertising media a business selects depends on a number of variables including the:

- type of product and its positioning
- size of the target market and its characteristics
- business's marketing budget
- cost of the advertising medium
- product's position on the product life cycle.

Sometimes a business will undertake an extensive advertising campaign that involves a number of advertising media in order to create a saturated coverage of a wide target market. This is the advertising strategy used, for example, when a new movie is released. There will be celebrity publicity events, electronic and print advertisements, billboards and e-marketing using pop-up banners and social media advertising.

FIGURE 10.22 While Australian online advertising market growth slowed in 2020, it still achieved 5.6 per cent year-on-year growth according to the IAB *Australia Online Advertising Expenditure Report* (OAER) compiled by PwC. All online advertising categories showed growth through the year, while video advertising saw the largest increase, with 19.9 per cent growth year-on-year.



SNAPSHOT

Case study: Huge decline in advertising spending

The COVID-19 pandemic has led to a dramatic drop in advertising spending. According to the Standard Media Index (SMI), media agency advertising spending dropped 35 per cent from April 2019 to April 2020. This drop equates to $331.13m of spending and is almost twice that seen during the depths of the global financial crisis (GFC). The only industries in which advertising spending increased were domestic banks and governments, which saw a 16 and 20 per cent increase respectively.

Some industries, such as travel, stopped most of their spending on advertising due to the COVID restrictions. This industry alone saw a decline of over 80 per cent and cut spending on advertising by $20.2 million. The cinema / theme park product category reported the third largest decline of 86 per cent, which represents a cut in spending of $16.3 million. The closure of cinemas meant there was no ad spend into cinemas and that in turn meant that those businesses themselves stopped advertising.

SMI AU: April 2020 Ad Spend Trends — COVID-19 Impact	
Media	**% Change from April 2019**
Television	–33%
Digital	–27%
Outdoor	–61%
Radio	–45%
Press	–35%
Magazines	–52%
Total (ex abnormals)	**–35%**

While some industries may have cut their ad spending altogether, many other industries who have faced budget cuts have moved towards cheaper and more flexible channels. For instance, digital display ads, social media and online video are channels that have started to increase in the short-term. Out-of-home advertising, such as billboards, experienced a larger decline due to the lower levels of exposure since more people are staying at home.

Since the GFC evolved over a few months, the decline in ad spend brought on by the pandemic has been more devastating to the media industry. This is because it occurred within weeks, which meant the industry had no time to prepare for such a dramatic drop in revenue.

As of September 2020, the latest SMI data showed that advertising spending was slowly recovering and that the huge drop in spending is starting to shrink. August numbers were already showing stronger spending than previous months.

FIGURE 10.23 Nielsen Ad Intel calculated the 20 biggest spending advertisers of 2019. Retailer Harvey Norman topped the list, spending $165.4 million. Harvey Norman uses a variety of advertising media in order to create a saturated coverage. For example, they advertise on television, radio, newspapers, magazines, billboards, social media and weekly catalogues.



Personal selling

Personal selling involves the activities of a sales consultant directed to a customer in an attempt to make a sale; it involves the human aspect of promotion. For some businesses — such as those offering expensive, complex or highly individual products — personal selling is *the* main promotional strategy. These products in particular require the personal contact of a sales representative to familiarise the customer with the product.

Although personal selling is an expensive promotional method, businesses are willing to spend the money on it because it offers three unique advantages. They are:

- The message can be modified to suit the individual customer's circumstances.
- The individualised assistance to a customer can create a long-term relationship resulting in repeat sales.
- The sales consultant can provide after-sales customer service in relation to product features, installation, warranties and servicing.

By listening to the customer's needs and then offering informed recommendations, customer satisfaction is increased, resulting in repeat business and building a good reputation for the business.

personal selling the activities of a sales representative directed to a customer in an attempt to make a sale

The success of the marketing plan often depends on the competency of the business's sales force, without which sales and revenue would soon decrease.

SNAPSHOT

Case study: MAPPEN's ad-free growth

MAPPEN is an online curriculum and professional learning application targeted to Australian primary schools, that provides teachers with lesson plans and built-in professional learning. The inspiration behind the business was to design an innovative solution that would solve one of the biggest systemic problems facing all school leaders and teachers — how to find the time to plan and write fully resourced lessons that meet all mandated standards and students' needs.

Growth has been rapid and remarkable; it took only two years for MAPPEN to find its way to over 300 schools in the first two years and turn over more than $1 million. What is surprising, however, is that this growth occurred without any spending on ads. In fact, the most the company ever spent on advertising was $1000 on Facebook. From the outset, the owners realised that what worked best for them was a combination of word-of-mouth and personal selling.

While there are many benefits of paid ads, the founders believe there are more effective ways of generating customers. While paid advertising will inform a large audience about a particular product, the team realised that face-to-face was the best approach to engage potential customers. Personal selling is more labour-intensive, but the team found that developing relationships was a more effective way of securing growth. Traditional advertising attempts to persuade customers that they need a particular product; however, the founders felt that they really needed to explain the benefits first. The conversion rate through personal selling was much higher than traditional advertising.

The first few schools they went to were schools they knew and were familiar with. Their clientele then gradually grew through word-of-mouth and teachers talking to other teachers. Many startups like MAPPEN are finding that sometimes the least expensive advertising mediums can sometimes generate the best returns.

BizFACT

In 2019 Coca-Cola Amatil spent $10 million hiring 97 extra sales representatives to target corner store and café owners to encourage them to buy their products and advise on how best to promote them. This strategy was successful in halting the decline in soft-drink sales due to health-conscious consumers turning away from their most popular products.

Relationship marketing

Customers want more individualised treatment. In response, businesses are looking for ways to develop long-term, cost-effective and strong relationships with individual customers, a process known as **relationship marketing**. The ultimate aim is to create customer loyalty by meeting the needs of customers on an individual basis, thereby creating reasons to keep customers coming back.

A highly successful relationship marketing strategy is loyalty programs. A **loyalty program** is a rewards-based program offered by a business to customers who frequently make purchases. This was introduced during the early 1990s with the flybuys loyalty reward program operated by the Coles Group. In 2007 the Woolworths Everyday Rewards scheme was introduced. These schemes offer rewards to those loyal customers who spend specified amounts or make repeat purchases. Relationship marketing can provide a business with a competitive advantage.

relationship marketing the development of long-term and cost-effective relationships with individual customers

loyalty program a rewards-based program offered by a business to customers who frequently make purchases

BizFACT

A recent marketing industry survey found that four in five shoppers tend to buy more from businesses whose loyalty cards they hold, and 55 per cent say that when choosing between two similar companies they'll usually pick one with a loyalty program.

FIGURE 10.24 Coles flybuys is one of the best-known loyalty programs in Australia. Members get points for each purchase when shopping at Coles, and can earn even more points by shopping at partner stores too (such as Kmart and Target). Plus, there are a variety of other ways to earn points, including banking, paying bills, travel and joining a gym. Once members reach 2000 points, they receive $10 off. They can either use the cash reward to reduce their grocery bill or they can purchase products with the points.



Sales promotion

A business may decide to offer a direct inducement to customers in an attempt to sell more of its product. This type of promotion is referred to as **sales promotion** and aims to:

- entice new customers
- encourage trial purchase of a new product
- increase sales to existing customers and repeat purchases.

FIGURE 10.25 Both Coles and Woolworths have launched a variety of successful sales promotions centred around limited-edition collectables. For example, Woolworth's Lion King Ooshies led to an increase in sales of over 7 per cent during the campaign. The success of these promotions relies heavily on an inherent human need to want to complete things. Each collectable promotion launched has driven strong sales and revenue growth for both supermarkets.



Sales promotion techniques are used primarily to increase the effectiveness of other promotion activities, especially advertising. Examples of special promotions include:

- *limited time offers.* Whether it's a coupon, discount code or voucher, these incentives offer discounts of a stated amount on particular items at the time of purchase. They are effective as they drive a sense of urgency and trigger consumers' fear-of-missing-out (FOMO).
- *free gifts*. Fairly self-explanatory, these are gifts the business offers customers in return for purchasing their product.
- *refunds*. Part of the purchase price is given back to those customers who send in a voucher with a specific proof of purchase. In recent years, refunds have become widely used on power tools and kitchen appliances.
- *samples*. A sample is a free item or container of a product. For example, when you visit a supermarket, you will often find a sales representative encouraging you to taste a product such as cheese, fruit, biscuits or cake.
- *point-of-purchase displays*. Special signs, displays and racks are supplied and installed by the manufacturer in retail outlets. They are usually located at the end of aisles in supermarkets to gain consumer attention and make more efficient use of floor space.

sales promotion the use of activities or materials as direct inducements to customers

- *contests and giveaways*. There are different forms of contests which can be run to gather more customer information or to motivate customers to try the product. Contests can be as simple as winning a gift or an online contest for which users have to enter their information.
- *deals.* Buy-one-get-one-free deals are among the most well-used promotional methods. These deals are enticing as people always like to get more for less and have a hard time saying no to the word 'free'. Additionally, businesses can use this promotion to unload overstocked inventory in a way that helps them still have a profit margin.

BizFACT

It is the role of public relations personnel to design, implement and manage the publicity events of the business.

Publicity and public relations

What's worse than being talked about? Not being talked about! Businesses rely on being in the public eye. Most businesses use publicity and public relations as a means of increasing sales and, therefore, profits. **Publicity** is any free news story about a business's products. It differs from advertising in that it is free and its timing is not controlled by the business. The main aims of publicity are to:

- enhance the image of the product
- raise awareness of a product
- highlight the business's favourable features
- help reduce any negative image that may have been created.

Public relations (PR) are those activities aimed at creating and maintaining favourable relations between a business and its customers. PR exposes a business or idea to an audience by using often unpaid third parties as outlets. This can be done by working with the media, by making speeches on special occasions or by some attention-seeking gesture such as a donation or a give-away sale that is reported by others. This means that PR is often more effective than paid advertising. Sometimes PR can even work out to be cheaper.

There are four main ways in which public relations activities can assist a business in achieving its objective of increased sales.

1. *Promoting a positive image:* reinforcing the favourable attitudes and perceptions consumers have regarding the business's reputation
2. *Effective communication of messages*: using advertising, sales promotions, publicity and personal selling to convey information about the business and its products
3. *Issues monitoring*: protecting sales by providing an early warning of public trends that could affect the business's sales. Remedial action can be taken before much harm is done to sales.
4. *Crisis management*: protecting a business's reputation as a result of negative or unfavourable rumours and adverse publicity, which, if left unchecked, might result in a loss of sales

publicity any free news story about a business's products

public relations (PR) those activities aimed at creating and maintaining favourable relations between a business and its customers

SNAPSHOT

Case study: True or false — all publicity is good publicity?

While publicity is all about trying to create a favourable image, the downside is that you can't control what is said about your business or your product or service. Therefore, businesses need to ensure that what they publicise can withstand public scrutiny.

The advent of social media has delivered a new army of critics and commentators, all of whom have the ability to disseminate their opinion about businesses. Is the saying 'there's no such thing as bad publicity' a myth? The following are two examples of companies that have attracted ongoing negative media coverage and publicity.

In January 2017 when President Trump announced his travel ban, Uber continued to operate its service at the airport. This was met with backlash from angry customers who accused the company of profiting off the taxi strike and putting its support behind Trump's immigration ban. The #DeleteUber hashtag emerged on Twitter and took social media by storm. As a result, hundreds of thousands of customers deleted the Uber app and deactivated their accounts within days of the campaign's launch on social media. The viral movement received significant media coverage and generated a lot of negative publicity for the company. This in turn damaged Uber's reputation and led to distrust in the company.



In 2019 Snapchat lost $800 million off its share price after running an ad which asked users to reveal whether they'd prefer to slap Rihanna or punch Chris Brown. The ad was developed to promote the company's latest game 'Would You Rather'. Users widely criticised the ad for making light of domestic violence and quickly took to social media to air their concerns.

FIGURE 10.26 Elon Musk, the CEO of Tesla, does not use traditional advertising methods. Instead, he provides the sort of publicity money can't buy. He is extremely proficient at using PR and publicity to influence people's opinions and attitudes about the Tesla brand. For example, in 2018 he put a Tesla into space aboard one of the SpaceX spacecraft. As far as we know, that car is still out there exploring our solar system.



10.6.2 The communication process

Marketing managers must be able to communicate clearly, efficiently and succinctly to their target markets. If the communication process becomes distorted or inefficient, the message becomes distorted. The resulting miscommunication may mean lost sales. Without effective communication, promotion is wasted.

Marketing managers can use a variety of channels to communicate a message. A **channel** is any method used for carrying a message. Two of the most common channels used for promotional communication include print and electronic media advertising. Any interference or distraction that affects any or all stages in the promotional communication process is referred to as **noise**. Examples of noise include faulty printing, competing messages, inappropriate language or images, jargon, misinterpretations or — perhaps one of the most common — people having conversations and fetching refreshments during commercial breaks.

Often customers may be more willing to purchase a product if the message is communicated via a respected and trusted channel, such as an opinion leader, or by word of mouth.

Opinion leaders

An **opinion leader** is a person who influences others. Their opinions are respected and they are often sought out for advice.

Marketing managers use opinion leaders as information outlets for new products or to endorse an existing one. Actors, athletes, musicians and models are regarded by some groups as opinion leaders and many businesses use celebrity endorsement as part of their marketing strategies.

Celebrity endorsement is a powerful marketing tool when the target audience align themselves with the ambassador chosen. Having that endorsement can open up a huge following. This is because ambassadors usually have a large social media following — a referral from them can be powerful and the company can gain instant followers and engagement. If businesses choose to use this strategy, however, they need to remember that their brand and image will be aligned to the ambassador; therefore, if that person's reputation becomes tarnished for whatever reason, this will affect the business's reputation.

FIGURE 10.27 Colin Kaepernick signed an endorsement deal worth millions of dollars with Nike in 2018 to be the face of their 'Just Do It' marketing campaign.



In 2018 Nike signed an endorsement deal with former NFL player Colin Kaepernick for millions of dollars (see figure 10.27). Kaepernik is a former San Francisco 49ers quarterback who last played in 2016. During that season he sparked controversy when he began protesting during the national anthem and refused to 'stand up to show pride in a flag for a country that oppresses black people and people of colour'. More NFL players then joined Kaepernick in protesting police brutality and social inequality.

Ever since Kaepernick's endorsement, Nike's value has skyrocketed. The company's stock reportedly increased over 18 per cent since the deal, adding a huge $26.2 billion to its market value. When Nike made the announcement of the signing, the February online release of a Kaepernick 'Icon' jersey, priced at $150, sold out in a matter of hours. Nike also sold 60 per cent more merchandise since releasing the Kaepernick ad.

channel any method used for carrying a message

noise any interference or distraction that affects any or all stages in the communication process

opinion leader a person who influences others

Word of mouth

Consumers tend to trust word-of-mouth communication more than business-sponsored commercials, especially if the message is being communicated by a friend or opinion leader. This is because the receiver places more trust in someone they know as opposed to a business advertising its products. When people influence each other during conversations, it is called **word-of-mouth communication**.

Businesses are increasingly using social media platforms such as Facebook and Twitter to engage in a form of word-of-mouth communication. Friends' recommendations can be a powerful influence, especially when there are many competing products from which to choose.

word-of-mouth communication
when people influence each other during conversations

SNAPSHOT

Case study: Social influencers

Many companies are aware that word-of-mouth is one of the most valuable forms of marketing — studies have shown that it influences 20 to 50 per cent of all purchasing decisions — so it's no surprise that in the new world of digital relationships, many companies have been teaming up with social media influencers across multiple platforms to promote their goods.



A social media influencer is a user of social media who has established credibility in a specific field and can thus influence their audience. Lots of brands, particularly in the fashion and lifestyle fields, have ditched sponsorship deals with big-name celebrities in favour of regular people with powerfully engaged social media followers.

Research from Twitter has shown that 49 per cent of consumers seek advice regarding purchases from social media influencers and 20 per cent of the people surveyed stated that a tweet from an influencer encouraged them to share their own recommendation. What is even more significant is that almost 40 per cent of Twitter users said they had made a purchase based on an influencer's endorsement.

Many companies are spending millions of dollars each year on influencer marketing. On top of sending free products, some companies pay influencers per post so that they can try their products and then post about them. For many brands, this does not cost as much as celebrity endorsement.

Instagram is clearly the place to be for influencer marketing. Instagram usage has grown tenfold over the last five years. It exceeded 1 billion daily users in 2018 and is rapidly on its way to a second billion. But who are the greatest Instagram influencers in 2020?

1. Cristiano Ronaldo
2. Selena Gomez
3. Kylie Jenner
4. Leo Messi
5. Kendall Jenner

10.6.3 Assess why a mix of promotional strategies is important in the marketing of goods and services

Since each element of the promotion mix has different benefits, it's important for businesses to use a mix of promotional strategies in order to cater to the needs of everyone in their target market. Businesses should not simply aim to satisfy one type of buyer; the aim of promotion is to attract as many potential customers as possible. Since different elements of the promotion mix will appeal to different types of customers, businesses need to use a combination.

Also, the different elements of the promotion mix may each play a part in influencing the same customer in different ways and assist them with their decision to purchase a product. For example, suppose you are interested in buying a mobile phone. Because of your interest, you may start paying attention to advertisements on the television or in magazines. You may search the internet to find out more about different phones, their features and prices. You may also contact sales people from different stores or post on Facebook asking your friends their opinion. Based on all this information, you may then decide to purchase a specific brand.

Which aspect of the promotional mix led you to decide on that particular brand? While some aspects may have been more influential than others, all the elements played a role in making your decision. Therefore, to get a better response from a target market, businesses need to adopt as many different components of the promotion mix as possible. These components should be coordinated and complement each other to help achieve the marketing objectives.

KEY IDEAS

- Promotion describes the methods used by a business to inform, persuade and remind a target market about its products.
- Promotion mix is the various promotion methods — advertising, personal selling and relationship marketing, sales promotions, and publicity and public relations — a business uses in its promotional campaign.
- Advertising is a paid, non-personal message communicated through a mass medium. The purpose of advertising is to inform, persuade and remind.
- Personal selling involves the activities of a sales representative directed to a customer in an attempt to make a sale.
- Relationship marketing is the development of long-term and cost-effective relationships with individual customers.
- Sales promotion is the use of activities or materials as direct inducements to customers.
- Publicity is any free news story about a business's products.
- Public relations (PR) are those activities aimed at creating and maintaining favourable relations between a business and its customers.
- Marketing managers can use a variety of channels to deliver a message including print and electronic media advertising.
- Often customers may be more willing to purchase a product if the message comes via a respected and trusted channel, such as an opinion leader, or by word of mouth.
- An opinion leader is a person who influences others and whose opinions are respected.
- Word-of-mouth communication occurs when people influence each other during conversations.
- It's important for businesses to use a mix of the promotional strategies in order to meet the different needs of their target market.

10.6 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.6 Quick quiz on	10.6 Exercise	10.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 13, 17, 19, 25, 27, 30, 33	6, 7, 9, 10, 11, 14, 15, 16, 18, 20, 21, 22, 24, 26, 28, 31, 34	8, 12, 23, 29, 32, 35, 36, 37

10.6 Exercise

Revision

1. **Define** the term 'promotion'.
2. **Recall** what promotion attempts to achieve.
3. **Identify** the four elements of the promotion mix.
4. **Recall** the main advantage of advertising.
5. **Identify** the five main types of advertising media.
6. Select which advertising media you consider to be the most effective if a business wants to communicate with (a) a mass market and (b) a niche market. **Justify** your selection.
7. **Why** is it important to identify the target market when designing an advertising program?
8. Find a recent Nerada Tea commercial online. **Assess** the advertisement in terms of communicating with its target market.
9. **Propose** which form of advertising media you would choose for the following products. **Justify** your choices.
   a. Nike sports shoes
   b. School textbooks
   c. A hairdressing salon
   d. Toys for children
   e. MacBook
10. **Why** do some marketers prefer to use personal selling as a promotional strategy?
11. **How** can personal selling be more persuasive than advertising?
12. In small groups, use the brainstorm technique to:
    a. account for the recent popularity with consumers of loyalty reward programs.
    b. **determine** the benefits to a business of this type of relationship marketing.
13. **State** the aims of sales promotion.
14. In your opinion, select the two most effective sales promotion techniques for sales promotion. **Justify** your answer.
15. **Distinguish** between publicity and public relations.
16. 'Advertising is what you pay for and publicity is what you pray for.' **Explain** what this statement means.
17. **Summarise** the four main ways in which public relations can assist a business to increase its sales.
18. 'Public relations should be viewed as a two-way communication process.' **Explain** the meaning of this statement.
19. In small groups, **identify** the different public relations activities your school uses to communicate with parents. Choose a spokesperson to share the group's answers with the rest of the class. The first items on your list can be newsletters and formal assemblies.
20. **Explain** why efficient communication is important to marketing managers.
21. **Account** for the use of opinion leaders in the promotion of a product. Provide three examples from current promotional campaigns.
22. **Propose** what you think are the strengths and weaknesses of the following promotion strategies. Share your answer with the rest of the class.
    a. A manufacturer of a new type of disposable razor gives out thousands of free razors at a football grand final.
    b. A lifestyle magazine runs its own lottery-style promotion for five weeks in which first prize is $20 000 worth of furniture.
    c. To boost sales, a computer manufacturer relies on word-of-mouth communication.

23. Using an example, **assess** why a mix of promotional strategies is important in the marketing of goods and services.

Read the 'Huge decline in advertising spending' case study and answer questions 24 to 26.

24. **How** has the pandemic affected spending on advertising?
25. **Identify** those industries that have experienced the largest decline in ad spending.
26. **Explain** how the pandemic has led to changes in the type of media used to advertise.

Read the 'MAPPEN's ad-free growth' case study and answer questions 27 to 29.

27. **Outline** the business opportunity that inspired MAPPEN.
28. **Discuss** the two main promotional methods used by MAPPEN.
29. **Assess** the use of paid ads for startup businesses.

Read the 'True or false— all publicity is good publicity?' case study and answer questions 30 to 32.

30. **State** whether you agree with the saying 'all publicity is good publicity'. Justify your answer.
31. **Discuss** the use of publicity as a marketing strategy
32. **Assess** the impact of the negative publicity on Uber and Snapchat.

Read the 'Social influencers' case study and answer questions 33 and 34.

33. **Define** a social media influencer.
34. **Why** are companies using social media influencers to promote their business or products?

Extension

35. Recently, you were elected to serve as a promotional organiser for a soccer tournament. The tournament will match several well-known celebrity teams from New South Wales against the best local players. Tickets will sell for $30 per person and your goal is to attract a large number of supporters. All proceeds will be given to a local charity. As you **create** a promotional plan, **determine** what segmentation variables will be most important. Propose the buying motives you will use to appeal to your target market.
36. In small groups, **create** a media release to advertise the opening of a new clothes store in your local area. Include the following details:
    - name, telephone number and address of the store
    - date of opening
    - hours of business
    - range of stock
    - any opening special
    - store logo.
37. Referring to a business you are familiar with, **analyse** and **evaluate** the promotion methods used for one of its products.

10.6 Exam questions

Question 1 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q17

A small business has developed a new piece of gym equipment that it wants to sell to gyms throughout Sydney.

What would be the most appropriate marketing strategy for this?

A. Advertising on billboards on main roads
B. Placing its logo on a sporting team's uniform
C. Sales representatives visiting gyms to demonstrate the product
D. Advertising on television during football games throughout the season

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q13

A beauty company sends samples of its new lip balm to members of its loyalty program and to online beauty bloggers.

What strategies is the company using?

A. Publicity and global branding
B. Global branding and opinion leaders
C. Customisation and relationship marketing
D. Relationship marketing and opinion leaders

Question 3 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q12

Which of the following is an example of publicity for a restaurant?

A. Changing the menu to include vegetarian dishes
B. A review of the restaurant by a food critic on his blog
C. Offering free dessert for customers who spend over $100
D. Establishing a loyalty scheme with rewards for regular diners

Question 4 (20 marks)

Source: HSC 2014 Business Studies Exam, Section IV, Q27

Assess the importance of using a mix of promotional strategies in the marketing of goods and services.

Question 5 (1 mark)

Source: HSC 2009 Business Studies Exam, Section I, Q5

Which of the following is an example of *promotion* as a marketing strategy for a new line of shampoo?

A. Creating a brand name
B. Making it available only in hair salons
C. Packaging in environmentally-friendly bottles
D. Advertising it as adding shine and volume to hair

More exam questions are available in your learnON title.

10.7 Place and distribution

SYLLABUS LINK In this subtopic you will learn about place/distribution, including distribution channels, channel choice (intensive, selective, exclusive) and physical distribution issues (transport, warehousing, inventory).

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The fourth 'P' of the marketing mix is **'place'** or **distribution**. Once a business manufactures a product, it must see that the product gets into the customers' hands. For this to happen successfully, an efficient distribution system is required. Distribution is necessary because most products are not used by the same business that makes them. This textbook, for example, was transported and warehoused a number of times between the authors, publisher, printer, wholesalers and retailers before it reached you, the consumer.

10.7.1 Distribution channels

place or **distribution** activities that make the products available to customers when and where they want to purchase them

distribution channels or **marketing channels** the routes taken to get the product from the factory to the customer

Distribution channels or **marketing channels** are the routes taken to get the product from the business to the customer. This process usually involves a number of intermediaries, such as the wholesaler, broker, agent or retailers. Apart from the retailer, the other intermediaries are often 'invisible', with the customer knowing very little about their role and operation.

FIGURE 10.28 The delivery of a product to a customer is the final stage in the distribution process. Blake Davies, a barista employed by Casualties Espresso in Port Macquarie, delivers coffee and food to customers on his skateboard. Juggling up to nine coffees at a time, Davies skilfully manoeuvres around people and cars to deliver his customers' morning cuppa.



Traditional distribution channels

The four most commonly used channels of distribution are described below.

1. *Producer to customer.* This is the simplest channel and involves no intermediaries. Virtually all services, from tax advice to car repairs, use this method.
2. *Producer to retailer to customer.* A retailer is an intermediary who buys from producers and resells to customers. This channel is often used for bulky or perishable products such as furniture or fruit.
3. *Producer to wholesaler to retailer to customer.* This is the most common method used for the distribution of consumer goods. A wholesaler is an intermediary who buys in bulk, from the producer, then resells in smaller quantities to retailers.
4. *Producer to agent to wholesaler to retailer to customer.* An agent distributes products to wholesalers but never owns the product. Agents are paid a commission by the producer. Usually agents are used for inexpensive, frequently used products. A business that does not have any sales representatives will often use an agent instead.

BizFACT

The Iconic does not have a traditional distribution channel. To cut delivery and distribution times, their suppliers list their products on The Iconic website but their stock is sent directly to consumers rather than to The Iconic's distribution centre. The Iconic's app, which has been downloaded on more than one million devices so far, is now the e-tailer's primary sales channel, and its growing marketplace.

Innovative distribution methods — non-store retailing

Businesses are always looking for different ways to distribute their products. The purchasing of products from a store or a supplier is the oldest and most common form of distribution. **Non-store retailing** — that is, retailing activity conducted away from the traditional store — is gaining in popularity. Methods such as door-to-door selling, mail-order catalogues, party-plan merchandising and vending machines have been used for a number of years. However, with rapid changes in electronic communication, businesses are beginning to exploit types of electronic marketing (e-marketing) as alternative methods. Two of the most rapidly developing methods are e-commerce and m-commerce.

1. *E-commerce* refers to the buying and selling of goods and services via the internet. The web is revolutionising the way consumers shop. Consumers who are 'time poor' prefer the convenience of shopping online. Other consumers like being able to shop around for the cheapest price or have the opportunity to select from a wide range of products at a time that suits them. Back in 2000, less than 1 per cent of retail sales came from e-commerce. However, online sales have climbed each year since then, and by 2019 online sales made up about 14.1 per cent of total retail sales. This will be discussed in more detail in subtopic 10.9.
2. *Mobile commerce (m-commerce)* refers to the buying and selling of goods and services through wireless handheld devices such as smartphones and tablets. As e-commerce sales continue their dramatic growth, mobile commerce is grabbing a larger market share, with smartphone-enabled purchases making up 49 per cent of total online retail commerce in 2020. This growth is partly due to retailers' ongoing efforts to provide smartphone-friendly offerings and checkout solutions to customers.

non-store retailing retailing activity conducted away from the traditional store

FIGURE 10.29 The steady rise of online sales has led to the 'retail apocalypse' — a US term that refers to the closing of a large number of retail stores. Since the pandemic, thousands of retail stores have closed and retail bankruptcies have been happening at a record pace. Could this be the end of bricks-and-mortar retailers?



As more people use the internet for shopping, the traditional distribution channels will be modified. Some retailers and wholesalers may be bypassed as customers deal directly with manufacturers. Electronic post and parcel delivery channels will be used more extensively to meet the increasing demand.

10.7.2 Channel choice — including intensive, selective and exclusive

How a business chooses the channel of distribution best suited to its product depends largely on the location of the business's market or market coverage. **Market coverage** refers to the number of outlets a firm chooses for its product.

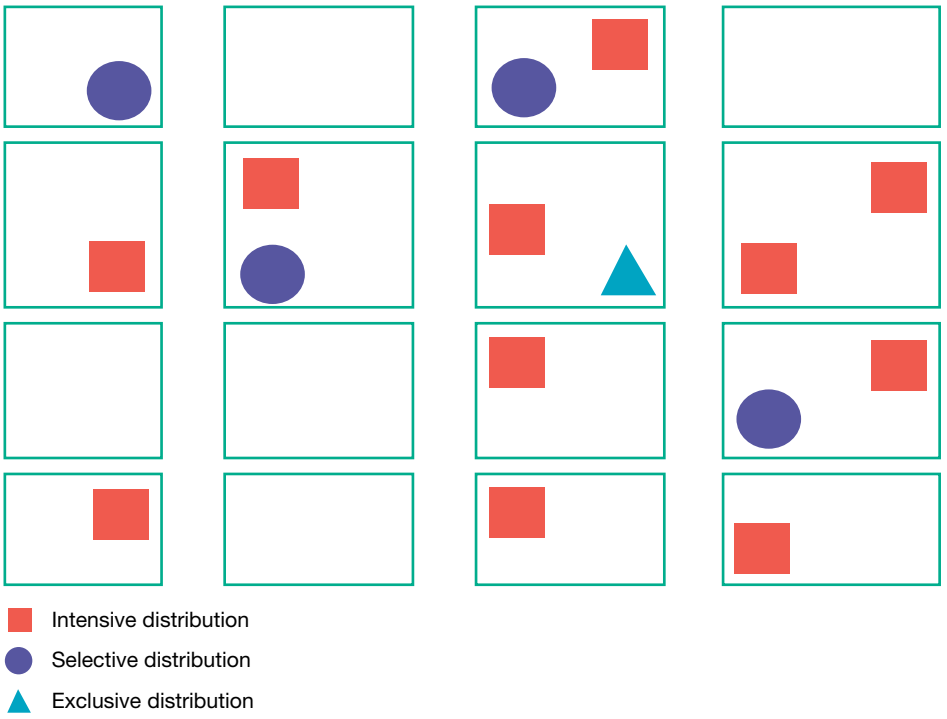
A business can decide to cover the market in one of three ways as follows, the difference being the intensity of coverage.

1. *Intensive distribution*. This occurs when the business wishes to saturate the market with its product. Customers can shop at local outlets and be able to purchase the product. Many convenience goods, such as milk, lollies and newspapers, are distributed this way.
2. *Selective distribution*. This involves using only a moderate proportion of all possible outlets. Clothing, furniture and electrical appliances are often distributed using this method. The customer is prepared to travel and seek out a specific retail outlet that stocks a certain brand.
3. *Exclusive distribution*. This is the use of only one retail outlet for a product in a large geographic area. This method of distribution is commonly used for exclusive, expensive products.

market coverage refers to the number of outlets a firm chooses for its product

Figure 10.30 illustrates the three levels of market coverage.

FIGURE 10.30 The boxes here represent the different customer groups that make up a market. The coloured shapes within the boxes represent the type of distribution method used to achieve market coverage. The square shape appears in many of the boxes because this distribution of product reaches a range of different customers.



BizFACT

Different channels of distribution are used to get the 'right' product in the 'right' quantity to the 'right' location at the 'right' time.

10.7.3 Physical distribution issues

Physical distribution is all those activities concerned with the efficient movement of the products from the producer to the customer. Physical distribution is therefore the movement of the products themselves through their channels of distribution. It is a combination of several interrelated functions, including transportation, warehousing and inventory control.

Transport

An intricate network of transportation is required to deliver the vast array of products to customers. Transportation is a key supply chain management function that involves the efficient movement of a product from the manufacturer to the customer.

The mode of transportation a business uses will largely depend on the type of product and the degree of service the business wishes to provide. The four most common methods of transportation are rail, road, sea and air. The transportation methods chosen must meet customers' needs. Customers demand products be delivered when they require them and in good order. Having a transportation program that can do this provides customer satisfaction and gives a business a competitive advantage.

Warehousing

Warehousing is a set of activities involved in receiving, storing and dispatching goods. A warehouse acts as a central organising point for storing goods that will be efficiently distributed later. While a small, home-based business might warehouse products in a spare room or garage, larger businesses typically own or rent space in a building that is specifically designed for storage.

Some basic warehousing elements that need to be considered include:

- a shelving system that offers maximum storage capacity and easy access
- inventory control software that can inform the business about the quantities of each product, as well as their location in the warehouse
- equipment that can move products, e.g. forklifts, conveyor belts, etc.
- security to protect the products being stored
- access to transportation to bring products in or move them out once orders are placed
- a climate control system for particular products, e.g. those requiring refrigeration.

As businesses look to improve efficiency, warehouse automation has been increasing. An automated warehouse uses a few key pieces of technology to move products, for example robotic systems. At its most basic, an automated warehouse attempts to cut down on manual tasks (see the following case study).

BizFACT

Amazon has been keeping its scientists busy with a range of new ideas for how best to store online purchases in preparation for distribution. And while it may sound far-fetched, the company has lodged a patent in the US that would see its storage warehouses submerged underwater, with items brought to the surface using acoustic vibrations. With online shopping accounting for about 15 per cent of all retail sales, and increasing, there will be a need for this extra storage.

Inventory

Customers find it frustrating when a product they wish to purchase is 'out of stock', and a business that repeatedly allows this to happen will lose sales and market share. To avoid this, businesses may implement an **inventory control** system. If a business carries too much stock on its inventory, it will experience high storage costs. However, too little stock results in lost sales or 'stock-out costs'. The goal of inventory is to find the correct balance between these two situations. Inventory management is examined in greater detail in chapter 5.

physical distribution all those activities concerned with the efficient movement of the products from the producer to the customer

inventory control a system that maintains quantities and varieties of products appropriate for the target market

SNAPSHOT

Case study: Woolworths warehouse automation

Around 700 jobs will be lost as Woolworths automates key logistics facilities in Sydney and Melbourne.

There are currently about 1350 people employed at warehouses in Minchinbury and Yennora in Sydney, and Mulgrave in Melbourne. All three centres will be closed in 2025.

Woolworths said that less than half those workers — just 650 staff — would be needed to run its new automated and semi-automated distribution centres, which would be located in the south-west Sydney suburb of Moorebank.



However, Woolworths will retain its current temperature-controlled operations at Minchinbury, which will continue to employ about 460 people.

The new Moorebank centres will be owned by Qube logistics and initially leased by Woolworths for 20 years.

Woolworths is planning to invest $700–780 million in the technology and fit-out of the new distribution centres, while Qube will invest between $420–460 million to build them.

The centres are targeting a five-star green rating with the inclusion of solar panels, LED lighting and rainwater harvesting.

Woolworths said the construction phase would employ about 1000 people.

'Fewer trucks, faster restocking'

It is connected by rail to Port Botany, and Woolworths said it will mean at least 26 000 fewer truck movements per year on Sydney's roads.

Woolworths chief supply chain officer Paul Graham said the company had seen the benefits of the new, automated Melbourne South Regional Distribution Centre and was looking to build on those in New South Wales.

'Cutting-edge automation will build tailored pallets for specific aisles in individual stores, helping us improve on-shelf product availability with faster restocking, reducing congestion in stores, and enabling a safer work environment for our teams with less manual handling,' he said in a statement.

'The new facilities will also help progress our localised ranging efforts, with the ability to hold many thousands more products centrally than we can in our existing facilities.'

Mr Graham said Woolworths would look to employ as many existing staff as possible in its new Moorebank facilities.

'We'll look to offer redeployment opportunities wherever possible with 650 roles available at the new Moorebank sites, as well as providing a wide range of support and career transition services to our team well before site closures,' he said.

However, Woolworths has set aside $176 million to cover potential redundancy costs for existing staff.

The new distribution centres remain subject to New South Wales government planning approval.

Source: Michael Janda, 'Woolworths warehouse automation set to eliminate 700 jobs in Sydney and Melbourne', www.abc.net.au, 23 June 2020.

Resources

Weblinks The Iconic
Red Balloon
Amazon

KEY IDEAS

- Place or distribution are activities that make products available to customers when and where they want to purchase them.
- Channels of distribution or marketing channels are the routes taken to get the product from the factory to the customer.
- The four most commonly used channels of distribution are:
  - producer to customer
  - producer to retailer to customer
  - producer to wholesaler to retailer to customer
  - producer to agent to wholesaler to retailer to customer.
- Non-store retailing is retailing activity conducted away from the traditional store, including e-commerce and m-commerce.
- Market coverage refers to the number of outlets a firm chooses for its product.
- A business can decide to cover the market in one of three ways:
  - intensive distribution: when the business wishes to saturate the market with its product
  - selective distribution: using only a moderate proportion of all possible outlets
  - exclusive distribution: only one retail outlet for a product in a large geographic area.
- Physical distribution is all those activities concerned with the efficient movement of the products from the producer to the customer.
- Physical distribution issues include:
  - transport: this refers to the efficient movement of a product from the manufacturer to the customer
  - warehousing: a set of activities involved in receiving, storing and dispatching goods
  - inventory: developing a system that maintains quantities and varieties of products appropriate for the target market.

10.7 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.7 Quick quiz | **10.7 Exercise** | **10.7 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 5, 9	3, 7, 10, 12, 14	4, 6, 8, 11, 13

10.7 Exercise

Revision

1. **Define** the term ‘place’.
2. **Clarify** the importance of distribution in the marketing process.

3. **Propose** a distribution channel for the sale of:
   a. a daily newspaper
   b. a washing machine
   c. an imported motor vehicle
   d. office furniture.
4. Traditional shopping transactions involve a number of organisations in the supply chain: producer to warehouse to wholesaler to retailer to consumer. **Create** a flowchart to show how an e-commerce transaction could take place.
5. In small groups, use the brainstorm technique to **identify** the advantages and disadvantages to a business of selling via the internet. Select a spokesperson to share the group's comments with the rest of the class.
6. From the following products, **determine** those that are intensively, selectively or exclusively distributed.
   a. Coca-Cola
   b. Ferrari motor vehicles
   c. Billabong clothing
   d. Streets ice-cream
   e. Samsung televisions
   f. Rare coins
7. **Why** would a business select an exclusive rather than an intensive distribution strategy?
8. **Determine** which method of transportation would be most appropriate for the following products: road, rail, air or boat. Justify your answer.
   a. Coal to Japan
   b. Wheat to the silo
   c. Sheep to the market
   d. Fresh fruit to Tokyo
   e. Iron ore from the mine to the port
   f. Pepsi to the supermarket
9. **Identify** the activities involved in warehousing.

Read the 'Woolworths warehouse automation' case study and answer questions 10 to 12.

10. **Discuss** the impact of the new automated warehousing for Woolworths.
11. **Predict** the impact the automated warehouses will have on customers.
12. **How** will these new warehouses help Woolworths cut costs?

Extension

13. Investigate the operation of an online retailer (e-tailer) such as The Iconic, Red Balloon or Amazon. **Evaluate** the site visited, reporting on:
    a. ease of navigation
    b. layout of the home page
    c. methods of payment
    d. ease of product selection
    e. return and refund policy
    f. delivery charges and options.
14. a. 'Holding either too little or too much stock is to be avoided.' **Discuss**.
    b. **Propose** a system a business can adopt to prevent either situation.

10.7 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q5

A bakery produces organic bread that is sold in health food stores.

Which is the most appropriate channel choice for this product?

A. Exclusive
B. Extensive
C. Intensive
D. Selective

Question 2 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q5

A manufacturer sells her organic meals only to major supermarkets.

Which distribution channel has the manufacturer chosen?

A. Exclusive
B. Intensive
C. Selective
D. Warehousing

Question 3 (3 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q22c

A business develops video games. It had three different games for sale last year. The table shows forecast and actual sales for each game.

	Forecast sales ($)	Actual sales ($)
Game A	500 000	495 000
Game B	200 000	100 000
Game C	300 000	800 000

With reference to the information, recommend a strategy for distributing game *C*.

Question 4 (4 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q21a & b

A producer of gourmet ice-creams chooses selective distribution for her products.

a. Why might the producer have chosen selective distribution for her products? **(2 marks)**
b. Outline ONE physical distribution issue that will need to be considered. **(2 marks)**

Question 5 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q8

A business has shifted from intensive distribution to more selective distribution.

What is the most likely reason for this?

A. To increase market share
B. To decrease personal selling strategies
C. To reposition products as higher quality
D. To expand the number of intermediaries

More exam questions are available in your learnON title.

10.8 People, processes and physical evidence

SYLLABUS LINK In this subtopic you will learn about people, processes and physical evidence.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

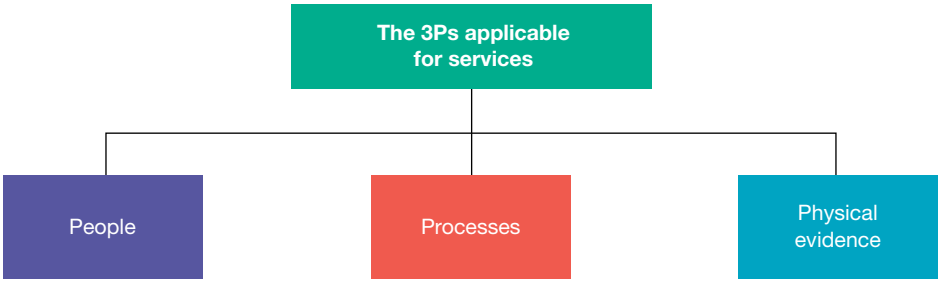
So far we have discussed the four Ps of the marketing mix, which is considered the basic cornerstone of marketing. This traditional approach was developed in the age of marketing dominated by the rapid growth in manufacturing during the 1950s to 1960s. Consequently, these four Ps are considered appropriate for tangible products (goods) such as clothing, electronic appliances, perfumes and motor vehicles. However, as the service sector within the economy expanded, this traditional approach to marketing was viewed as somewhat outdated.Therefore, three more Ps have been added — people, processes and physical evidence (see figure 10.31) — which apply especially to intangible products (services) such as tourism, entertainment and hospitality.

These three more Ps, when combined with the original four Ps, create the **extended marketing mix**. Extending the marketing mix by adding people, processes and physical evidence to the usual 4Ps connects the marketing function much closer to both human resource management and operations, thus illustrating the interdependence between these functions.

BizFACT

It is important to acknowledge that even goods have a service component surrounding them such as after-sales service.

FIGURE 10.31 The three extra Ps of the extended marketing mix. Although the three Ps' role in the success of the marketing process may not be as obvious as that of the original four Ps, they play an unassuming yet important role in ensuring the success of the product.



10.8.1 People

The **people** element refers to the quality of interaction between the customer and those within the business who will deliver the service. All the people involved in the business can have an impact on the marketing mix. It is therefore important that businesses recruit the right workers and then train them appropriately on how to perform the service and leave a good impression.

extended marketing mix the combination of people, processes and physical evidence with the four main elements of the marketing mix

people the people element refers to the quality of interaction between the customer and those within the business who will deliver the service

Consumers base their perceptions and make judgements about a business based on how the employees treat them. For example, in a hotel or restaurant, the employees are actively involved in delivering the marketing message because they are the 'human face' of the business. How the staff speak to customers, deal with enquiries and handle complaints are all part of the marketing experience and of critical importance. Consequently, it is vital that owners and managers establish a culture of customer focus and put it into practice.

A culture that has evolved to include poor practices or indifferent service can be a disaster for marketing, so it is important that leaders in the business set the standard, and ensure it is followed. All business owners want their business name, products and brand to have the highest possible reputation. Maintaining this reputation is in the hands of the staff. It is essential they be trained with the appropriate skills, be motivated to provide good service, and have a positive attitude towards the products they are selling.

FIGURE 10.32 A study by KPMG in 2019 surveyed more than 2500 Australian consumers about their interactions with over 100 brands. Their report found that the 50 companies that offered the best customer service enjoyed 54 per cent greater revenue growth and 202 per cent greater profitability than the worst performing companies studied. Singapore Airlines was recognised two years in a row as the country's top customer service provider.



People are the most important element in any service or experience. The interaction between the employees, especially frontline or customer service staff, and customers can determine the success of any marketing campaign.

10.8.2 Processes

When you order a meal from a McDonald's restaurant it will be delivered within a few minutes. Behind this efficient delivery system is a set of well-planned and well-organised processes. When employees such as those at McDonald's provide a service, they rely on a delivery system — a set of processes — to perform their task. **Processes** refers to the flow of activities that a business will follow in its delivery of a service. This may relate to the actual delivery of the product, or how the customer finds out about the product, selects it and then makes their purchase. All businesses set up operating systems and processes as part of the way they do business. Businesses need to ensure that their processes and procedures are customer-friendly and that they satisfy customer needs.

Consider all the processes involved in booking a flight online. The airline's website is used to enter the details. A confirmation email will be automatically generated providing a booking reference. An electronic boarding pass can be downloaded and printed. A day prior to the flight, a seating allocation can be done online. The delivery system that allows this to happen is part of the process element of marketing.

The total purchasing experience is important in achieving customer satisfaction. Do customers have to wait a long time to be served? Are there long queues at checkouts? Can goods ordered online be guaranteed delivery within a reasonable time? Are invoices correct? All these questions relate to the processes and systems used by the business in carrying out its operations.

processes refers to the flow of activities that a business will follow in its delivery of a service

Customers will often want access to a variety of payment methods, such as cash, EFTPOS, PayPass or PayWave, or credit cards, as well as deferred payments such as lay-by and Afterpay. Ensuring all these processes are available and working efficiently will enhance the marketing of the business. Even simple things such as answering a telephone promptly, having a reliable message system, and responding to messages within a reasonable time can be process issues that can make a difference between gaining or losing a customer. All systems and processes need to be designed to maximise the benefit for the customer, not just for the convenience of the business or its staff.

BizFACT

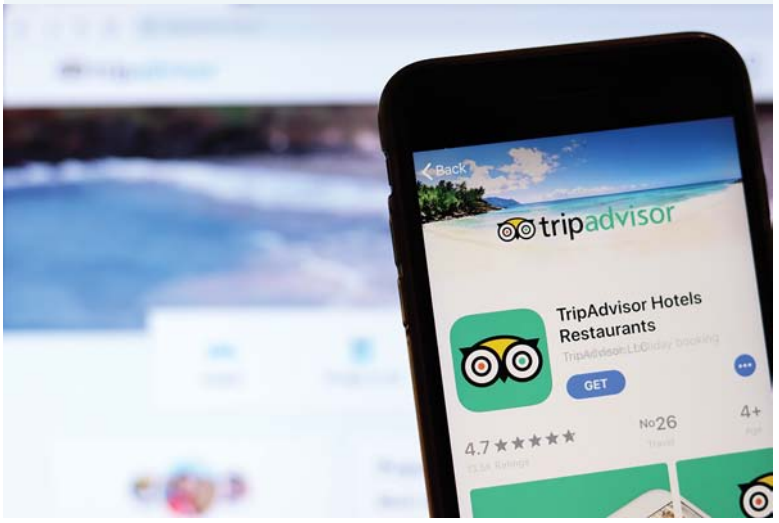
Convenient methods of payment, such as PayPass, PayWave or Afterpay provide an efficient process to assist in the marketing strategy.

10.8.3 Physical evidence

Imagine you go to a restaurant. You are very satisfied with the product, price, people and process, but the cutlery was dirty, the chairs were uncomfortable and the menu was difficult to read. You would probably not eat there again because of this physical evidence. **Physical evidence** refers to everything that the customer sees when interacting with a business. This could refer to the physical environment experienced by the customer or the materials needed to carry out the service such as signage, business logo or brochures.

Customers make judgements about the business based on these features. Essentially, physical evidence can assist a business with positioning its brand and attracting its target market. Unlike tangible goods, it is difficult for a business's marketing services to provide customers with a 'try before you buy' sample unless a free trial is offered. Customers initially buy services on trust and they make judgements about the business based on the physical evidence. Consequently, a business should provide high-quality physical evidence to create an image of value and excellence.

FIGURE 10.33 Review websites can provide evidence that may influence potential customers.



Physical evidence also refers to the physical state of the business premises, and the physical state of a website or online presence. A clean and well-presented location can be reassuring to the customer that high standards are observed, while an untidy or dirty premises does not inspire such confidence. The state of the online presence is also important. A website that is simple to navigate, with clear links to different products, as well as clear contact details and a secure ordering system, will always win over a website that is messy and hard to navigate.

Providing access to feedback from customers can also be a way of providing physical evidence to potential customers. The hospitality industry now has a number of review websites such as Zomato and Gourmet Traveller, and holiday destinations and accommodation are regularly reviewed on sites such as TripAdvisor. Encouraging satisfied customers to use independent review websites can provide valuable evidence that can influence the decisions made by potential customers (see figure 10.33).

physical evidence everything that the customer sees when interacting with a business

SNAPSHOT

Case study: PACK & SEND — people, processes and physical evidence

PACK & SEND is Australia's leading and most recognised parcel courier and freight delivery reseller.

CEO and founder Michael Paul established the company with his wife in 1993 after noticing that businesses and consumers were looking for one-stop-shop solutions for sending anything, anywhere — that also included a convenient packaging service. The three extra Ps of the extended marketing mix have played a crucial role in the success of this business; so much so, that two of them have become part of their five core values guiding their actions and decisions in striving to achieve their purpose. One of their core values is:

> **People are the cornerstone of our success**
>
> *We promote an environment of teamwork, mutual respect and growth in learning and personal development.*
>
> We recognise that the company's success depends upon the initiative taken individually and the ability to work as a team. Therefore, we believe in recruiting quality people, mentoring and training for performance, engaging them with the brand values, listening for feedback and leading with integrity.

Michael Paul considers internal factors, such as business culture and employees, to be the key difference between successful businesses. He believes it is important that the management team nurture a culture that truly values people, regardless of their position, because a supportive team culture can be one of the company's greatest strengths. This culture will help align all the stakeholders around the vision, mission and values of the brand.

Another one of PACK & SEND's core values, which relates to 'processes' is:

> **Systems are the foundation of great organisations**
>
> *We believe the true product of our business is not what we sell but how we sell it. That is, the true product of our business is the business itself — the systems.*
>
> We recognise that the success of our organisation is dependent on all people in the business following a system. Therefore, we believe in the systemisation of all areas of our business for uniform application across our network — so that we can achieve higher productivity and customers can always experience a consistent superior service.

PACK & SEND operates an international franchise model. Systemisation is therefore very important because at the core of a franchise's success is a tried, tested, and perfected system that can then be duplicated over and over again. 'Systemising helps a franchisor keep track of metrics and identify what works and what doesn't, enabling them to pinpoint the areas in which it makes strategic sense to invest more. Systemisation is also essential to create a business model that is a format for success which of course improves many processes such as employee training and allows new franchisees to easily pick up where their predecessors left off.'

The variety of processes PACK & SEND have established in the delivery of their services contribute to the aim to always satisfy customer's needs. PACK & SEND are the only couriering and logistics company where customers can engage with the brand via three channels: by visiting one of their 100+ retail service centres, phoning the company's call centre or online.

In relation to 'physical evidence', even though the company offers an online booking system, they still advocate physical points-of-presence with more than 100 retail service centres in Australia, New Zealand and the United Kingdom. The company feels that these service centres play a big part in improving delivery services for e-commerce customers. 'Important e-commerce solutions like convenient product returns, alternate delivery points and convenient parcel drop-off points are all logistics services that are reliant on a national retail footprint. While it's true that most people have been keen adopters of the Internet, there's nothing like being able to walk into a store and have a conversation with someone. Physical retail spaces offer convenience, multisensory consumer experiences (the desire to see, touch and feel products), personal consultancy and a friendly face on the other side of the counter.'

KEY IDEAS

- Three more Ps have been added that apply especially to intangible products (services): people, processes and physical evidence.
- The people element refers to the quality of interaction between the customer and those within the business who will deliver the service.
- Consumers base their perceptions and make judgements about a business based on how the employees treat them.
- Processes refers to the flow of activities that a business will follow in its delivery of a service.
- Without a tangible product, the processes must be highly efficient to achieve customer satisfaction.
- Physical evidence refers to everything that the customer sees when interacting with a business. This could refer to the physical environment experienced by the customer or the materials needed to carry out the service such as signage, business logo or brochures.
- A business should provide high-quality physical evidence to create an image of value and excellence.

10.8 Activities

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10.8 Quick quiz on | **10.8 Exercise** | **10.8 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 6, 7, 9, 12, 13	2, 3, 4, 5, 8, 10, 11, 14, 15, 16, 17, 19	18, 20

10.8 Exercise

Revision

1. **Identify** the three extra Ps of the extended marketing mix.
2. **Why** is it important to extend the marketing mix in the current business environment?
3. **Deduce** whether the extension of the marketing mix means that some of the traditional Ps are less relevant today.
4. **Why** is a positive culture in a business an important element in marketing?
5. Select which of the traditional Ps of the marketing mix you consider most likely associated with customer service. **Justify** your answer.
6. Think of a business where the 'people' element was outstanding. **Clarify** what made the interaction so positive.
7. **Define** the term 'processes'.
8. **Investigate** the main processes involved with the following businesses: (a) M and S Davidson Accountant, (b) Billabong cafe, (c) Theatre Royal, (d) Excelsior Hotel.
9. **Identify** six elements an airline could use as physical evidence to create a positive image.
10. **Why** is it important for a business to display favourable physical evidence?
11. **How** can staff in a business contribute to the positive marketing of the business?
12. **Outline** two reasons why physical evidence is an important part of the marketing mix.
13. **Identify** two examples of systems and processes that could be used to market a business.
14. An online business sends an email to all customers after goods have been delivered to their homes. This email directs the customers to a survey website where they are invited to rate the quality of the service they received from the business. **Explain** how this business is making use of 'physical evidence' as part of its marketing mix.

Read the 'PACK & SEND — people, processes and physical evidence' case study and answer questions 15 to 17.

15. **How** do PACK & SEND look after their 'people'?
16. **Why** is systemisation so important to PACK & SEND?
17. To **what extent** are physical points-of-presence important for online businesses?

Extension

18. In small groups, use the brainstorm technique to **determine** the (a) people and (b) processes involved in a business that offers inclusive tours of Europe.
19. **Recommend** a set of five processes a business would need to adopt to resolve issues when customers complain about a faulty product.
20. 'Most goods have a service component surrounding them. Consequently, businesses selling goods such as motor vehicles or electrical appliances must take into consideration the extended marketing mix.' **Evaluate** the accuracy of this statement. Provide examples in your answer.

10.8 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q17

Staff members at VAL's vegan restaurant wear uniforms with a large letter V on them. They are expected to greet customers with a smile and clean up any spills immediately.

Which element of the marketing strategy are these requirements an example of?

A. Packaging
B. Positioning
C. Promotion mix
D. Physical evidence

Question 2 (1 mark)

Abdulla has a staff that has experience in dealing with all types of customers. Her strategy is that staff must provide a positive experience for customers. Which marketing strategy best describes Abdulla's actions?

A. Physical evidence
B. People
C. Promotion
D. Channel choice

Question 3 (1 mark)

A dentist posts out reminders to her patients. Which marketing strategy is the dentist using?

A. Processes
B. Physical evidence
C. People
D. Distribution

Question 4 (1 mark)

Ben and Stuart have re-modelled the interior of their clothing shop. It is now a very modern shop with references to men's style around the walls. Ben and Stuart say they are building the customers' expectations of the clothes they sell and the service they provide. Which marketing strategy best describes this action?

A. Processes
B. People
C. Physical evidence
D. Product

More exam questions are available in your learnON title.

10.9 E-marketing

SYLLABUS LINK In this subtopic you will learn about e-marketing as a marketing strategy.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Technology has driven the push to market products to customers worldwide. Businesses now have access to global markets through setting up websites that can promote products and then dispatch them to the other side of the globe within 24 hours of ordering. With rapid changes in electronic communication and the development of the 'information superhighway', marketers are beginning to exploit all types of e-marketing. **E-marketing** (electronic marketing) is the practice of using the internet to perform marketing activities.

FIGURE 10.34 Australians spent $29.7 billion on online shopping in 2020. There has been an increase in online shopping as consumers changed their purchasing behaviour and retailers increased their online capabilities in response to the COVID-19 pandemic. Approximately 80.8 per cent of people in Australia were shopping online and very soon one out of every ten items will be purchased off e-commerce stores.



Recent surveys have shown that Australian businesses, especially retailers, have been slow to adopt e-marketing, with many offering product information, but no opportunity for customers to actually purchase online. While 71 per cent of Australians use social media, only 51 per cent of SMEs have a social media presence. In addition, the majority of small businesses in Australia do not have a website — 59 per cent to be exact.

In this new digital age, when most people search and shop online for the products and services they want, businesses need to realise that traditional marketing methods alone are no longer enough. If a business wants to be successful, they need to be where the customer is; if not, they're missing the boat. The big risk for Australian businesses is that consumers seeking the convenience of online shopping will purchase from overseas retailers and completely bypass local businesses.

BizFACT

The terms internet marketing, web marketing and online marketing are frequently interchanged and can often be considered synonymous.

10.9.1 E-marketing technologies

The main technologies presently available for e-marketing include web pages, podcasts, electronic messages, blogs, location-based marketing and social media advertising.

e-marketing (electronic marketing) the practice of using the internet to perform marketing activities

Web pages

A web page conveys information in the form of a combination of text, graphics, animation and video. A number of related web pages linked together form a website. When searching for the website of a particular business, the user will normally be directed first to that business's home page. This contains basic information about the business and a number of links to other web pages within the website that can provide detailed information about the location of the business premises (including maps and photographs), available products and online ordering facilities. A well-designed home page is a powerful marketing tool.

FIGURE 10.35 A recent study by GoDaddy has revealed that the majority (59 per cent) of small businesses in Australia do not have a website. The main reasons survey participants gave for not having a website were: that they felt their business was too small (44 per cent); because it is too expensive (30 per cent); and because they don't have the time to build or manage one (17 per cent).



Podcasts

Podcasting involves the distribution of digital audio or video files over the internet. As a general rule, a podcast is directed to a number of users who subscribe to that particular podcasting service, and who receive regular updates.

Business's main use of podcasts is for marketing and advertising purposes. Many independent podcasters sell advertising time in the same way as commercial radio stations. If a particular podcast is aimed at the same audience as the target customers of a business, podcast advertising can be a very effective way of reaching those customers. For example, a sporting goods store may choose to advertise through a podcaster aiming at triathletes; a specialist food store owner could look at advertising on a podcast aimed at vegetarians and vegans.

Electronic messages

A commercial electronic message is any electronic message (such as email, SMS, MMS or instant message) that offers, advertises or promotes a business, good or service. For example, businesses can use this method to send a newsletter, promote a sale or send a coupon to loyal customers for a discount.

SMS has distinct advantages over email in that messages are delivered automatically to one or more recipients without the need for them to dial in or log on. Text messages can also be used to alert regular customers of any special deals on offer and notify suppliers of the arrival of a goods shipment.

Blogs

A **blog** is an online diary or journal. It is usually possible to add comments, ask questions, provide feedback or share opinions on a blog. A business can use blogs in a number of ways.

Many businesses set up external blogs, which allow for communication between the business and its existing and potential customers. A blog of this type can be used to announce new products or changes in trading hours, and to gather feedback and comments from a variety of stakeholders. As a public relations exercise, an external blog can have the following advantages for a business:

1. It allows the business owner and employees to establish a reputation for expertise, by providing detailed information on products and services.
2. New ideas for products and services can be put to the public to gain comment and feedback.
3. A blog by its nature is informal, so it can present a human face to the public and build trust with customers.

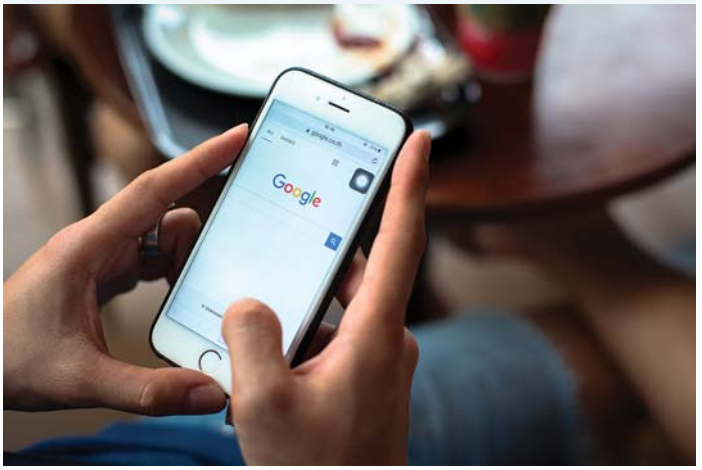
podcasting the distribution of digital audio or video files over the internet

blog an online journal that can be added to by readers

Location-based marketing

The ability for mobile devices to track and report a person's location has enabled businesses to tailor marketing messages based on a person's location. Location-based marketing allows businesses to adapt and deliver targeted marketing messages to customers based on where they are located through mobile devices. By knowing where consumers are, brands are able to tap into daily habits and encourage consumers with relevant offers and messages based on their location. Customers receive these marketing messages by using their mobile to search for local businesses on the internet or 'check in' to a particular place through an online location-based service.

FIGURE 10.36 A popular example of location-based marketing is geotargeting. Geotargeting is based off IP addresses. Every connected device has a unique IP address, making it identifiable. Device IP addresses can then be matched to determine where users are located. For example, Google search results — if you search 'coffee shops', Google will use location data based on the IP address of the device you are searching from to return information on coffee shops in your area.



Social media advertising (SMA)

Over the past few years, businesses have been increasingly using social media to advertise their products. Businesses are becoming increasingly aware that **social media advertising (SMA)** can have positive results, especially when used in combination with traditional advertising methods. The main advantages of SMA are that it is:

- inexpensive in comparison to traditional advertising methods
- easy to use and monitor
- an effective method to gain exposure
- possible for marketers to accurately measure the **reach** (the number of people exposed to the message) and **frequency** (the average number of times someone is exposed) of SMA.

However, the main disadvantage of SMA is that marketers do not have complete control over what online consumers write about the business. Users have the freedom to discuss, review, criticise and even ridicule a product or a specific business.

The reason for this not-so-quiet revolution in marketing and advertising is that marketers realise they must go to where the customers are to be found. Facebook, for example, has over 2.89 billion monthly users.

In the early days, online advertising was very much like an outdoor billboard. Now, due to the rapid advances in technology, SMA is more engaging and inclusive. Businesses are getting customers they have reached via a social network platform to, in turn, reach out to other potential customers. Online customers are not simply being targeted for advertising; in many cases they are contributors in the creation and distribution of advertising. In this way, the SMA enables businesses to constantly build relationships with their customers (see the following case study)

social media advertising (SMA) a form of online advertising using social media platforms such as Facebook, YouTube and Twitter to deliver targeted commercial messages to potential customers

reach the number of people exposed to the message of an advertisement

frequency the average number of times someone is exposed to the message of an advertisement

SNAPSHOT

Case study: Social media advertising — #MesCheveux



After gaining seventeen years' experience in the hairdressing industry and establishing a great reputation through working at prestigious salons, Charlie Helou decided to take the risk and start his own salon, Mes Cheveux, in 2015 with business partner Josephine Staltari.

With high-quality products, modern facilities and highly skilled and creative professionals, Mes Cheveux has positioned itself as a five-star luxurious salon in the Parramatta area. Being in the establishment phase, the owners didn't have a lot of funds to spend on marketing and so they came to rely on social media advertising.

Mes Cheveux has a vibrant social media presence on Instagram and Facebook. Since hairdressing is a visual industry, social media is the perfect platform for the salon to 'show off' their work as well as their exclusive products and services. 'This is probably the main way we use social media: to showcase what our talented stylists can do. We often post before-and-after pictures of our client's new hairstyles. Not only is this proof of what we do, but if the customer shares those photos with their own personal networks, this generates greater exposure for our business.' Social media has also changed the requests they get from clients. 'Many clients refer to some of our posts for inspiration on their cut, colour or style and come in already knowing what they want done.'

Being in a prime location in Westfield Parramatta, the salon gets a lot of business from passing trade. However, Charlie has found that a large percentage of new business has been generated from social media. 'Salon testimonials and reviews are a great way to attract brand new clients to the salon. Word of mouth recommendations through social media are an effective way of building brand awareness and increasing new client patronage.'

Social media is a powerful marketing tool that has allowed them to 'chat' with customers even after they've left the salon. 'We can show customers new things around the salon, remind them to use certain products, send warm wishes on special occasions and of course show everyone our work!' Charlie receives many enquiries through social media outside their opening hours, which he always makes sure he responds to in a timely manner.

Charlie also uses social media as a research tool. He currently follows industry leaders, fashion houses and other stylists. Social media platforms have enabled him to keep up with the latest industry trends, be inspired by other hairdressers' creativity and keep an eye on what their competition is doing.

'Two of the best things about social media is that it's not an expensive form of marketing and it's simple to use — it requires only a small amount of attention each day to create a loyal brand following. Social media is a great way to engage with our local community as well as current and potential customers and spread more awareness about our salon.'

FIGURE 10.37 In 2019 Dove launched a campaign called Project #ShowUS. According to Dove, 70 per cent of women don't feel represented in media and advertising. The campaign involved creating the world's largest photo library created by women and non-binary individuals to shatter beauty stereotypes. The project aimed to showcase unfiltered beauty and a more inclusive approach to what beauty looks like. With over 1 000 000 uses of the hashtag and 13 000 images in the photo library, this campaign demonstrates how brands can use online forums to create positive changes.



BizFACT

Facebook and Google are set to continue their dominance of the global digital advertising market. Google made over US$134 billion in revenue from digital advertising in 2019 and Facebook made over US$31 billion. Combined, that equates to almost half of the world's total digital ad spend.

Of course, as with traditional advertising, SMA raises concerns including issues of privacy, accuracy, honesty and consumer trust. A number of legal issues are presently evolving, such as establishing age limits for users — Facebook and YouTube specifically prohibit use by children under the age of 13 — and the proliferation of fake and unofficial 'fan pages'.

It is expected that SMA will expand rapidly over the next few years as new, highly interactive mobile platforms and networks increasingly gain consumer acceptance.

KEY IDEAS

- With rapid changes in electronic communication, marketers are beginning to exploit all types of e-marketing.
- E-marketing is the practice of using the internet to perform marketing activities.
- Technology not only provides a faster, more efficient way of doing business, it can also be a very effective way of attracting new customers.
- The main technologies presently available for e-marketing include web pages, podcasts, electronic messages (email and SMS), blogs, location-based marketing and social media advertising.
- A web page is a powerful marketing tool that conveys information in the form of a combination of text, graphics, animation and video.
- Location-based marketing allows businesses to adapt and deliver targeted marketing messages to customers based on where they are located through mobile devices.
- A commercial electronic message is any electronic message (such as email, SMS, MMS or instant message) that offers, advertises or promotes a business, good or service.
- Many businesses set up external blogs, which allow for communication between the business and its existing and potential customers.
- The development of social networking sites has made it easier for individuals and businesses to create and share many different types of content on the web.
- Social media advertising (SMA) is a form of online advertising, using social media platforms such as Facebook, YouTube and Twitter to deliver targeted commercial messages to potential customers.
- SMA enables businesses to constantly build relationships with their customers.

10.9 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.9 Quick quiz on	10.9 Exercise	10.9 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 5, 6, 10	2, 3, 4, 7, 9, 11, 14	8, 12, 13, 15

10.9 Exercise

Revision

1. **Define** the term ‘e-marketing’.
2. As a class, use the brainstorm technique to **propose** reasons why (a) large Australian retailers have been slow to adopt e-marketing and (b) online shopping is very popular with Australian customers.
3. **Explain** how each of the following could be used in e-marketing.
   - **a.** Web pages
   - **b.** Email
   - **c.** SMS
   - **d.** Blogs
   - **e.** Location-based marketing
4. Select one of the five technologies listed in question 3, and **examine** it in more detail using the internet. Prepare a short report (200–300 words) for presentation to the class. Your report should include:
   - origins of the technology
   - changes that have occurred in the availability and use of the technology
   - examples of e-marketing use by at least two businesses.
5. **Define** the term ‘social media advertising (SMA)’.

6. a. **State** the main (i) advantages and (ii) disadvantages of SMA.
   b. Justify which you consider to be the more important: the advantages or disadvantages.
7. **How** does SMA enable businesses to constantly build relationships with their customers?
8. In small groups, use the brainstorm technique to **predict** the future of SMA.
9. **Why** are SMEs encouraged to use e-marketing?

Read the 'Social media advertising — MesCheveux' case study and answer questions 10 to 12.

10. **Outline** the positioning of Mes Cheveux.
11. **Explain** how the salon uses social media.
12. **Assess** the impact social media advertising has had on Mes Cheveux.

Extension

13. It is clear that e-marketing is growing rapidly, and more and more businesses are embracing it. A successful online presence goes beyond simply setting up a website. Imagine you are a business consultant and a number of your clients want assistance with how to operate a successful online business. **Create** a booklet that could be used by a number of different types of businesses, and which includes advice on the following:
    - setting up, maintaining and improving a website
    - promoting the website
    - improving online market share
    - establishing online payment options.
14. **Demonstrate** why it is important to preserve confidentiality of customer information gathered through e-marketing strategies.
15. 'Technology has opened up a whole new channel for marketers to market products to consumers that they don't really need.' **Evaluate** the accuracy of this statement.

10.9 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q2

An entrepreneur uses social media to sell make-up to her friends and acquaintances.

What marketing strategy is the entrepreneur using?

A. E-marketing
B. Personal selling
C. Product differentiation
D. Intensive channel choice

Question 2 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q20

A business firm has improved the security of its online payment system.

Which aspect of social responsibility is this an example of?

A. E-commerce
B. Quality of working life
C. Ecological sustainability
D. Managing cultural diversity

Question 3 (3 marks)

Sonny has recently joined a removals and transport company. He has the computer skills necessary to help the business use e-marketing. Outline e-marketing and describe its advantages to this business.

More exam questions are available in your learnON title.

10.10 Global marketing

SYLLABUS LINK In this subtopic you will learn about global marketing, including global branding, standardisation, customisation, global pricing and competitive positioning.

You will also learn to explain how globalisation has affected marketing management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

A business's marketing plan must be modified and adapted to suit overseas markets. Within each foreign market, the business will be faced with a marketing environment and target markets that differ from the domestic scene. The extended marketing mix needs to be adapted accordingly.

10.10.1 How globalisation has affected marketing management

Many **transnational corporations (TNCs)** adopt a global marketing approach that involves developing marketing strategies as if the entire globe were one large market — a standardised approach. Alternatively, some businesses believe the marketing mix should be customised to take into account differences among countries' cultures, religions and tastes. Despite the process of globalisation, most businesses still view overseas markets as different in some way to domestic markets. This results in a degree of uncertainty and increased risk in developing global marketing strategies.

FIGURE 10.38 Airbnb originally began as a small marketplace for local community members to list properties as accommodation for visitors and guests. By leveraging the right hashtags on social media and investing in a variety of global marketing strategies, Airbnb expanded from a small community in California to over 7 000 000 listings in over 100 000 cities worldwide. Today, Airbnb is available in 26 different languages, allowing it to effectively reach users around the world.



Irrespective of which approach is adopted, all businesses marketing on a global scale need to rely on market research to understand the complexities of the global marketing environment before they can design the marketing mix. It is essential to analyse overseas markets to an even greater depth than is necessary for domestic markets. Many businesses have failed because they entered global markets without first gathering adequate market intelligence.

What should a business know before it decides to engage in global marketing? First, it needs information to make specific marketing decisions, such as the price to charge, the type of packaging necessary, the distribution channel to use and any product characteristics needing modification. Second, information about the country's economic, political, social and cultural features should be gathered.

transnational corporations (TNCs) any businesses that have production facilities in two or more countries and that operate on a worldwide scale

10.10.2 Global branding

We are surrounded by global products all carrying global brand names. **Global branding** is the worldwide use of a name, term, symbol or logo to identify the seller's products.

Businesses are increasingly using global branding for a number of reasons:

- It can be cost effective because one advertisement can be used in a number of locations.
- It provides a uniform worldwide image.
- The successful brand name can be linked to new products being introduced into the market.

A successful brand is one of the most valuable resources a company has. For example, the value of Apple, Sony, McDonald's, Coca-Cola, Mercedes-Benz, Kellogg's and Nike is indisputable. Global branding equates to global recognition, irrespective of the language barrier (see figure 10.39).

Once a business has established its name, it will usually attempt to market the brand globally. Often, businesses will keep their brand name the same across multiple countries. For example, Nike is called Nike across the globe, and Starbucks coffee shops are always called Starbucks. But sometimes brands decide to use different names for each territory they enter. A good example of this is Rexona, an Australian deodorant brand. In the United States, Rexona is known as Degree, in the UK it's called Sure, in Japan and South Korea it's called Rexona, and it's known as Shield in South Africa. But, whatever the name, it always carries the iconic 'tick' logo.

global branding the worldwide use of a name, term, symbol or logo to identify the seller's products

FIGURE 10.39 McDonald's golden arches are the most recognised symbol in the world; in fact they are more recognisable than the Christian cross. A survey of people across multiple countries showed that 88 per cent of people could identify the McDonald's logo as opposed to only 54 per cent who could name the Christian cross.



BizFACT

Apple's iPhone is available in over 100 countries and is the same design regardless of region. Apple does not customise its phones in terms of features and looks; they have a standardised design and the same range of products for all countries (except for the power source and carrier's specifics).

10.10.3 Standardisation

As global marketing increases, businesses are faced with a difficulty: should they use a standardised or customised marketing strategy, or a combination?

A **standardised approach** is a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over. Therefore, the marketing mix will be the same in all markets — a globalisation of the marketing mix. It is a case of 'one marketing plan fits all'. Examples of standardised products are electrical equipment, mobile phones, soft drinks, music, cosmetics, movies and fast foods.

This strategy has obvious cost savings for businesses. Production runs can be longer, thereby achieving economies of scale; research and development costs are reduced; spare parts and after-sales service are simplified; promotion strategies can be standardised; and any evaluation and modification of the plan is a much simpler task.

BizFACT

For businesses to succeed overseas, they must appeal to their international consumer base. Ford found that in Belgium, enticing customers with a dead body in every car wasn't the best way to make a sale. Hoping to highlight the cars' excellent manufacturing, Ford launched an ad campaign that execs thought said, 'Every car has a high-quality body'. However, when translated, the slogan read, 'Every car has a high-quality corpse' — far from the image they were hoping to evoke.

10.10.4 Customisation

In spite of the advantages of a standardised approach, when entering an overseas market, many businesses find it necessary to either modify the existing marketing mix or develop a new one. In doing so, they are adopting a customised approach. A **customised approach** (also called a **local approach**) is a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries.

Adopting this philosophy requires the marketing plan to be customised according to the economic, political and sociocultural characteristics of the target country (see the BizFact about PepsiCo.).

Of course, it is possible for a business to adopt a middle path — that is, a combination of the two approaches. One company to successfully achieve this is McDonald's. Although it has standardised its name, logo, production methods and much of its menu, there are local variations. McDonald's has the McArabia in the Middle East (a flatbread sandwich), macaroons in France, the McSpaghetti in the Philippines, a green chilli cheeseburger in Mexico and bulgogi burgers in South Korea.

standardised approach a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over

customised approach or **local approach** a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries

BizFACT

PepsiCo makes local soft drinks like Shani, a blackberry- and currant-flavoured soda, which is popular in the Middle East during Ramadan, the Muslim holy month.

Over the last decade, as the scale of globalisation has intensified, it has become apparent that the standardisation approach is being used more frequently than the customised approach.

SNAPSHOT

Case study: IKEA — standardised versus customised marketing

IKEA adopts a partially standardised global marketing strategy by selling highly standardised products intended for the global market. While they adopt this approach toward their products, their main promotional tool, the IKEA catalogue, is customised to suit different countries around the world. This is because a kitchen in Australia, for instance, will look very different to a kitchen in Japan or Germany.



IKEA showrooms and catalogues display products by grouping them in actual room settings so that it's easy for customers to re-create what they see in their own home. When designing their catalogues, the furniture company uses a team of ethnographers to travel across the globe to see what life is like in each country. Based on this, IKEA drastically changes the room settings to suit different regions so that their catalogues appeal to the correct audience in each country. They therefore use lots of different layouts to localise the rooms in their brochures. For example, in the Chinese catalogues, the kitchens are a lot smaller. In Saudi Arabia, women and girls have been photoshopped out of many catalogues.

10.10.5 Global pricing

One of the major challenges facing transnational corporations is **global pricing**: how to coordinate their pricing policy across different countries. It is one of the most critical but complex issues that global businesses have to deal with because price is the only element of the marketing mix that generates revenue. All other elements involve costs. Therefore, a business's global pricing strategy is a major determinant of profits. Accurate pricing decisions must be made if the business's overseas expansion is to be successful.

A global business can implement one of three global pricing strategies.

Customised pricing

Customised pricing occurs whenever consumers in different countries are charged different prices for the same product. In determining the price for an overseas market, many global businesses practise the *cost-plus method* to cover the added costs of exportation. Such costs include transportation, taxes, warehousing and **tariffs**. A cost-plus method to pricing products for global markets is usually the most commonly used method because of the added expense associated with exporting.

global pricing how businesses coordinate their pricing policy across different countries

customised pricing occurs whenever consumers in different countries are charged different prices for the same product

tariff a tax on an imported product

Market-customised pricing

This strategy allows for even more flexibility than the customised pricing strategy. **Market-customised pricing** sets prices according to local market conditions. To avoid competition from a domestic business, the global business may need to adopt a market-customised pricing strategy that allows marketers to vary the price depending on the level of demand and competition within the overseas market. In a competitive market, for example, the price charged may have to be lower than in a market where the business has a monopoly.

BizFACT

The exchange rate tells us how much a unit of one currency is worth in terms of another. For example, if A$1 = US$0.70 that means one Australian dollar is worth 70 US cents. Conversely, one US dollar would be worth A$1.43.

Additionally, the price charged in other countries is also influenced by foreign currency exchange rates (see the BizFact above). Fluctuations in the exchange rate can change the prices charged across countries and are a major risk for global businesses.

market-customised pricing
prices that are set according to local market conditions

FIGURE 10.40 Apple, Microsoft and Adobe, who adopt market-customised pricing for their products, have faced strong criticism for charging Australians more for music, movies and TV shows. They defended these higher prices by claiming that every market is different and they have to take into account factors such as freight charges, local sales taxes, levies, import duties and competition as well as the fact that the entertainment industry in Australia charges a higher price for media delivered to Australia.



Standard worldwide price

Standardised pricing is the practice of charging customers the same price for a product anywhere in the world. It will succeed only if the foreign marketing costs remain low enough not to affect overall costs. Two major risks are associated with this strategy:

1. A domestic business may undercut the standardised price.
2. Changes in the exchange rate may negatively impact on the exported price.

10.10.6 Competitive positioning

Competitive positioning relates to how a business will differentiate its products. It centres on how a business will carve out a place in the competitive marketing environment. As in a domestic market, a global business must clearly show how its products are better than the competitors' products. Without differentiation, it takes more time, money and effort to encourage potential customers to purchase a business's products. To differentiate successfully, and avoid competing on price only — a difficult situation to sustain over the long term — the business should strive to develop product leadership, positive customer relationships and operational excellence.

standardised pricing the practice of charging customers the same price for a product anywhere in the world

competitive positioning relates to how a business will differentiate its products

Ultimately, to develop and maintain a competitive position in an increasingly challenging environment, businesses must gain a deep understanding of their dynamic environments in which they operate, and form their strategies according to evolving conditions.

on Resources

Video eLesson Innovation and Smiggle (eles-1053)

Weblink Proctor & Gamble

KEY IDEAS

- A business's marketing plan must be modified and adapted to suit overseas markets.
- All businesses marketing on a global scale need to rely on market research to understand the complexities of the global marketing environment before they can design the marketing mix.
- Global branding is the worldwide use of a name, term, symbol or logo to identify the seller's products.
- A standardised approach is a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over.
- A customised approach is a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries.
- It is possible for a business to adopt a middle path — that is, a combination of the two approaches.
- Global pricing is how businesses coordinate their pricing policy across different countries.
- Customised pricing occurs whenever consumers in different countries are charged different prices for the same product.
- Market-customised pricing sets prices according to local market conditions. This strategy allows for even more flexibility than the customised pricing strategy.
- Standardised pricing is the practice of charging customers the same price for a product anywhere in the world. It will succeed only if the foreign marketing costs remain low enough not to affect overall costs.
- Competitive positioning relates to how a business will differentiate its products. It centres on how a business will carve out a place in the competitive marketing environment.

10.10 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

10.10 Quick quiz on | **10.10 Exercise** | **10.10 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 7, 11	5, 6, 8, 9, 10, 12	13, 14, 15

10.10 Exercise

Revision

1. **Identify** the two approaches a business can take towards its global activities.
2. **Recall** what a business should know before it decides to engage in global marketing.
3. **Define** the term 'global branding'.
4. **State** the three main reasons why businesses use a global branding strategy.
5. **Distinguish** between a standardised and customised global marketing strategy. Provide examples in your answer.
6. **Account** for why McDonald's would use a combination of a standardised and a customised marketing strategy.
7. **Summarise** the three global pricing methods.
8. **Explain** which global pricing method you consider to be the most flexible.
9. **How** does competition in the overseas market affect global pricing?
10. 'Consumers are not standardised globally; therefore, with global brands, you either get lowest common denominator advertising or you get advertising that's right somewhere, but wrong elsewhere.' **Discuss** this statement.

Read the 'Ikea—standardised versus customised marketing' case study and answer questions 11 and 12.

11. **Identify** those aspects of the marketing mix that IKEA standardises and customises.
12. **Why** does IKEA customise its catalogues?

Extension

13. 'Standardisation of production is of greater benefit to the producer than the consumer. It allows transnational conglomerates to treat the world as one single market, irrespective of social and cultural differences.' **Evaluate** the accuracy of this statement. Provide examples to support your answer.
14. Proctor & Gamble (P&G) is a large United States company that provides consumer products of more than 80 brands worldwide. Its main products include cleaning products, detergents, pet supplies, and pharmaceutical and personal care products. Research online and examine its corporate structure. **Determine** the benefits to Proctor & Gamble of adopting global business units (GBUs) and market development organisations (MDOs).
15. A manufacturer of shoes has decided to export to China. The marketing manager assumes that with such a large population a lot of shoes can be sold. **Assess** whether China might be a good or bad market opportunity.

10.10 Exam questions

Question 1 (10 marks)

Source: HSC 2020 Business Studies Exam, Section II, Q22

A popular Australian guitar manufacturer is about to enter the US market using a standardised marketing strategy.

a. Clarify the purpose of a SWOT analysis for this business. **(3 marks)**

b. Recommend a pricing method this business could adopt for the US market. **(3 marks)**

c. Justify this business's decision to adopt a standardised marketing strategy **(4 marks)**

Question 2 (20 marks)

Source: HSC 2018 Business Studies Exam, Section IV, Q27

Explain the influence of globalisation on the interaction of price and quality.

Question 3 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q19

Why might a business adopt a standardised global approach to marketing?

A. To cater for local tastes

B. To minimise risk by hedging

C. To increase market segmentation

D. To take advantage of economies of scale

Question 4 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q11

An Australian business sells its *Bonza Pies* in both Australia and China. *Bonza Pies* sold in China are made to a different recipe.

What is this an example of?

A. Customisation and hedging

B. Global pricing and standardisation

C. Customisation and global branding

D. Global branding and standardisation

Question 5 (2 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q23a

XYZ Ltd produces sports shoes which are worn by elite athletes and the general public in North America. XYZ Ltd is keen to expand into Europe and Asia.

What is ONE possible benefit to XYZ Ltd of using global branding as a marketing strategy?

More exam questions are available in your learnON title.

10.11 Review

10.11.1 Summary

Market segmentation

- The main goal of a marketing manager is to develop and maintain a mix of marketing strategies that matches the needs of customers in the target market.
- Marketing segmentation involves dividing the total market into segments.
- A business selects one of these segments to become the target market.
- The ultimate aim of market segmentation is to increase sales, market share and profits by better understanding and responding to the desires of the different target customers.
- The consumer market can be segmented according to four main variables:
  - demographic — features of a population
  - geographic — urban, regional and rural locations
  - psychographic — personality characteristics
  - behavioural — customers' relationship to the product.

Product and service differentiation and positioning

- Product/service differentiation, in its broadest sense, is the process of developing and promoting differences between the business's products or services and those of its competitors.
- Four important points of differentiation are customer service, environmental concerns, convenience, and social and ethical issues.
- Product positioning refers to the technique in which marketers try to create an image or identity for a product/service compared with the image of competing products/services.

Products — goods and services

- A product is a good or service that can be offered in an exchange for the purpose of satisfying a need or want.
- Most products are combinations of tangible and intangible benefits — the total product concept.
- With mass-produced products, competition is often based on the differences in the intangible benefits.
- A brand is a name, term, symbol, design or any combination of these things that identifies a specific product and distinguishes it from its competition.
- A brand name is that part of the brand that can be spoken.
- Logos can be categorised into five basic types: brandmark logos, wordmark logos, lettermark logos, combination mark logos and emblems.
- To guard against other businesses using its brand name or symbol, a business can apply to have the name registered.
- Manufacturer's or national brands are those owned by a manufacturer.
- A private or house brand is one that is owned by a retailer or wholesaler.
- Generic brands are products with no brand name at all.
- To assist sales, the packaging of a product is sometimes as important as the product itself.
- Marketers can use labels to promote other products or to encourage proper use of products and therefore greater consumer satisfaction with products.

Price

- Price refers to the amount of money a customer is prepared to offer in exchange for a product.
- There are three main pricing methods:
  - Cost-based (mark-up) pricing is a pricing method derived from the cost of producing or purchasing a product and then adding a mark-up.
  - Market-based pricing is a method of setting prices according to the interaction between the levels of supply and demand.

- Competition-based pricing is where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to competitors' prices. A business can select a price that is below, equal to or above those of competitors.
- Once the basic price has been set using the preferred pricing method, the business then fine-tunes this price in line with its pricing strategy.
- The four main pricing strategies include:
  - price skimming, which occurs when a business charges the highest possible price for the product during the introduction stage of its life cycle
  - price penetration, which occurs when a business charges the lowest price possible for a product or service to achieve a large market share
  - loss leader, which is a product sold at or below cost price. Although the business makes a loss on this product, it hopes that the extra customers will buy other products as well.
  - price points (or price lining), which is selling products only at certain predetermined prices.
- Normally, products of superior quality are sold at higher prices.
- Prestige or premium pricing is a pricing strategy where a high price is charged to give the product an aura of quality and status.

Promotion

- Promotion describes the methods used by a business to inform, persuade and remind a target market about its products.
- Promotion mix is the various promotion methods — advertising, personal selling and relationship marketing, sales promotions, and publicity and public relations — a business uses in its promotional campaign.
- Advertising is a paid, non-personal message communicated through a mass medium. The purpose of advertising is to inform, persuade and remind.
- Personal selling involves the activities of a sales representative directed to a customer in an attempt to make a sale.
- Relationship marketing is the development of long-term and cost-effective relationships with individual customers.
- Sales promotion is the use of activities or materials as direct inducements to customers.
- Publicity is any free news story about a business's products.
- Public relations (PR) are those activities aimed at creating and maintaining favourable relations between a business and its customers.
- Marketing managers can use a variety of channels to deliver a message including print and electronic media advertising.
- Often customers may be more willing to purchase a product if the message comes via a respected and trusted channel, such as an opinion leader, or by word of mouth.
- An opinion leader is a person who influences others and whose opinions are respected.
- Word-of-mouth communication occurs when people influence each other during conversations.
- It's important for businesses to use a mix of the promotional strategies in order to meet the different needs of their target market.

Place and distribution

- Place or distribution are activities that make products available to customers when and where they want to purchase them.
- Channels of distribution or marketing channels are the routes taken to get the product from the factory to the customer.
- The four most commonly used channels of distribution are:
  - producer to customer
  - producer to retailer to customer
  - producer to wholesaler to retailer to customer
  - producer to agent to wholesaler to retailer to customer.

- Non-store retailing is retailing activity conducted away from the traditional store, including e-commerce and m-commerce.
- Market coverage refers to the number of outlets a firm chooses for its product.
- A business can decide to cover the market in one of three ways:
  - intensive distribution: when the business wishes to saturate the market with its product
  - selective distribution: using only a moderate proportion of all possible outlets
  - exclusive distribution: only one retail outlet for a product in a large geographic area.
- Physical distribution is all those activities concerned with the efficient movement of the products from the producer to the customer.
- Physical distribution issues include:
  - transport: this refers to the efficient movement of a product from the manufacturer to the customer
  - warehousing: a set of activities involved in receiving, storing and dispatching goods
  - inventory: developing a system that maintains quantities and varieties of products appropriate for the target market.

People, processes and physical evidence

- Three more Ps have been added that apply especially to intangible products (services): people, processes and physical evidence.
- The people element refers to the quality of interaction between the customer and those within the business who will deliver the service.
- Consumers base their perceptions and make judgements about a business based on how the employees treat them.
- Processes refers to the flow of activities that a business will follow in its delivery of a service.
- Without a tangible product, the processes must be highly efficient to achieve customer satisfaction.
- Physical evidence refers to everything that the customer sees when interacting with a business. This could refer to the physical environment experienced by the customer or the materials needed to carry out the service such as signage, business logo or brochures.
- A business should provide high-quality physical evidence to create an image of value and excellence.

E-marketing

- With rapid changes in electronic communication, marketers are beginning to exploit all types of e-marketing.
- E-marketing is the practice of using the internet to perform marketing activities.
- Technology not only provides a faster, more efficient way of doing business, it can also be a very effective way of attracting new customers.
- The main technologies presently available for e-marketing include web pages, podcasts, electronic messages (email and SMS), blogs, location-based marketing and social media advertising.
- A web page is a powerful marketing tool that conveys information in the form of a combination of text, graphics, animation and video.
- Location-based marketing allows businesses to adapt and deliver targeted marketing messages to customers based on where they are located through mobile devices.
- A commercial electronic message is any electronic message (such as email, SMS, MMS or instant message) that offers, advertises or promotes a business, good or service.
- Many businesses set up external blogs, which allow for communication between the business and its existing and potential customers.
- The development of social networking sites has made it easier for individuals and businesses to create and share many different types of content on the web.
- Social media advertising (SMA) is a form of online advertising, using social media platforms such as Facebook, YouTube and Twitter to deliver targeted commercial messages to potential customers.
- SMA enables businesses to constantly build relationships with their customers.

Global marketing

- A business's marketing plan must be modified and adapted to suit overseas markets.
- All businesses marketing on a global scale need to rely on market research to understand the complexities of the global marketing environment before they can design the marketing mix.
- Global branding is the worldwide use of a name, term, symbol or logo to identify the seller's products.
- A standardised approach is a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over.
- A customised approach is a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries.
- It is possible for a business to adopt a middle path — that is, a combination of the two approaches.
- Global pricing is how businesses coordinate their pricing policy across different countries.
- Customised pricing occurs whenever consumers in different countries are charged different prices for the same product.
- Market-customised pricing sets prices according to local market conditions. This strategy allows for even more flexibility than the customised pricing strategy.
- Standardised pricing is the practice of charging customers the same price for a product anywhere in the world. It will succeed only if the foreign marketing costs remain low enough not to affect overall costs.
- Competitive positioning relates to how a business will differentiate its products. It centres on how a business will carve out a place in the competitive marketing environment.

10.11.2 Key terms

advertising media refers to the many forms of communication used to reach an audience
behavioural segmentation the process of dividing the total market according to the customers' relationship to the product
blog an online journal that can be added to by readers
brand a name, term, symbol, design or any combination of these that identifies a specific product and distinguishes it from its competition
brand name that part of the brand that can be spoken
brand symbol or **logo** a graphic representation that identifies a business or product
bundle pricing where customers gain a 'package' of goods and services in addition to the tangible good they purchased
channel any method used for carrying a message
competition-based pricing where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to the competitor's price
competitive positioning relates to how a business will differentiate its products
cost-based pricing a pricing method derived from the cost of producing or purchasing a product and then adding a mark-up
customised approach or **local approach** a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries
customised pricing occurs whenever consumers in different countries are charged different prices for the same product
demand the quantity of a product consumers are willing to purchase at a particular price
demographic segmentation the process of dividing the total market according to particular features of a population, including the size of the population, age, sex, income, cultural background and family size
distribution channels or **marketing channels** the routes taken to get the product from the factory to the customer
e-marketing (electronic marketing) the practice of using the internet to perform marketing activities
ethical consumerism involves buying products that are not harmful to the environment, animals and society
extended marketing mix the combination of people, processes and physical evidence with the four main elements of the marketing mix
Fair Trade movement an alternative method of international trade that promotes environmentalism, fair wages, alleviation of global poverty and a fair price for farmers and workers
frequency the average number of times someone is exposed to the message of an advertisement
generic brands products with no brand name at all

geographic segmentation the process of dividing the total market according to geographic locations
global branding the worldwide use of a name, term, symbol or logo to identify the seller's products
global pricing how businesses coordinate their pricing policy across different countries
inventory control a system that maintains quantities and varieties of products appropriate for the target market
label that part of the package that contains information
labelling the presentation of information on a product or its package
loss leader a product sold at or below cost price
loyalty program a rewards-based program offered by a business to customers who frequently make purchases
manufacturer's brand or **national brand** a brand owned by a manufacturer
mark-up a predetermined amount (usually expressed as a percentage) that a business adds to the cost of a product to determine its basic price
market-based pricing a method of setting prices according to the interaction between the levels of supply and demand — whatever the market is prepared to pay
market-customised pricing prices that are set according to local market conditions
market coverage refers to the number of outlets a firm chooses for its product
market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics
noise any interference or distraction that affects any or all stages in the communication process
non-store retailing retailing activity conducted away from the traditional store
opinion leader a person who influences others
packaging the development of a container and the graphic design for a product
people the people element refers to the quality of interaction between the customer and those within the business who will deliver the service
personal selling the activities of a sales representative directed to a customer in an attempt to make a sale
physical distribution all those activities concerned with the efficient movement of the products from the producer to the customer
physical evidence everything that the customer sees when interacting with a business
place or **distribution** activities that make the products available to customers when and where they want to purchase them
podcasting the distribution of digital audio or video files over the internet
prestige or **premium pricing** a pricing strategy where a high price is charged to give the product an aura of quality and status
price the amount of money a customer is prepared to offer in exchange for a product
price leader a major business in an industry whose pricing decisions heavily influence the pricing decisions of its competitors
price penetration when a business charges the lowest price possible for a product or service so as to achieve a large market share
price points (or **price lining**) selling products only at certain predetermined prices
price skimming when a business charges the highest possible price for the product during the introduction stage of its life cycle
private or **house brand** a brand that is owned by a retailer or wholesaler
processes refers to the flow of activities that a business will follow in its delivery of a service
product/service differentiation the process of developing and promoting differences between the business's products or services and those of its competitors
product/service positioning the technique in which marketers try to create an image or identity for a product compared with the image of competing products
products goods or services that can be offered in an exchange for the purpose of satisfying a need or want
promotion the methods used by a business to inform, persuade and remind a target market about its products
promotion mix the various promotion methods a business uses in its promotional campaign. Methods include:

- advertising
- personal selling and relationship marketing
- sales promotions
- publicity and public relations.

psychographic segmentation the process of dividing the total market according to personality characteristics, motives, opinions, socioeconomic group and lifestyles
public relations (PR) those activities aimed at creating and maintaining favourable relations between a business and its customers

publicity any free news story about a business's products
reach the number of people exposed to the message of an advertisement
relationship marketing the development of long-term and cost-effective relationships with individual customers
sales promotion the use of activities or materials as direct inducements to customers
segmentation variable a characteristic of an individual or group that is used by marketing managers to divide a total market into segments
social media advertising (SMA) a form of online advertising using social media platforms such as Facebook, YouTube and Twitter to deliver targeted commercial messages to potential customers
standardised approach a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over
standardised pricing the practice of charging customers the same price for a product anywhere in the world
supply the quantity of a product businesses are willing to offer for sale at a particular price
tariff a tax on an imported product
total product concept the tangible and intangible benefits (attributes) a product possesses
trademark signifies that the brand name or symbol is registered and the business has exclusive right of use
transnational corporations (TNCs) any businesses that have production facilities in two or more countries and that operate on a worldwide scale
value for money the desire to obtain the best quality, features and performance for a given price of a product
word-of-mouth communication when people influence each other during conversations

Resources

Digital documents	Key terms glossary (doc-35641) Chapter crossword (doc-36217)
Interactivity	Chapter crossword (int-7163)
Exam question booklet	Chapter 10 Exam question booklet (eqb-0032)

10.11 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

Exercise 1: Multiple choice questions

1. In addition to the four elements of the marketing mix, the extended marketing mix also includes which of the following?
   - **A.** People, promotion, processes
   - **B.** People, physical evidence, processes
   - **C.** Product, price, promotion
   - **D.** Promotion, people, physical evidence

2. Which distribution channel would be used by a business that provides a service?
   - **A.** Producer – Consumer
   - **B.** Producer – Retailer – Consumer
   - **C.** Producer – Wholesaler – Consumer
   - **D.** Producer – Wholesaler – Retailer – Consumer

3. A beauty salon developed a new training program to assist staff in using the latest technology. Which marketing strategy is this an example of?
   - **A.** People
   - **B.** Processes
   - **C.** Positioning
   - **D.** Physical evidence

4. Theresa owns a gelato store. In summer when demand for her products is higher, she increases her prices slightly.
Which pricing method does this business use?
A. Cost based
B. Price points
C. Market based
D. Competition based

5. An airline carrier redesigns their logo.
Which marketing strategy has this business modified?
A. Place
B. Price
C. Product
D. Promotion

6. A watch manufacturer sells their products at major department stores.
Which channel choice are they using?
A. Exclusive
B. Expansive
C. Intensive
D. Selective

7. A global furniture manufacturer sells a slightly different product range in each country it operates in.
What is this an example of?
A. Customisation
B. Standardisation
C. Global branding
D. Competitive positioning

8. A business sends an SMS to customers from its database to inform them of a new competition they are running.
Which elements of the promotion mix is this business using?
A. Publicity and personal selling
B. Personal selling and relationship marketing
C. Relationship marketing and sales promotion
D. Sales promotion and publicity

9. A watch manufacturer recently promoted a new image of the business as being superior and better quality than its competitors.
Which marketing strategy is this an example of?
A. Branding
B. Positioning
C. Market segmentation
D. Product/service differentiation

10. Which of the following are both physical distribution issues?
A. Transport and inventory
B. Inventory and physical evidence
C. Physical evidence and warehousing
D. Warehousing and channel choice

Exercise 2: Exam practice questions

Question 1 (4 marks)
Describe how a business would benefit from using opinion leaders in the marketing of their product. Support your answer with a relevant example.

Question 2 (3 marks)
Describe ONE global marketing strategy.

Question 3 (4 marks)
Explain why goods or services are central to both marketing and operations.

Question 4 (4 marks)
Explain the relationship between product/service differentiation and product/service positioning.

Question 5 (4 marks)
RAM Pty Ltd invented and developed a new drug. **Recommend** ONE pricing strategy that this business could use.

Question 6 (6 marks)
Assess why a mix of promotional strategies is important in the marketing of goods and services.

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Teacher-led video Chapter 10 Exam practice solutions (tlvd-1873)

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Topic 2 Marketing review

Marketing: Practice examination

Section I — Multiple choice questions (10 marks)

1. A business has developed a new tablet. Management has set a high price during the introduction stage. Which type of pricing strategy is this business using?
   - **A.** Skimming
   - **B.** Cost-based
   - **C.** Penetration
   - **D.** Market-based
2. A car manufacturer seeks a variety of component parts as inputs from different suppliers in order to produce their final product. This business would belong to which market?
   - **A.** Consumer
   - **B.** Industrial
   - **C.** Niche
   - **D.** Resource
3. A lounge manufacturer sells their products through large department stores. Which channel choice is the manufacturer using?
   - **A.** Competitive
   - **B.** Exclusive
   - **C.** Intensive
   - **D.** Selective
4. Techtronics Limited is a producer of computers and consumer electronics. Updating technology is the main business strategy at Techtronics, with most employees having an engineering orientation. Management spends a great deal of time on design and manufacturing processes rather than on researching customers' needs. Which of the following statements is true?
   - **A.** Techtronics is practising the selling approach.
   - **B.** Techtronics is practising the marketing approach.
   - **C.** Techtronics is practising the production approach.
   - **D.** Techtronics is practising the customer orientation approach.
5. A business has used a competition to try to increase sales for one of their products. Which element of the promotion mix is this an example of?
   - **A.** Advertising
   - **B.** Public relations
   - **C.** Sales promotion
   - **D.** Relationship marketing
6. Which of the following best describes a market niche?
   - **A.** A market niche is a broadly selected target market segment.
   - **B.** A market niche is a narrowly selected target market segment.
   - **C.** A market niche involves a business directing its marketing efforts to an international target market.
   - **D.** A market niche involves a business directing its marketing efforts to two or more target market segments.
7. What are the three new elements that have been added to the extended marketing mix?
   - **A.** Place, processes and physical evidence
   - **B.** Processes, physical evidence and people
   - **C.** Physical evidence, people and product
   - **D.** People, product and processes

8. What does the worldwide use of a name or logo to identify the seller's products refer to?
   - **A.** Customisation
   - **B.** Standardisation
   - **C.** Global branding
   - **D.** Competitive positioning
9. Which of the following is a legal influence on marketing?
   - **A.** Warranties
   - **B.** Truth and accuracy
   - **C.** Engaging in fair competition
   - **D.** Products that may damage health
10. At which stage of the marketing process is a SWOT analysis conducted?
   - **A.** Market research
   - **B.** Situational analysis
   - **C.** Establishing market objectives
   - **D.** Developing marketing strategies

Section II — Short answer questions (46 marks)

1. **a.** **Define** the term 'marketing'. **2 marks**
   b. **Explain** why marketing needs to be an evolutionary process. **4 marks**
   c. 'The marketing concept should be integrated into all key business functions.' **Evaluate** the accuracy of this statement. **6 marks**
2. **a.** **Identify** the stages of the product life cycle. **2 marks**
   b. **Demonstrate** why a business must be able to launch, modify and delete products in response to changes in the product life cycle. **6 marks**
3. **a.** **Outline** how a marketing plan would reflect a business's socially responsible philosophy. **3 marks**
   b. **Discuss** whether a marketing manager should take into account any social consequences of a marketing campaign. **5 marks**
   c. 'Viral marketing is particularly insidious and open to unethical marketing practices.' **Critically evaluate** the accuracy of this statement. Provide examples in your answer. **6 marks**
4. **a.** Briefly **outline** the three Ps of the extended marketing mix. **6 marks**
   b. **Examine** why the extended marketing approach is important in the current business environment. **6 marks**

Section III — Extended response questions

1. Recently, you were elected to serve as promotional organiser for a touch football tournament. The tournament will match several well-known celebrity teams from New South Wales against the best local players. Ticket sales will sell for $30 per person and your objective is to attract a large number of supporters. All proceeds will be given to a local charity. Develop a promotional plan by actioning the following:
   a. **Identify** what market segmentation variables would be most important.
   b. **Recommend** THREE promotional strategies.
2. **Assess** why a mix of promotional strategies is important in the marketing of goods and services.
3. **How** do consumer laws influence a business's marketing strategies?
4. 'Marketing is a system of business activities designed to plan, price, promote and distribute something of value for the benefit of the customer at a profit.' With reference to a business you have studied, **assess** the accuracy of this statement.

Marketing: Practice business report — 20 marks

Your answer will be assessed on how well you:

- demonstrate knowledge and understanding relevant to the question
- apply the hypothetical business situation
- communicate using relevant business terminology and concepts
- present a sustained, logical and cohesive response in the form of a business report.

A business, Roo's Outback Eatery Pty Ltd, is opening an additional restaurant in NSW. They plan to reposition the restaurant as an exclusive venue specialising in modern Australian food with quality customer service. The owners require assistance with the following:
- promoting their business in the new area
- making existing customers aware of their new positioning.

You have been hired as a consultant to write a report for the owners. In your report:

- explain the importance of conducting a situational analysis
- recommend THREE promotional strategies for this business.

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Digital document Sample HSC Business Report (doc-14150)

TOPIC

3 Finance

FOCUS AREA

The focus of this topic is the role of interpreting financial information in the planning and management of a business.

OUTCOMES CHECKLIST

Students should be able to:

- ☐ evaluate management strategies in response to changes in internal and external influences
- ☐ discuss the social and ethical responsibilities of management
- ☐ analyse business functions and processes in large and global businesses
- ☐ explain management strategies and their impact on businesses
- ☐ evaluate the effectiveness of management in the performance of businesses
- ☐ plan and conduct investigations into contemporary business issues
- ☐ organise and evaluate information for actual and hypothetical business situations
- ☐ communicate business information, issues and concepts in appropriate formats
- ☐ apply mathematical concepts appropriately in business situations.

CHAPTER SEQUENCE





SNAPSHOT

Case study: Guzman Y Gomez



As we saw in the Preliminary Course, many small to medium enterprises (SMEs) don't survive, even during good times. So what happens when you throw a once-in-a-lifetime global pandemic into the mix?

The COVID-19 pandemic caused havoc among many industries. Those businesses that survived had to be flexible and adapt to changes in the external environment. It was very difficult for many businesses to achieve their financial objectives during this time. Those businesses that did survive successfully adapted their business operations in response to the changes that were thrown at them during the pandemic.

One such business was Guzman Y Gomez (GYG). Ruben and Natalie Henriques own four GYG franchise stores. The effective financial management strategies the owners implemented from the outset are key to their success and growth. These strategies will be addressed in Chapter 15. The economic outlook, however, obviously had a big impact on this business.

While many restaurants suffered during 2020, Ruben and Natalie considered themselves fortunate to be part of the fast-food industry, which has historically held up very well during recessions. During downturns, many people eat more affordable meals and so they tend to opt for fast food. In the first few months of the COVID-19 pandemic, a couple of the Henriques' restaurants experienced slightly weaker sales due to the shutdowns, while other people in the restaurant business (especially in city centres) saw a 60 to 80 per cent decline in sales.

As customers grew accustomed to working from home and ordering via delivery, GYG saw sales start to increase. They continued to open stores during COVID and offered customers savings through reduced burrito prices, free delivery and introducing new value menu items. These changes led to record sales figures in the months of May, July and September for their restaurants.

online only

11 Kathmandu case study: Finance

This case study provides detailed information on the financial management of outdoor apparel and equipment retailer, Kathmandu, including case study content and exercises.

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Digital documents Kathmandu case study: Finance (doc-35644)
Answers for case study (doc-35645)

Weblink Kathmandu

11 Kathmandu case study: Finance

LEARNING SEQUENCE

11.1 Role of financial management
11.2 Influences on financial management
11.3 Processes of financial management
11.4 Financial management strategies
11.5 Review

11.1 Role of financial management

Kathmandu Holdings Limited (KHL) is a global outdoor, lifestyle and sports company, consisting of three iconic brands: Kathmandu, Rip Curl and Oboz, bringing to market goods with a focus on sustainability. While the Kathmandu brand was born in 1987, Kathmandu Holdings formed in 2009 as a publicly listed company. Together with the acquisition of Oboz (2018) and Rip Curl (2019), Kathmandu Holdings has transformed from a leading Australasian retailer to a brand-led global multi-channel business.

The Kathmandu Holdings Limited (KHL) Chairman and Chief Executive Officer's letter in the 2020 Annual Report states:

'Sales and profit results for Kathmandu in FY20 reflect the global impact of the COVID-19 pandemic. The (company) responded quickly by raising capital to strengthen its balance sheet, reduced costs and adjusted its operating structure. As initial lockdowns and social distancing measures eased, strong sales recovery and cash generation allowed the (company) to end the financial year well placed both financially and operationally.' To this end the company raised $207 million in equity to strengthen its balance sheet and enable future investment, closed stores and stood down staff temporarily and scaled up its online technology to meet surges in customer demand. As the economy opened up, stock levels fell as (some) customers returned to bricks-and-mortar stores.

Company management is confident of its brand positioning to take advantage of increased participation in outdoor activities in a post-COVID-19 world. Risk of a second wave of COVID-19 is always a possibility but financial health is apparent through a strong balance sheet, low debt, healthy inventory and strong cash flow supported by its acquisition of the Oboz and Rip Curl brands to support product diversity.

This assessment of the company's financial position is a reflection of how management sees its period of transformation (through the acquisition of its new brands) and how it also sees its strategic financial future. A rapid response to external shocks such as the global pandemic included suspending dividends and reducing costs. Exploiting online opportunities to meet ongoing demand in an uncertain economic and retail environment will enable it to achieve profitability, growth, efficiency, liquidity and solvency objectives.

on Resources

Sample responses Chapter 11 Exercise questions – sample responses (sar-0191)
Weblink Kathmandu

11.2 Influences on financial management

Most recent data indicates $165 426 000 in retained profits for Kathmandu Holdings Limited (KHL), the newly combined brands of Kathmandu, Rip Curl and Oboz, which is a decrease from $197 120 000 in 2019. These funds can be used at management discretion across the business including retiring external (often interest-bearing) debt.

FIGURE 11.1 In an overall sluggish retail market sector, Kathmandu's recent positive financial performance went against many market expectations.



The company utilises a range of debt options in both the short and long term and this means that interest accrues on any borrowings. In KHL's most recent financial result, record low levels of net debt have reduced financial costs such as those related to interest. This indicates less reliance on borrowed funds to fund its operations.

In terms of equity finance the company lists on both the Australian Securities Exchange (ASX) and the New Zealand Stock Exchange (NZX) (its code is KMD) and is identified by each exchange as a retailer of apparel and equipment for travel and adventure. Further, prospective shareholders are able to purchase shares accordingly. Dividends paid to existing shareholders include franking credits, however, the firm does not have a dividend re-investment plan.

Short-term external funds are available through major Australian and New Zealand financial institutions. This is in the form of unsecured debt and, given the current low interest rates, offers a relatively cheap source of funds should the business wish to borrow, especially as it investigates overseas expansion and upgrading its digital platforms.

KHL is governed by the rules that apply to listed public companies as determined by the Australian Securities and Investments Commission (ASIC). Additionally corporate governance principles recently introduced in Australia and New Zealand led to structural changes within KHL in accordance with the increased ethical expectations of public companies. Australian Taxation Office legislative requirements that apply to corporations such as KHL result in the company having existing taxation liabilities of $13 631 000 down from $23 745 000 in 2019.

The combined effects of the COVID-19 pandemic and the ongoing slow sales recorded in the retail sector continue to pose problems for the industry. Despite this KHL recorded group sales of $801 000 000 which included group online sales of $106 400 000 (an increase of 46 per cent from 2019). Kathmandu recorded an increase in sales of 12.5%. Reduced debt levels and a decline in effective interest rates have reduced finance costs, which is important in a price-driven and heavily competitive retail market.

Note: The KHL annual report uses NZ$ in its financial data. In this case study, all financial figures have been calculated using an exchange rate of A$1 = NZ$1.05

on Resources

Sample responses Chapter 11 Exercise questions – sample responses (sar-0191)

Weblink Kathmandu

11.3 Processes of financial management

The financial needs of the company are addressed via management's analysis of financial reports, which are prepared annually. Record systems must meet accounting requirements as set out in Australia's corporate legislation. With respect to financial risk (for example, the financial loss if a customer fails to meet its contractual obligations), minimal exposure is apparent according to the existing levels of receivables and debtors.

The cash flow statement for the most recent accounting period indicates a surplus of funds ($231 885 000). This cash flow amount comprises receipts from sales, payments to suppliers and employees, purchase of property, plant and equipment, dividends paid and the repayment of outstanding loans. The significant rise in the cash position can be attributed to the equity raising held earlier in the year.

The final cash position has increased with operating cash flow increasing 50.9 per cent to $931 000 000 from the previous year due to an increase in sales, less income taxation and interest paid and also the proceeds from the equity raising. Despite the improved cash position, payment for the cash acquisition of Rip Curl and Oboz and retiring debt absorbed significant reserves.

The income statement indicates a net profit of $8 879 000 (down from $57 633 000). Sales have increased 67 per cent and this is reflected in better net and profit outcomes. Operating expenses have changed little and remained steady at 43 per cent of sales despite an increase in sales.

Expenses such as selling expenses could be expected to rise when sales increase but this did not occur as management sought to control these and other expenses in a difficult trading period.

The balance sheet reflects a $315 000 000 net profit (down 44.5 per cent from the previous year) that, whilst lower than the previous year, includes restructuring costs.

This balance sheet position indicates an increase in total assets to $1 573 432 000 ($594 553 000 the previous year) through higher cash (equity raising contribution $207 000 000), inventories and intangibles (acquisitions). Total liabilities have increased from $152 491 000 to $794 230 000. The net assets position has increased from $442 062 000 to $779 202 000 which would indicate a strong financial position.

11.3.1 Financial ratios and management strategies

The method of preparation of financial statements used by KHL is one that ensures each is easy to understand for stakeholders generally, but particular effort has been made to ensure the data are accessible and useful to shareholders. The intention is to present the information simply so that the financial drivers of the company are easily identifiable.

The financial statements have also been prepared in accordance with generally accepted accounting practice (GAAP), other financial reporting standards and international financial reporting standards (IFRS). The firm Price waterhouse Coopers was the appointed auditor of the financial statements to ensure compliance with accepted accounting conventions.

The company is also required to appoint an audit and risk committee whose responsibility it is to:

- oversee the process of financial reporting, internal control, continuous disclosure, financial and non-financial risk management and compliance and external audit
- monitor Kathmandu's compliance with laws and regulations and its own codes of conduct and ethics
- encourage effective relationships with and communication between the Board, management and Kathmandu's external auditor.

The balance sheet and income statement, shown in figures 11.2 and 11.3, are used to make the liquidity, gearing, profitability and efficiency calculations.

FIGURE 11.2 Kathmandu consolidated statement of comprehensive income for FY 2020

Consolidated Statement of Comprehensive Income

For the Year Ended 31 July 2020

	Section	2020 NZ$'000	2019 NZ$'000
Sales	2.2	801,524	538,855
Cost of sales		(334,493)	(206,362)
Gross profit		467,031	332,493
Other income	2.2	27,369	1,130
Selling expenses	2.2	(169,272)	(160,581)
Administration and general expenses	2.2	(176,237)	(73,477)
		(318,140)	(232,928)
Earnings before interest, tax, depreciation and amortisation		**148,891**	**99,565**
Depreciation and amortisation	3.2–3.4	(103,027)	(15,272)
Earnings before interest and tax		**45,864**	**84,293**
Finance income		449	37
Finance expenses		(23,803)	(2,952)
Finance costs – net	4.1.1	(23,354)	(2,915)
Profit before income tax		**22,510**	**81,378**
Income tax expense	2.3	(13,631)	(23,745)
Profit after income tax		**8,879**	**57,633**
Profit for the period attributable to:			
Shareholders of the company		8,145	57,633
Non-controlling interest		734	–
Other comprehensive income/(expense) that may be recycled through profit or loss:			
Movement in cash flow hedge reserve	4.3.2	(9,259)	620
Movement in foreign currency translation reserve	4.3.2	259	(3,297)
Movement in other reserves	4.3.2	(61)	–
Other comprehensive expense for the year, net of tax		**(9,061)**	**(2,677)**
Total comprehensive income/(expense) for the year		**(182)**	**54,956**
Total comprehensive income/(expense) for the period attributable to:			
Shareholders of the company		(920)	54,956
Non-controlling interest		738	-
Basic earnings per share	2.4	1.7cps	16.0cps
Diluted earnings per share	2.4	1.6cps	15.9cps
Weighted average basic ordinary shares outstanding ('000)	2.4	493,347	359,600
Weighted average diluted ordinary shares outstanding ('000)	2.4	494,582	361,566

FIGURE 11.3 Kathmandu consolidated balance sheet for FY 2020

Consolidated Balance Sheet

As at 31 July 2020

	Section	2020 NZ$'000	2019 NZ$'000
ASSETS			
Current assets			
Cash and cash equivalents	3.1.2	231,885	6,230
Trade and other receivables	3.1.3	73,668	14,206
Inventories	3.1.1	228,793	122,773
Derivative financial instruments	4.2	53	4,964
Current tax asset		3,790	–
Total current assets		**538,189**	**148,173**
Non-current assets			
Trade and other receivables	3.1.3	3,945	–
Property, plant and equipment	3.2	90,722	60,319
Intangible assets	3.3	682,578	386,061
Right-of-use assets	3.4.1	257,998	–
Total non-current assets		**1,035,243**	**446,380**
Total assets		**1,573,432**	**594,553**
LIABILITIES			
Current liabilities			
Trade and other payables	3.1.5	143,698	74,560
Interest bearing liabilities	4.1	–	–
Derivative financial instruments	4.2	7,414	113
Current tax liabilities		8,060	6,458
Current lease liabilities	3.4.2	77,579	–
Total current liabilities		**236,751**	**81,131**
Non-current liabilities			
Derivative financial instruments	4.2	–	9
Non-current trade and other payables	3.1.5	14,413	–
Interest bearing liabilities	4.1	241,270	25,500
Deferred tax	2.3	81,452	45,851
Non-current lease liabilities	3.4.2	220,344	–
Total non-current liabilities		**557,479**	**71,360**
Total liabilities		**794,230**	**152,491**
Net assets		**779,202**	**442,062**
EQUITY			
Contributed equity – ordinary shares	4.3.1	626,380	251,113
Reserves	4.3.2	(16,611)	(6,171)
Retained earnings		165,426	197,120
Non-controlling interest		4,007	–
Total equity		**779,202**	**442,062**

11.3.2 Liquidity

The information for the assessment of the business's ability to meet short-term financial obligations can be assessed by the current ratio. The current ratio for the business in FY 2019 and 2020 was as follows.

- $2019: \frac{\$148\ 173\ 000}{\$81\ 131\ 000} = \$1.82$

  For every $1 of current liabilities the business had $1.82 of current assets.

- $2020: \frac{\$538\ 189\ 000}{\$236\ 751\ 000} = \$2.27$

  For every $1 of current liabilities the business has $2.27 of current assets.

It would appear that the business had higher liquidity in 2020 than 2019. If we assume a preferred figure of $2 of current assets for every $1 of current liabilities, the firm appears to be operating in a satisfactory position in that it is able to meet current financial obligations.

The increase in the liquidity position perhaps reflects the need for controlling inventory levels given the uncertainty of global supply chains. KHL has sought to ensure adequate stock to meet surges in online demand.

Further, cash has increased due to the equity raising, however there has been an increase in trade and other payables. Overall working capital management appears effective through control of current assets and current liabilities in accordance with management goals.

11.3.3 Gearing

The following information has been extracted from the balance sheet and shows the company in a sound position. It is measured using the debt to equity ratio.

- $2019: \frac{152\,491}{442\,062} = 0.34$

  For every $1 of debt there is $1.34 of equity.

- $2020: \frac{794\,230}{779\,202} = 1.01$

  For every $1 of debt there is $1.01 of equity.

There has been a reduction in equity over the period, which would pose some concern for the company. The equity raising strategy certainly strengthened its gearing position (and also provided some much needed liquidity due to the effects of COVID-19). Leasing liabilities are an important aspect of the businesses 'bricks and mortar' retail strategy and this and the increase in interest-bearing liabilities are evident in the increase in non-current liabilities. The growth of trade and other payables and the increase in current lease liabilities are also significant. The company's auditors appear to be satisfied that it will be able to meet these liabilities despite uncertain trading conditions.

11.3.4 Profitability

Gross profit ratio

The following information was extracted from the income statement through the gross profit ratio.

Gross profit ratio has fallen from 61 per cent to 58 per cent (as the cost of sales has increased slightly) and the net profit ratio (after taxation) has fallen significantly from 11 per cent to 1 per cent.

- 2019 : $\frac{332\,493}{538\,855} = 0.61$

  For every $1 of sales there is 61¢ of gross profit.

- 2020 : $\frac{467\,031}{801\,524} = 58\%$

  For every $1 of sales there is 58¢ of gross profit.

The increase in sales is reflected in a higher gross profit, but a higher cost of sales driven by higher sales has meant that the gross profit ratio has not changed significantly. The concerted effort by management to rein in costs including both fixed and variable costs, as well as efforts to minimise expenses such as those related to advertising and in-store labour, is apparent.

Net profit ratio (Net profit before taxation)

The following information was extracted from the income statement through the net profit ratio.

- 2019 : $\frac{57\,633}{538\,855} = 0.1069$

  For every $1 of sales there is 10.69¢ of net profit.

- 2020 : $\frac{8\,879}{801\,524} = 0.0110$

  For every $1 of sales there is 1.1¢ of net profit.

The lower net profit ratio reflects the substantially higher administration and general expenses, depreciation and finance expenses, despite an increase in sales.

11.3.5 Return on equity ratio

The following information was extracted from the balance sheet through the return on equity ratio.

- 2019 : $\frac{57\,633}{594\,553} = 0.0969$

  The business generates 9.69¢ net profit for every $1 invested in the business.

- 2020 : $\frac{8\,879}{1\,573\,432} = 0.0056$

  The business generates 0.56¢ net profit for every $1 invested in the business.

The return on equity ratio had deteriorated quite markedly. The business decided to suspend dividend payments for the current year due to the effects of COVID-19 in a bid to manage its profitability.

Profitability management has been a feature of the company's performance and has been attributed to the growth in sales and management's ability to minimise costs particularly those in relation to human resources through a more efficient use of capital equipment and labour.

11.3.6 Efficiency

Expense ratio

The following information was extracted from the income statement through the expense ratio.

- $2019: \frac{237\,010}{538\,855} = 0.44$

  Expenses account for 44¢ of every dollar of sales.

- $2020: \frac{369\,312}{801\,524} = 0.4607$

  Expenses account for 46¢ of every dollar of sales.

Accounts receivable ratio

The following information was extracted from the income statement and the balance sheet. The accounts receivable ratio for the most recent trading periods is:

- $2019: \frac{538\,855}{14\,206} = 37.93$

  Payment is received every 10 days (365/37.93).

- $2020: \frac{801\,524}{73\,688} = 10.87$

  Payment is received every 34 days (365/10.87).

Efficiency is determined by considering the expense ratio and the accounts receivable turnover ratio.

There is a slight improvement in the management of expenses; however, there appears to be a significant decline in the accounts receivable turnover ratio. The longer duration in receiving payments in the form of receivables is something that the finance manager would be keen to monitor. Going from just under two weeks to nearly a month for settlement of these debts could compromise the company's liquidity position if left unchecked.

The KHL Chairman recognised the challenging business environment in 2020. Some of the challenges were internal and others external.

'This was a transformational year for the business and our team, with the successful acquisition and integration of Rip Curl, the Group's swift and strong response to COVID-19, and the strength of our three brands clearly evident. Sales and profit results for Rip Curl, Kathmandu, and Oboz in FY20 reflect the global impact of the COVID-19 pandemic. The Group responded quickly by raising capital to strengthen its balance sheet, reduced costs and adjusted its operating structure. As initial lockdowns and social distancing measures eased, strong sales recovery and cash generation allowed the Group to end the financial year well placed both financially and operationally.'

The year ahead will no doubt throw up more challenges and the management team will again need to display agility and respond accordingly in order to ensure that KHL continues on its path to long-term and short-term success.

This is not lost on management who see KHL's future in diversity — geographically and via distribution channels, products and seasonality. This will be underpinned by its sustainable and customer-focused approach.

FIGURE 11.4 Kathmandu key performance indicators

KEY PERFORMANCE INDICATORS		2017	2016
Sales	↑ 4.6%	**$445.3m**	**$425.6m**
Same store sales growth		*5.5%*	*4.4%*
Gross profit	↑ 3.7%	**$276.2m**	**$266.4m**
Gross margin		*62.0%*	*62.6%*
Operating expenses	↑ 1.8%	**$205.4m**	**$201.6m**
Operating expenses % of sales		*46.1%*	*47.4%*
Dividend	↑ 18.1%	**13.0cps**	**11.0cps**
Net Debt	↓ (81.3)%	**$6.9m**	**$36.8m**
Share Price	↑ 26.1%	**$2.27**	**$1.80**

Sustainability is apparent in the overall business philosophy — that of a diverse, inclusive workplace with strong community ties both locally and internationally.

As well as the production of authentic, inspirational brands, financial management also has a strong sense of ethical expectations in its approach to delivering net zero environmental harm, ensuring its suppliers meet minimum expectations on social and environmental impacts using recycled materials where possible.

KHL uses PwC chartered accountants to ensure that financial reports are free from misstatement and also to confirm activities conducted by various aspects of the business through the audit process.

This included observing the stocktake process, assessing inventory levels for accuracy, discussing accounting standards including the valuations of intangible assets and all were met with the auditor's approval including acknowledgment of the disruption caused by COVID-19.

The Board and management of the company are committed to adhering to best practice governance principles and maintaining the highest ethical standards.

The company seeks to provide clear, concise financial statements and these reports are verified by the chief executive officer and chief financial officer.

This ethical approach would appear to be endorsed through the independent audit process.

on Resources

Sample responses Chapter 11 Exercise questions – sample responses (sar-0191)

Weblink Kathmandu

11.4 Financial management strategies

In respect to cash flow, management is aware of the need to maintain cash inflow through allowing consumers to purchase online or in store.

Working capital management and the need for liquidity was identified early in the year.

The company appears to have secured its liquidity position with its equity raising decision, the accumulation of inventory so that any production disruptions due to COVID-19 do not prevent it from generating cash through sales (either in store or online) and the decision to prearrange an advance with its financial institution. Immediate liabilities including loans have been retired to further consolidate short term liabilities (net debt $9.4 million). The nature of the business's activities in retail results in reliance on leasing of stores often in expensive shopping centres. The $377 million of liquidity to manage the ongoing uncertainty around the pandemic also provides some economic certainty for KHL.

FIGURE 11.5 Kathmandu operates internationally, which means it is exposed to foreign exchange risk from changes in the value of currencies.



With respect to profitability, the management's ability to control costs has rendered it more capable of dealing with the financial costs of the pandemic. Fixed and variable costs have been managed through decisions to reduce operating expenditure and deferred non-essential capital projects. In addition suspended dividend payments, capital raising, government subsidies and a waiver obtained from its bank syndicate until July 2021 also assist with cost management.

Revenue controls through a strong trading performance, cash generation in key markets, and the earlier than expected re-opening of stores (and subsequent strong cash flow) will assist in meeting (revised) profitability expectations for the next 12 months.

The financial management decisions at KHL in relation to global considerations mean that it enters into forward exchange contracts to manage the risk associated with the purchase of currencies denominated across different exchange rates. The company operates internationally and is exposed to foreign risk arising from changes in the value of currencies such as the Australian dollar, New Zealand dollar and the Great British pound.

Other financial influences such as interest rate swaps are used to exchange a floating rate of interest for a fixed rate of interest. The objective is to minimise the effect of interest rate volatility and in turn the impact upon the company's financial results.

The company is also exposed to changes in interest rates on its borrowings and fluctuations in exchange rates on its foreign currency (mostly United States dollar) purchases and as such uses financial instruments such as derivatives to hedge this exposure.

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Sample responses Chapter 11 Exercise questions – sample responses (sar-0191)

Weblink Kathmandu

11.5 Review

11.5 Activities

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Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 6	2, 5, 7	3, 4

11.5 Exercise

1. **Outline** the performance of Kathmandu with respect to strategic financial objectives.
2. **Compare** the use of internal and external sources of finance.
3. **Analyse** the government and global market influences on financial management at Kathmandu.
4. Use the monitoring and controlling statements — cash flow, income statement and balance sheet — and the results for each to **assess** business performance in respect to liquidity, gearing, profitability and efficiency results from 2016 and 2017. Can you identify strategies for improvement?
5. **Examine** the ethical approach to financial reporting practices.
6. **Outline** the global financial management issues.
7. **Compare** the risks involved in domestic and global financial transactions.

Resources

Sample responses Chapter 11 Exercise questions – sample responses (sar-0191)

Weblink Kathmandu

12 Role of financial management

12.1 Overview

LEARNING SEQUENCE

12.1 Overview
12.2 Strategic role of financial management
12.3 Objectives of financial management
12.4 Interdependence with other key business functions
12.5 Review

12.1.1 Introduction

Finance is often regarded as the lifeblood of a business. It is therefore one of the most important of all business functions. It might be useful to think of the role of finance like that of the heart in the human body. The basic role of the heart is to pump the necessary blood to every part of the body. Similarly, the finance department has to supply the necessary funds to each business function in order for them to effectively carry out their activities.

Financial management is the planning and monitoring of a business's financial resources to enable the business to achieve its financial objectives. Financial management is crucial if a business is to achieve its financial goals. Common financial management objectives include maximising profitability, growth, efficiency, liquidity and solvency. These financial objectives can be either short or long term.

The activities of every aspect of a business have an impact on the company's financial performance and must be evaluated and controlled. This is why it is crucial that financial managers work closely with the other key business functions in order to achieve the business's objectives, as the mismanagement of finance can lead to significant problems.

FIGURE 12.1 Finance is often regarded as the lifeblood of a business. The role of finance can be compared to the role of the heart in the human body. The basic function of the heart is to pump necessary blood to every part of your body. Similarly, the finance department has to supply the necessary funds to each business function in order for them to effectively carry out their activities.



financial management the planning and monitoring of a business's financial resources to enable the business to achieve its financial objectives

on Resources

Digital document Key terms glossary (doc-35646)
Exam question booklet Chapter 12 Exam question booklet (eqb-0034)

12.2 Strategic role of financial management

SYLLABUS LINK In this subtopic you will learn about the strategic role of financial management.

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12.2.1 What does 'strategic role of financial management' mean?

Businesses have specific goals they wish to achieve in relation to investment in capital (machinery and technology), training staff, marketing and the expansion of operations. The strategies that a business adopts work towards achieving its goals both in the short and longer term. **Strategy** refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business. Developing a **strategic plan** as part of a business's financial management will ensure that the business survives and grows in the competitive business world. Strategic plans encompass a long-term view of where the business is going, how it will get there and a monitoring process to keep track of progress along the way.

strategy refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

strategic plan a plan that encompasses the strategies that a business will use to achieve its long-term goals

FIGURE 12.2 Wesfarmers' strategic objective is to deliver satisfactory returns to shareholders through financial discipline and exceptional management of a diversified portfolio of businesses. The Wesfarmers Way is the framework for the company's business model and comprises core values, growth enablers and value-creating strategies directed at achieving the Group's primary objective of providing a satisfactory return to shareholders.



The long-term or strategic role of financial management is to ensure that a business achieves its goals and objectives. This can only be accomplished if the business's finances are managed effectively.

The strategic role of financial management includes:

- setting financial objectives and ensuring the business is able to achieve these goals
- sourcing finance
- preparing budgets and forecasting future finances
- preparing financial statements
- maintaining sufficient cash flow
- distributing funds to other parts of the business.

Strategic planning of **financial resources** is essential to a business's success and growth (see the following case study).

FIGURE 12.3 Money (finance) is needed both to start a business and to keep it operating. According to ASIC, around 44 per cent of small businesses fail due to poor financial management. Proper financial management therefore contributes to success and ensures that objectives and goals are being achieved.



financial resources those resources in a business that have a monetary or money value

SNAPSHOT

Case study: Financial plans



Businesses that put together a realistic financial plan are more likely to gain the finance they need to grow and endure the difficulties that inevitably crop up.

Most business owners will create a business plan that sets out the desired goals and direction of the business. While no two business plans are alike, most will include some common elements such as goals, operational plans, marketing plans and human resource plans. The financial section of the business plan, however, is one of the most fundamental sections of the plan. This is because the other sections of the plan won't mean a thing if they can't be justified with the correct figures.

There are two very important reasons why business owners need a financial plan.

1. They will need to have a financial plan if they intend on seeking finance. Financial institutions, investors or other lenders want to see evidence that the business is likely to grow and make a profit, and that it will be able to make repayments.
2. A financial plan is crucial is to help the owners predict how their business will perform. The financial plan will give them an indication as to whether the business will be viable or whether they are wasting their time and/or money.

What should the financial section of a business plan include? To begin with, the financial plan should include financial projections. For example, it should include a sales forecast, an expenses budget, cash flow projection, income projection, a balance sheet and a break-even analysis. While there is a temptation to be overly optimistic when forecasting in an attempt to attract investors, it is important that the owners be realistic.

Once the financial plan has been created, it is important that owners continuously review and revise their plan and don't forget about it. The owners or financial managers should continuously work out the actual figures and compare them with their projections. They should then use those comparisons to revise their financial plan for the future.

Resources

Weblinks Wesfarmers 2020 Annual Report
Wesfarmers

KEY IDEAS

- Financial management is the planning and monitoring of a business's financial resources in order to allow the business to achieve its financial objectives.
- The long-term or strategic role of financial management is to ensure that a business achieves its goals and objectives.

12.2 Activities

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12.2 Quick quiz | **12.2 Exercise** | **12.2 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 7, 9, 10	3, 5, 8	6

12.2 Exercise

Revision

1. **Define** the term 'financial management'.
2. **Outline** the benefits of developing a strategic plan as part of a business's financial management.
3. **Construct** a concept map summarising the strategic roles of financial management.

Read the opening case study on Guzman Y Gomez in the topic 3 opener and answer questions 4 to 6.

4. **Outline** how Ruben and Natalie have worked towards achieving their financial management objectives.
5. **Explain** the cash flow management strategies Ruben and Natalie have implemented.
6. **How** has the economic outlook influenced this franchise?
7. **Identify** some common elements of a business plan.
8. **Why** is the financial plan the most important element of the business plan?
9. **Outline** what should be included in the financial plan.

Extension

10. Research and **outline** some of the strategies Wesfarmers implemented in 2020 to help them achieve the objectives illustrated in figure 12.2. Use the **Wesfarmers 2020 Annual Report** and **Wesfarmers** weblinks in the Resources tab to help with your research.

12.2 Exam questions

Question 1 (1 mark)

Senior management of a large business comes from their outlets around Australia to discuss the business's financial plans. Which are the most likely financial plans discussed at the meeting?

A. Strategic plans
B. Tactical plans
C. Operational plans
D. Pricing plans

Question 2 (1 mark)

Which of the following statements about the strategic role of financial management is the most correct?

A. Sets short term goals
B. Separates itself from other business activities
C. Follows the lead of other business managers
D. Provides a framework for all other business activities

Question 3 (2 marks)

Describe the strategic role of financial management.

Question 4 (3 marks)

Explain the strategic role of financial management in the success of a business using an example such as Kathmandu.

More exam questions are available in your learnON title.

12.3 Objectives of financial management

SYLLABUS LINK In this subtopic you will learn about the short-term and long-term objectives of financial management including profitability, growth, efficiency, liquidity and solvency.

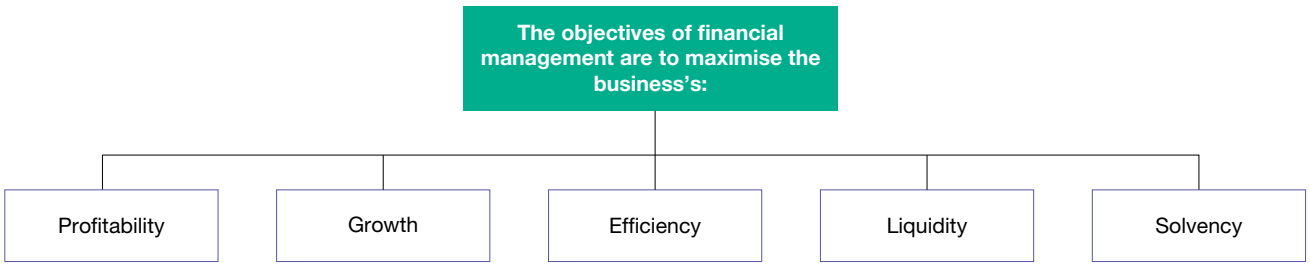
You will also learn to explain potential conflicts between short-term and long-term financial objectives.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA)

Long-term financial goals are determined for a set period of time, generally more than five years, whereas short-term goals are the tactical (one to two years) and operational (day-to-day) plans of a business. For a business to achieve its longer-term goals it must have a number of short-term, specific objectives.
The objectives of financial management are to maximise the business's:

- profitability
- growth
- efficiency
- liquidity
- solvency.

FIGURE 12.4 The business objectives of financial management



The responsibility of financial management is to make decisions about the best way to achieve those objectives. This will involve identifying and evaluating alternative courses of action and making recommendations.

12.3.1 Profitability

Profitability is another important financial objective of management. Profitability is the ability of a business to maximise its profits. Profits satisfy owners or shareholders in the short term but are also important for the longer-term sustainability of a firm.

To ensure that profit is maximised, a business must carefully monitor its revenue and pricing policies, costs and expenses, inventory levels and levels of assets. Profitability will be examined in more detail in chapter 14.

12.3.2 Growth

Growth is the ability of the business to increase its size in the longer term. Growth of a business depends on its ability to develop and use its asset structure to increase sales, profits and market share. Growth is an important financial objective of management as it ensures that the business is sustainable into the future.

FIGURE 12.5 In a bid to overturn their recent decrease in profits, Blackmores set a strategic objective in 2020 of delivering sustainable, profitable growth over the next four years. In order to achieve this growth, the company decided to increase investment in its key China growth market, enter India within a year, boost its presence in Indonesia and launch a series of new supplements for pets.



12.3.3 Efficiency

Efficiency is the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets.

Efficiency generally relates to the operations or revenue-producing activities of the business. Achieving efficiency requires a firm to have control measures in place to monitor assets. A business that aims for efficiency must monitor the levels of inventories and cash and the collection of receivables. Efficiency will be examined in more detail in chapter 14.

profitability the excess of revenue or income over expenses or costs

growth the ability of the business to increase its size in the longer term

efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets

12.3.4 Liquidity

Liquidity is an important financial objective of management. Liquidity is the extent to which a business can meet its financial commitments in the short term (less than 12 months). A business must have sufficient cash flow to meet its financial obligations or be able to convert current assets into cash quickly, for example, by selling inventory.

Controls over the flow of cash into and out of the business ensure that it has supplies of cash when needed. Cash shortfalls and excess or idle cash must be avoided as both involve loss of profitability for a business. Liquidity will be examined in more detail in chapter 14.

12.3.5 Solvency

Solvency is the extent to which the business can meet its financial commitments in shorter term (less than 12 months) and the longer term (more than 12 months). Solvency is particularly important to the owners, shareholders and creditors of a business because it is an indication of the risks to their investment.

Solvency indicates whether a business will be able to repay amounts that have been borrowed for investments in capital (such as equipment and machinery and/or premises). A good indicator to measure solvency is to use **gearing**, which measures the percentage of the assets of the business which are funded by external sources. This way, it measures the business's reliance on outside finance. Solvency (as measured by the level of gearing) is examined in more detail in chapter 14.

12.3.6 Short-term and long-term financial objectives

The financial objectives of a business are based on the goals of its strategic plan, which can be translated into both the short and long term.

- *Short-term financial objectives* are the tactical (one to two years) and operational (day-to-day) plans of a business. These would be reviewed regularly to see if targets are being met and if resources are being used to the best advantage to achieve the objectives. For example, if management has a goal to achieve a 15 per cent increase in profit for the next 10 years, the tactical plans might involve purchasing additional machinery, updating old equipment with new technologies, expanding into new markets and providing new services.
- *Long-term financial objectives* are the strategic plans of a business. They are determined for a set period of time, generally more than five years. They tend to be broad goals such as increasing profit or market share, and each will require a series of short-term goals to assist in its achievement. The business would review their progress annually to determine if changes need to be implemented.

12.3.7 Potential conflicts between short-term and long-term financial objectives

Many business objectives complement each other and meet the needs of a broad range of stakeholders. However, sometimes potential conflicts can arise between short-term and long-term financial objectives. For example, a common financial long-term objective is growth. The decision to expand would have the support of managers, employees, suppliers and the local community. However, expansion is often associated with increased costs and gearing, which will lead to lower overall profits in the short term. This decision may therefore cause conflict with the business owners or shareholders as well as investors. In the longer term, however, most business owners would be pleased to support an expansion if it increases the overall value of the business.

Another example that illustrates the conflict between short-term and long-term financial objectives would be the decision to invest in research and development. Investing in research is very expensive and it might take many years to achieve useful results. Therefore, it is a strategy that is bad in the short term, but in the long run, can make the company lots of money.

liquidity the extent to which a business can meet its financial commitments in the short term (less than 12 months)

solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)

gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.

The conflict between short-term versus long-term results is critical in business. This is because in order to achieve long-term profitability, businesses need to invest in human and physical resources. Many of these resources cost money and will take a long time to pay off, therefore minimising the business's ability to meet its short-term obligations.

Reconciling these conflicting goals is not always easy and short-term thinking by managers may discourage important long-term investment in the business, which could have led to increased profits. Financial managers must constantly assess the achievement of the specific objectives and attempt to satisfy as many goals as possible.

SNAPSHOT

Case study: How Telstra deals with conflicts between short-term and long-term goals

Can you sacrifice temporary pleasure for long-term gain? Take, for example, your health. Would you choose the short-term satisfaction of indulging in chocolates and cake over the long-term effect on your wellness? Have you splurged on something expensive despite this impacting on your long-term ability to save and invest? Just as you will encounter many opportunities for short-term pleasure that may delay or prevent you from achieving your long-term goals, many business managers sacrifice the long-term health of their business to achieve quick results.

According to a 2006 *Financial Analysts Journal* article, 'Value destruction and financial reporting decisions', 'Almost 80 per cent of CFOs (Chief Financial Officers) … admit they would sacrifice economic value for the firm in order to meet that quarter's earnings expectations'. In other words, a majority of CFOs would sacrifice long-term gain for short-term profits.

In contrast to this trend, Telstra chief executive Andy Penn has admitted in the past that he's willing to sacrifice short-term profits to win customers in the long-term by investing in and building superior networks.

Telstra depends heavily on its mobile services division to generate profits to offset declines in other areas such as fixed-line phone calls. Since their dominance in the market has become threatened by competition, Mr Penn believes having a superior mobile network is essential for delivering higher profits in the long-term. He feels that investing in a better mobile network will deliver better profit margins in the future, which will help pay for this investment. Telstra is therefore making short-term sacrifices to grow the business, leading to long-term gains.



KEY IDEAS

- The goals of a business can include increasing market share and profits. These goals are translated into objectives that aim to provide greater details and outcomes. This means they can be measured and evaluated for current and future plans.
- The main objectives of financial management include profitability, growth, efficiency, liquidity and solvency.
- The short-term objectives of a business include both tactical and operational plans, which would be reviewed regularly to determine if targets are being met.
- The long-term objectives of a business include strategic plans and are set for periods of more than five years. They form the basis on which all short-term goals are established.
- While many business objectives complement each other, sometimes potential conflicts can arise between short-term and long-term financial objectives.

12.3 Activities

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12.3 Quick quiz on	12.3 Exercise	12.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4	3, 5, 6	7

12.3 Exercise

Revision

1. **Identify**, with examples, the objectives of financial management.
2. **Outline** the relationship between short-term and long-term financial objectives.
3. **Demonstrate** potential conflicts between short-term and long-term financial objectives.

Read the case study 'How Telstra deals with conflicts between short-term and long-term goals' and answer questions 4 and 5.

4. **Identify** your long-term goals as well as the obstacles that could give you short-term satisfaction but will delay you from achieving those goals.
5. **How** is Telstra dealing with the conflict between their short-term and long-term objectives?

Extension

6. Using an example, such as Kathmandu, **outline** a conflict between a short-term and long-term objective and **recommend** a strategy that management could adopt to reconcile this conflict.
7. Use the internet to **examine** the annual reports of three businesses.
   a. Identify two goals.
   b. Describe the strategies used to achieve these goals.
   c. Propose reasons why some of the goals may not have been achieved in that financial year.

12.3 Exam questions

Question 1 (2 marks)

Source: HSC 2018 Business Studies Exam, Section II, Q24

Why is liquidity an objective of financial management?

Question 2 (1 mark)

Source: Adapted from HSC 2017 Business Studies Exam, Section I, Q4

A business ensures all its debts are paid as they fall due.

Which financial objective is the business satisfying?

A. Efficiency
B. Growth
C. Bankruptcy
D. Solvency

Question 3 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q4

Solvency is the ability of a business to

A. maximise its profits.
B. increase its market share.
C. meet its long-term financial commitments.
D. meet its short-term financial commitments.

Question 4 (3 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q21a

Sue is a sole trader whose business is growing rapidly as sales are increasing. As a result of the growth, she needs to purchase stock worth $10 000.

Explain a potential conflict between a short-term and a long-term financial objective for Sue.

Question 5 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q2

A business is planning to increase its market share by merging with a competitor.

What financial objective does this best illustrate?

A. Growth
B. Liquidity
C. Profitability
D. Solvency

Question 6 (1 mark)

Source: HSC 2009 Business Studies Exam, Section I, Q3

A business uses factoring to pay creditors.

Which financial objective is the business trying to achieve?

A. Efficiency
B. Liquidity
C. Profitability
D. Solvency

More exam questions are available in your learnON title.

12.4 Interdependence with other key business functions

SYLLABUS LINK In this subtopic you will learn about the interdependence of financial management with other key business functions.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The key business functions include:

- operations
- marketing
- finance
- human resources.

Interdependence refers to the mutual dependence that the key functions have on one another. The key functions work best when they overlap and employees work towards common goals. Each function area depends on the support of the others if it is to perform at capacity.

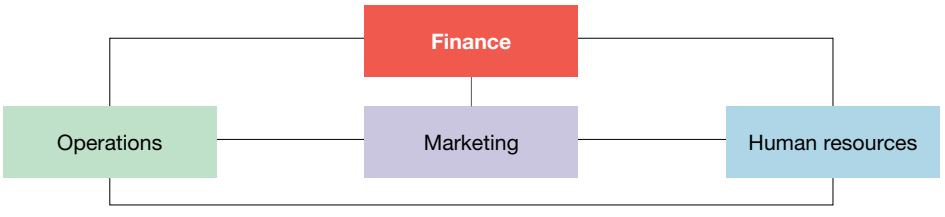
As mentioned at the beginning of this chapter, finance is often regarded as the lifeblood of a business. The finance department has to supply the necessary funds to each aspect of the business in order for them to effectively carry out their activities. The marketing, operations and human resources departments rely on financial managers to allocate them adequate funds, i.e. the operations department requires funds to purchase inputs and carry out their transformation processes, the marketing department requires funds to undertake the various forms of promotion and the human resources department requires funds in order to pay for staff.

In return, the finance department also relies on the other three key business functions. The finance department relies on operations to produce the products, on marketing to promote the products and on human resources to manage staff. Each of these functions helps the business generate sales and therefore provide income to the finance department.

Each business function helps the business generate sales and therefore helps provide income to the finance department. Since the activities of each business function will have an impact on the company's financial performance, they must be evaluated and controlled. This is why it is crucial that financial managers work closely with the other key business functions, in order to achieve the business's objectives.

interdependence the mutual dependence that the key business functions have on one another

FIGURE 12.6 Without finance there would be very little business. Finance (funding) flows to each functional area within a business, which enables it to achieve its goals.



KEY IDEAS

- Interdependence of the key business functions means that each function is not able to operate in isolation successfully — it relies on the others to perform its role in achieving the broader goals of a business.
- The marketing, operations and human resources departments rely on financial managers to allocate them adequate funds.
- The finance department relies on operations to produce the products, on marketing to promote the products and on human resources to manage staff.

12.4 Activities

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12.4 Quick quiz on	12.4 Exercise	12.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1	2, 4, 7	3, 5, 6

12.4 Exercise

Revision

1. **Outline** what is meant by interdependence in business.
2. **Explain** the interdependence of finance and operations in a business. Support your answer with a relevant example. Remember to explain how finance depends on operations and operations depends on finance.
3. **Why** is the financial function critical to the long-term success of a business? In your answer, refer to the interdependent nature of the key business functions.
4. **How** is finance interdependent with marketing?
5. **Justify** why finance is often regarded as the lifeblood of a business.

Extension

6. **Construct** a diagram to illustrate how finance is interdependent with one other key business function.
7. A major business decision, such as launching a new product, requires all four business functions to work with each other. **Describe** how each of the four key business functions would work on the new product launch, i.e. what would their role be?

12.4 Exam questions

Question 1 (1 mark)

Source: HSC 2012 Business Studies Exam, Section II, Q22d

Explain the interdependence of finance and operations in a business. Support your answer with relevant examples.

Question 2 (1 mark)

The management of Soft Soul Shoes has decided to have staff placed on sales commission and incentives as a way to reach monthly budgets. Which two key functions are most involved in this decision?

A. Marketing and finance
B. Finance and operations
C. Human resources and marketing
D. Human resources and finance

More exam questions are available in your learnON title.

12.5 Review

12.5.1 Summary

Strategic role of financial management

- Financial management is the planning and monitoring of a business's financial resources in order to allow the business to achieve its financial objectives.
- The long-term or strategic role of financial management is to ensure that a business achieves its goals and objectives.

Objectives of financial management

- The goals of a business can include increasing market share and profits. These goals are translated into objectives that aim to provide greater details and outcomes. This means they can be measured and evaluated for current and future plans.
- The main objectives of financial management include profitability, growth, efficiency, liquidity and solvency.
- The short-term objectives of a business include both tactical and operational plans, which would be reviewed regularly to determine if targets are being met.
- The long-term objectives of a business include strategic plans and are set for periods of more than five years. They form the basis on which all short-term goals are established.
- While many business objectives complement each other, sometimes potential conflicts can arise between short-term and long-term financial objectives.

Interdependence with other key business functions

- Interdependence of the key business functions means that each function is not able to operate in isolation successfully — it relies on the others to perform its role in achieving the broader goals of a business.
- The marketing, operations and human resources departments rely on financial managers to allocate them adequate funds.
- The finance department relies on operations to produce the products, on marketing to promote the products and on human resources to manage staff.

12.5.2 Key terms

efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets
financial management the planning and monitoring of a business's financial resources to enable the business to achieve its financial objectives
financial resources those resources in a business that have a monetary or money value
gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.
growth the ability of the business to increase its size in the longer term
interdependence the mutual dependence that the key business functions have on one another
liquidity the extent to which a business can meet its financial commitments in the short term (less than 12 months)
profitability the excess of revenue or income over expenses or costs
solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)
strategic plan a plan that encompasses the strategies that a business will use to achieve its long-term goals
strategy refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business

Resources

Digital documents	Key terms glossary (doc-35646) Chapter crossword (doc-36218)
Interactivity	Chapter crossword (int-7165)
Exam question booklet	Chapter 12 Exam question booklet (eqb-0034)

12.5 Activities

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Exercise 1: Multiple choice questions

1. Which of the following is the strategic role of financial management?
   - **A.** To increase market share and expand the product range
   - **B.** Good/service differentiation and cost leadership
   - **C.** To manage the business's finances to ensure that goals and objectives can be achieved
   - **D.** To develop strategies to retain, reward and motivate skilled employees to achieve the business's objectives
2. Effective financial management begins with which of the following?
   - **A.** Market research into the needs and interests of the target market
   - **B.** Setting financial goals and planning
   - **C.** Sourcing finance
   - **D.** Preparing financial statements
3. A business has recently improved their debt to equity ratio from 3.5 : 1 to 2 : 1.
   Which of the following financial objectives has been achieved?
   - **A.** Efficiency
   - **B.** Liquidity
   - **C.** Profitability
   - **D.** Solvency
4. A manufacturer recently implemented a variety of strategies to minimise costs in order to maximise their profits.
   Which of the following financial objectives has been achieved?
   - **A.** Growth
   - **B.** Efficiency
   - **C.** Liquidity
   - **D.** Solvency
5. Which of the following are both objectives of financial management?
   - **A.** Effectiveness and profitability
   - **B.** Profitability and liquidation
   - **C.** Liquidation and solvency
   - **D.** Solvency and growth
6. Which of the following terms best describes a business's ability to meet its short-term debts as they fall due?
   - **A.** Debt
   - **B.** Efficiency
   - **C.** Liquidity
   - **D.** Solvency
7. It is to the benefit of the entire business if each of the business functions work together and support each other to achieve the business's goals. What does this statement reflect?
   - **A.** Capabilities of the key business functions
   - **B.** Strategic roles of the key business functions
   - **C.** Interdependence of the key business functions
   - **D.** Tactical roles of the key business functions

8. Trailblazing Toys produces ride-on toys. It is concerned about projections of a recession over the next few years and its ability to repay a loan on a new warehouse. Which financial management goal does this concern relate to?
   - **A.** Solvency
   - **B.** Profitability
   - **C.** Liquidity
   - **D.** Efficiency

9. What are the short-term objectives that relate to the next one to two years known as?
   - **A.** Tactical plans
   - **B.** Operational plans
   - **C.** Financial plans
   - **D.** Strategic plans

10. Sensational Swimwear has committed to a long-term goal of increasing profits by 15 per cent over 10 years, which can only be achieved through meeting a range of short-term goals, including buying new equipment and hiring more staff. What does this situation reflect?
    - **A.** The challenges a business faces when trying to achieve too many business goals at the same time
    - **B.** The need to prioritise specific business objectives to ensure the interests of all stakeholders are met
    - **C.** A common concern that all businesses face at some point along the life cycle about how to allocate resources to best achieve short-term goals
    - **D.** The conflict that can occur between trying to achieve long-term goals, while experiencing short-term costs in the process

Exercise 2: Exam practice questions

Question 1 (2 marks)

Outline the strategic role of financial management.

Question 2 (3 marks)

Outline ONE potential conflict between a short-term and long-term financial objective.

Question 3 (4 marks)

Distinguish between the objectives of liquidity and profitability.

Question 4 (4 marks)

Explain how finance is interdependent with operations. Use an example to support your answers.

Question 5 (4 marks)

Recommend a strategy a manufacturer could implement to achieve the financial objective of efficiency.

Question 6 (5 marks)

Analyse the relationship between the financial objectives of growth and profitability.

Resources

Teacher-led video Chapter 12 Exam practice solutions (tlvd-1875)

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13 Influences on financial management

13.1 Overview

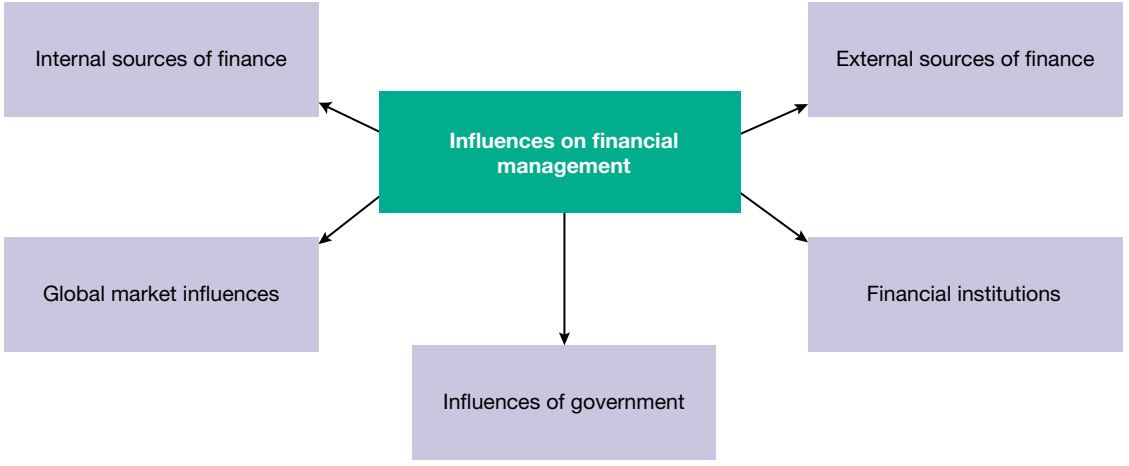
LEARNING SEQUENCE

13.1 Overview
13.2 Sources of finance — internal and external
13.3 Financial institutions
13.4 Influence of government
13.5 Global market influences
13.6 Review

13.1.1 Introduction

The influences on the financial management of a business include a range of external factors such as the domestic government's economic decisions and legislation, and the global economy, which has become a major influence on not just the financial function but all aspects of business operations. Internal factors also have an impact on the financial management of a business and these are more directly controlled and monitored by management through its short- and long-term planning. Figure 13.1 outlines the main influences on the financial management of a business.

FIGURE 13.1 Influences on financial management



on Resources

Digital document Key terms glossary (doc-35648)
Exam question booklet Chapter 13 Exam question booklet (eqb-0035)

13.2 Sources of finance — internal and external

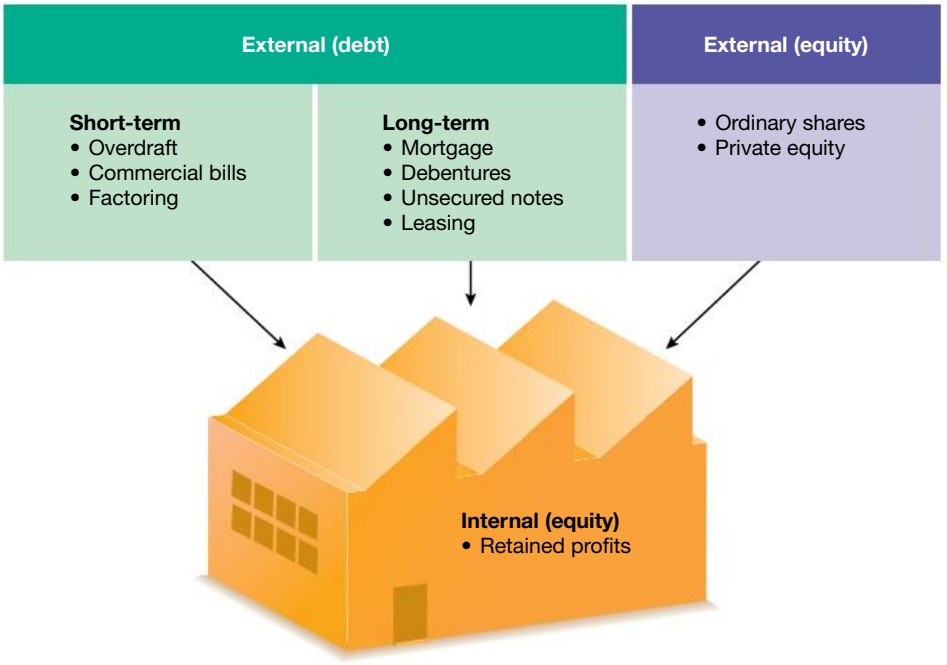
SYLLABUS LINK In this subtopic you will learn about internal and external sources of finance. Internal sources of finance include retained profits, and external sources of finance include debt, short-term and long-term borrowing, and equity including ordinary shares and private equity.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

A business cannot establish itself and thrive without funds to enable it to pursue its activities. The range of activities in which a business is involved during its life cycle includes the initial set-up — whether establishing a new business or buying one that is already established — and might include expanding its range of products, introducing a new product, expanding the number of outlets, upgrading its systems and technology, employing more staff and building a new warehouse.

In the establishment phase of a business, owners and/or shareholders usually contribute funds. In later years, when a business is in the growth stage, a number of options can be considered regarding sources of funds and how those sources will be used. Sources of funds may be internal or external (see figure 13.2). Finding the appropriate source of funds for the business's needs involves **financial decision making**, which means that relevant information must be identified, collected and analysed to determine an appropriate course of action.

FIGURE 13.2 Internal and external source of funds



13.2.1 Internal sources

Internal finance refers to funds generated from inside the business. For example, profits can be retained to finance expansion.

financial decision making requires relevant information to be identified, collected and analysed to determine an appropriate course of action

internal finance funds generated from inside the business; for example, profits can be retained to finance expansion

Retained profits

The most common source of internal finance is retained earnings or profits in which all profits are not distributed, but are kept in the business as a cheap and accessible source of finance for future activities. Most businesses keep some of their profit in

the form of retained earnings. In Australia, the majority of businesses rely on internal sources of funds to finance growth (see the following case study).

SNAPSHOT

Case study: Internal funding preference for SMEs



New research from the Australian Centre for Business Growth found that most Australian SMEs are relying on profits and earnings, rather than external funds, to finance growth and accelerate expansion.

The Centre's longitudinal study revealed that 86 per cent of the CEOs surveyed are relying on internal funds (retained profits) rather than external sources of funds to grow. Less than half (42 per cent) are using bank loans, 34 per cent are accessing government grants and none of the businesses studied were considering crowdfunding or listing on the ASX.

This over-reliance on profits to fund growth can actually be inhibiting the growth of SMEs. While most SMEs surveyed were growing four times faster than the national economy (on average 12 per cent per year), nine out of ten businesses were financing this growth using profits or the owner's assets. While these figures indicate that this reliance on internal funding appears to be working, if these businesses had access to additional capital, they could probably grow even more.

According to the study, there are a few reasons why SME owners and managers are not using external sources of funds. Some are fearful of growth, many are satisfied with their current size and others don't know what to grow. Other managers reported that they were afraid they wouldn't be able to repay the loan and end up in liquidation.

The biggest reason why many SME owners relied on internal sources, however, was because that's how they funded their business in the past and they don't really understand the alternatives.

Years ago, many people thought they had to save up for the full cost of a property before buying it. Today, most people save up for a deposit and borrow the rest from a bank. This has provided more opportunities for people to invest in property. If businesses were also more eager to invest in external funds, they too would be able to experience even greater growth.

13.2.2 External sources

External finance refers to the funds provided by sources outside the business, including banks, other financial institutions, government, suppliers or financial intermediaries. Finance provided from external sources through creditors or lenders is known as **debt finance**.

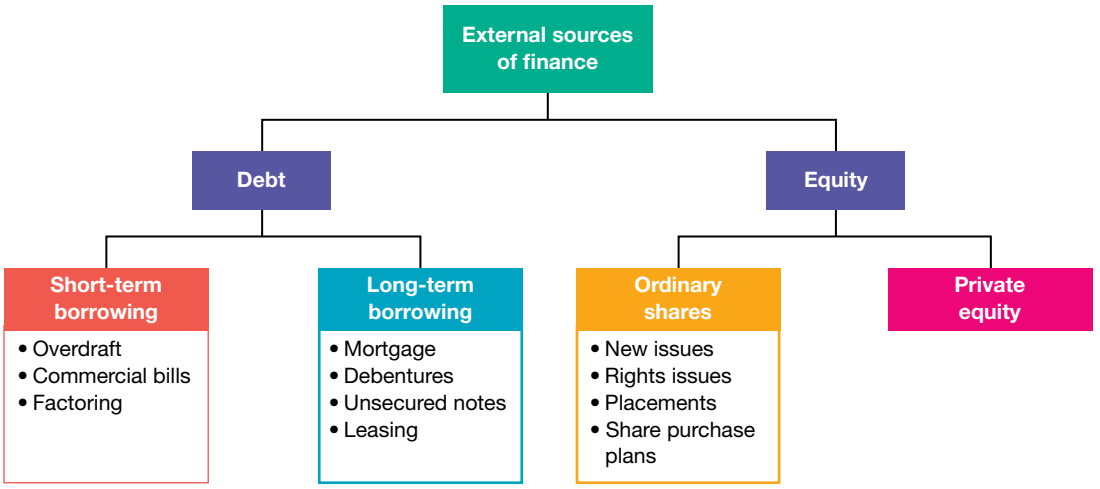
Using debt as a source of finance means that the business relies on outside sources rather than the owners to finance the business. The increased funds for the business should mean increases in earnings and hence profits. Regular repayments on the borrowings must be made so firms have to generate sufficient earnings to make the payments. There is an increase in risk for businesses using debt, as the interest and bank and government charges have to be paid on top of the principal borrowed. However, Australia's tax system has promoted debt financing for businesses by providing tax deductions for interest payments.

external finance funds provided by sources outside the business, including banks, other financial institutions, government, suppliers or financial intermediaries

debt finance relates to the short-term and long-term borrowing from external sources by a business

Types of external debt include short- and long-term borrowing (see figure 13.3). The advantages and disadvantages of debt and equity financing, as well as matching the terms and sources of finance to business purpose, will be examined in more detail in chapter 14.

FIGURE 13.3 External sources of finance — debt and equity



Debt: short-term borrowing

Short-term borrowing is provided by financial institutions through overdrafts, commercial bills and bank loans. This type of borrowing is used to finance temporary shortages in cash flow or finance for working capital. Short-term borrowing generally refers to those funds that will be repaid within 12 months. Short-term debts are recorded as current liabilities on the balance sheet.

Overdraft

An **overdraft** is one of the most common types of short-term borrowing. A bank allows a business or individual to overdraw their account up to an agreed limit and for a specified time, to help overcome a temporary cash shortfall. Overdrafts assist businesses with short-term liquidity problems; for example, a seasonal decrease in sales. Costs for overdrafts are minimal, and interest rates are lower than on other forms of borrowing. As interest rates are usually variable, interest is paid on the daily outstanding balance of the account. Banks usually require the agreed limits to the overdraft to be maintained at a high level and require some security. Overdrafts are repayable on demand, although this is not common.

overdraft when a bank allows a business or individual to overdraw their account up to an agreed limit and for a specified time, to help overcome a temporary cash shortfall

FIGURE 13.4 Overdrafts are the most commonly utilised source of funds for small businesses. According to Statista, 35.4 per cent of small businesses, 46.5 per cent of medium businesses and 48.5 per cent of large businesses in Australia use bank overdrafts.



Many businesses prefer overdrafts to short-term bank loans because bank loans do not have the same flexibility as overdrafts. An overdraft is like a line of credit, which business owners only need to dip into as and when they need it. Businesses that experience a temporary shortfall in funds can be covered immediately with an overdraft, which can give business owners real peace of mind. They are essentially a safety net. The other advantage is that there is no regular repayment schedule; owners can pay the money back when they are able.

Commercial bills

Commercial bills are primarily short-term loans issued by financial institutions, for larger amounts (usually over $100 000) for a period of generally between 30 to 180 days. The borrower receives the sum immediately and promises to repay the money with interest at a future time; that is, the full amount borrowed doesn't have to be repaid until the end of the term.

Commercial bills are flexible both in relation to the interest that needs to be paid and the repayment period. These types of loans are usually secured against the business's assets and are generally rolled over until the borrower has the funds to repay the loan in full.

Factoring

Factoring is a short-term source of borrowing for a business. It enables a business to raise funds immediately by selling accounts receivable at a discount to a firm that specialises in collecting accounts receivable (a finance or factoring business). Factoring is an important source of short-term finance because the business will receive up to 90 per cent of the amount of receivables within 48 hours of submitting its invoices to the factoring company. By having immediate access to funds, the business will improve its cash flow and gearing. The business does not have to worry about the collection of accounts or the costs involved in this process. However, it must be remembered that the full amount will not be received for accounts.

A factoring company may offer its services with or without recourse.

- 'Without recourse' means that the business transfers responsibility for non-collection to the factoring company.
- 'With recourse' means that bad debts will still be the responsibility of the business.

Factoring involves greater risk than other sources of short-term borrowing such as overdrafts and commercial bills because of the likelihood of unpaid debts. It is a relatively expensive source of finance because the business is usually responsible for debts that remain unpaid, and commission is paid on the debt. In the past, factoring was used as a last resort but this attitude has changed in the last decade, and factoring is seen as a legitimate means of financing the activities of a business.

commercial bills primarily short-term loans issued by financial institutions, for larger amounts (usually over $100 000) for a period of generally between 30 and 180 days

factoring the selling of accounts receivable for a discounted price to a finance or factoring company

SNAPSHOT

Case study: OSCAR Natural — factoring and invoice discounting

Small and medium-sized enterprises (SMEs) are increasingly using factoring as a source of finance despite the fact that it costs more than traditional forms of funding. Factoring is particularly appealing to the construction, manufacturing, agriculture and mining, transport and storage, wholesale trade and labour hire markets since they have traditionally extended longer payment cycles to their clients, which ties up funds.

OSCAR Natural is a company that produces natural shaving products. The owner, Oscar de Vreis, used factoring from the outset to fund his business.



'Without factoring, stockists pay your invoice on 60 or 90 days. A factoring firm will advance you between 70 per cent and 85 per cent of the value of the invoice as soon as it's issued so you can keep in sync with your cash flow. The more successful you are, the more you need it because you need the funds to order stock.'

While Oscar admits that factoring is more expensive than an overdraft, he prefers this type of funding because, unlike with some other forms of debt finance, he doesn't need to provide security or give up any equity in the business. There are some drawbacks with factoring, however.



'The biggest headache with factoring is that the admin team at the factoring company reconcile the payments and inevitably they make errors and have occasionally applied payments to the wrong invoices.'

Once Oscar's company became more profitable, he was offered invoice discounting. This is very similar to factoring but it is only offered to more established companies that have a high turnover rate.The main difference between factoring and invoice discounting is that the business, not the lender, collects payments from customers, which means that their customers will not be aware that they have taken on cash flow finance. With invoice discounting, the finance company pays a certain percentage of the invoice amount (generally 80 to 90 per cent of the total) but it's up to the business to collect the payments as normal and then repay the lender (with fees and interest charges). Oscar prefers this method of finance as it enables him to maintain his standards of customer service and keep a direct relationship with his debtors.

Debt: long-term borrowing

Long-term borrowing relates to funds borrowed for periods longer than 12 months. Long-term borrowing is usually used to purchase major assets such as buildings and equipment, and the assets often serve as security on the loan. Despite some risks, long-term borrowing is a common source of financing for businesses.

Long-term debts are recorded as non-current liabilities on the balance sheet.

Mortgage

A **mortgage** is a loan secured by the property of the borrower (business). The property that is mortgaged cannot be sold or used as security for further borrowing until the mortgage is repaid. Mortgage loans are used to finance property purchases, such as new premises, a factory or office. They are repaid with interest, usually through regular repayments, over an agreed period of time.

Debentures

Debentures are issued by a company for a fixed rate of interest and for a fixed period of time. Companies provide them as a way to raise funds from investors, as opposed to financial institutions. A debenture is a promise made by a company to repay money that has been lent to the business. An investor lends money to a company and in return the company issues a debenture with a promise to make regular interest payments for a defined term and then repay the loan at a particular date in the future.

Companies that borrow offer security to the lender usually over the company's assets. On maturity, the company repays the amount of the debenture by buying back the debenture. The amount of profit made by a company has no effect on the rate of interest because debentures carry a fixed rate of interest. Debenture products must have a prospectus. This will tell investors everything they need to know about the company, how they will use the funds and the terms of the investment. Finance companies raise much of their funds through debenture issues to the public.

mortgage a loan secured by the property of the borrower (business)

debenture a promise issued by a company to repay a loan for a fixed rate of interest and for a fixed period of time

BizFACT

Before buying debentures, investors should always get financial advice and read the prospectus. This will tell them how the company will use the money as well as the return being offered. Will it compensate for the risks?

Unsecured notes

An **unsecured note** is a loan from investors for a set period of time. Unsecured notes are not secured against the business's assets and therefore present the most risk to the investors in the note (the lender). For this reason they attract a higher rate of interest than a secured note. Companies sell unsecured notes to generate money for their initiatives, such as share repurchases and acquisitions.

FIGURE 13.5 In 2019, Virgin Australia issued $325 million of five-year unsecured notes with interest of 8 per cent and calls at three and four years. As Australia's response to COVID-19 escalated, Virgin was forced to ground its aircraft and requested financial support from the Australian government. With no commitment from the government, Virgin entered into voluntary administration in April 2020. It is expected that any steps taken to ensure the airline's viability will result in economic loss to those unsecured creditors.



Leasing

Leasing is usually a long-term source of borrowing for businesses. It involves the payment of money for the use of equipment that is owned by another party. A variety of business assets are suitable for leasing, including business cars, plant and machinery, equipment, computers and software.

Leasing enables an enterprise to borrow funds and use the equipment without the large capital outlay required. Costs and benefits of the financial asset are transferred from the lessor to the lessee. The lessee uses the equipment and the lessor owns and leases the equipment for an agreed period of time. A long-term lease cannot usually be cancelled.

unsecured note a loan from investors for a set period of time. Unsecured notes are not secured against the business's assets.

leasing the payment of money for the use of equipment that is owned by another party

FIGURE 13.6 To help mitigate the impact of COVID-19, the federal government introduced a range of measures to support SMEs who have an annual turnover of under $50 million and are signed up to JobKeeper. New regulations regarding commercial leases, as well as a mandatory code of conduct, took effect from 29 May 2020 to 30 September 2020. During this period, landlords were forced to give tenants rent reductions and, if a tenant failed to pay rent or was unable to open, the landlord could not start court or tribunal proceedings.



BizFACT

A motor vehicle leased for two weeks would be leased as an operating lease. The leasing firm would be responsible for repairs to the motor vehicle; and if the vehicle was returned earlier than two weeks, there would be an adjustment to the lease payment.

A motor vehicle leased for three years would be leased as a financial lease. The firm leasing the motor vehicle would be responsible for insurance and maintenance of the vehicle, and the term of the lease would be close to the economic life of the vehicle.

Since the 1960s, leasing as a source of finance has been used widely in Australia. The main participants in lease finance have been finance companies. Businesses choose the equipment, arrange for the finance company to purchase it, then lease it from the finance company, which retains ownership for the period of the lease. There are two types of leases, operating and financial (see the BizFact).

- Operating leases are assets leased for short periods, usually shorter than the life of the asset. The owner carries out the maintenance on the asset. Operating leases can be cancelled, often without penalty.
- Under the conditions of a financial lease, the lessor purchases the asset on behalf of the lessee. Financial leases are usually for the life of the asset. Lease repayments are fixed for the economic life of the asset, usually between three and five years. Plant, vehicles, equipment, furniture and fittings are leased as financial leases. There are usually penalties for cancellation of financial leases. Leasing assets for long periods as financial leases is cheaper than leasing them as operating leases.

Some of the advantages of leasing as a source of finance include:

- It assists a business with their cash flow; this is because the cash outflows or payments related to leasing are spread out over several years, hence saving the burden of a one-off significant cash payment.
- The costs of establishing leases may be lower than other methods of financing.

- If some assets are leased a business may be in a better position to borrow funds.
- It provides long-term financing without reducing control of ownership.
- It permits 100 per cent financing of assets.
- Repayments of the lease are fixed for a period so cash flow can be monitored easily.
- Lease payments are a tax deduction.
- Payment usually includes maintenance, insurance and finance costs.

However, a disadvantage of leasing is that interest charges may be higher than for other forms of borrowing.

Corporations are required by law to reveal significant leases in their published financial statements or in notes to the financial statements.

Equity

In the Preliminary course, we learnt that equity finance refers to funds contributed by the business owners; for example, capital or reinvesting net profit back into the business. **Equity** as an *external* source of funds refers to the finance raised by a company through inviting *new* owners. For example, this can be done by issuing shares to the public through the Australian Securities Exchange (ASX). This is used as an alternative to debt funding. Equity as a source of external finance includes:

- ordinary shares (new issue, rights issue, placements, share purchase plan)
- private equity.

equity as an external source of funds, refers to the finance raised by a company through inviting new owners

FIGURE 13.7 In 2017, the Australian government amended the Corporations Act 2001 allowing companies to access crowd-sourced equity funding (CSEF) (refer to BizFACT). The government introduced these changes to make it easier and less expensive for small businesses to raise equity and to remedy the shortage of finance options available for SMEs and start-ups.



BizFACT

Crowd-sourced equity funding (CSEF) is an innovative type of fundraising that allows a large number of individuals to make small financial investments (up to $10 000) in exchange for an equity stake in the company. CSEF is similar to other forms of crowdfunding in that it enables companies to raise funds through an online portal. The difference is that investors receive a share of the company rather than a product or service. Eligible companies will be able to raise up to $5 million a year this way.

Ordinary shares

Ordinary shares are the most commonly traded shares in Australia. The purchase of ordinary shares by individuals means they have become part-owners of a publicly listed company. This means they get voting rights according to the number of shares that they have as well as payments called **dividends**. When shareholders purchase shares in a company, they are providing a source of finance (equity) for that business. The value of the share is determined by a company's current or future performance.

dividend a distribution of a company's profits (either yearly or half-yearly) to shareholders, calculated as a number of cents per share

The following terms refer to variations in the type or issue of ordinary shares.

TABLE 13.1 The different types of ordinary shares commonly traded in Australia

New issue	A new issue refers to a security that has been issued and sold for the first time on a public market, e.g. the Australian Securities Exchange. Initial public offerings (IPOs) are the most common new issues. An IPO, or 'float', is when a private company lists on a stock exchange for the first time to raise funds by selling shares to the public. In order to raise funds via an IPO, the company must first prepare a prospectus and lodge it with the Australian Securities and Investments Commission (ASIC). The prospectus must contain all the relevant information potential investors would require to make an informed judgement regarding investment in the company. Companies use IPOs to raise money that can then be used to help grow the business. IPOs give investors the chance to buy shares at a set price before the company begins trading on the ASX in the hope that those shares will rise over time. Most new issues come from privately held companies that become public and present investors with new opportunities (see the following case study)
Rights issue	A rights issue is an invitation to existing shareholders to purchase additional new shares in the same company. This type of issue gives existing shareholders securities called rights. With the rights, the shareholder can purchase new shares at a discount to the market price on a set future date. Until the set date at which the new shares can be purchased, shareholders may trade the rights on the market in the same way that they are able to trade ordinary shares. Rights are considered to be a type of option since it gives shareholders the right, but not the obligation, to purchase additional shares in the company. Usually the current shareholders will have the right to purchase new shares in proportion to the number of shares they currently own. The shareholder does not have to take up the rights issue. Companies most commonly issue a rights offering to raise additional funds or to pay down debt, especially if they are unable to borrow more money. Let's look at an example. Imagine that you owned 2000 shares worth $4 each in XYZ Pty Ltd. The company needs to raise funds to pay off some of their outstanding debts. They therefore announce a rights offering in an attempt to raise $10 million by issuing 20 million shares to existing shareholders at $2 each. But this issue is a three-for-ten issue. In other words, for every 10 shares you have, the company is offering you another three at a discounted price of $2. This is 50 per cent less than the $4 price at which the shares are currently trading.

(continued)

TABLE 13.1 The different types of ordinary shares commonly traded in Australia *(continued)*

Placements	Another way a company can raise additional funds is to do a 'share placement'. A placement involves creating new shares in return for capital and issuing them to selected investors at a discount to the market price of the company's shares. In other words, additional shares are offered at a discount to their current trading price to special institutions or investors who are able to invest a large sum of money. This discount is intended to persuade specific investors to invest in the company. Placements are typically issued without a full disclosure document, and therefore participation is limited to institutional investors or investors who qualify under s708 of the *Corporations Act 2001* (Cth). Placements can sometimes disadvantage existing shareholders by diluting or reducing their interests in the company's earnings. For example, imagine you own 1000 out of 20 000 issued shares in a particular company. In other words, you own 5 per cent of the company and are theoretically entitled to 5 per cent of its earnings. Now imagine that the company decided to raise funds through a placement of 2000 shares at the current market price to a major investor. Your holding has now been diluted to 4.5 per cent!
Share purchase plans	Share purchase plans refer to an offer to existing shareholders in a listed company to purchase newly issued shares in that company without brokerage fees. The shares are usually offered at a discount to the current market price. Share purchase plans allow companies to issue new shares to current shareholders without issuing a prospectus. They can only issue a maximum of $30 000 in new shares to each shareholder.

SNAPSHOT

Case study: Forbidden Foods launch on the ASX

Forbidden Foods is an Australian health food manufacturer that caters to health-conscious consumers by offering premium products under the Forbidden, Sensory Mill and Funch brand names. Ten years after they began, the business raised $6 million in an IPO.



In 2010, university friends Jarrod Milani and Marcus Brown founded Forbidden Foods with the aim to take on the Australian rice market armed with a single product — a 500-gram bag of black rice. Aged 20 and 21 at the time, the owners struggled to get finance from banks for the business and had to finance the business launch using their credit cards. From that beginning, Forbidden Foods has now expanded to supplying over 3500 retailers as well as exporting to multiple international markets including New Zealand, Ireland, the US and Singapore.

In 2020, the owners decided to pursue equity financing in order to access funds to enable the business to expand. They wanted to exploit opportunities in the external environment which included: increased demand for healthy, organic and natural foods, an increase in disposable incomes and a greater focus on environmental sustainability. Forbidden Foods needed $7 million to $10 million to execute their growth plans over the next five to seven years. The owners therefore decided to issue shares to the public for the first time to help them raise this capital so they could expand their market reach and increase brand awareness. Their plan was to use the funds to launch new innovative product lines, to deepen their market penetration and broaden their international focus.

Forbidden Foods offered 30 million shares at an issue price of $0.20 per share (raising $6 million). The offer closed on 14 August and they commenced trading on the ASX on 1 September. Investors clearly liked what

Forbidden Foods was offering, and the stock price doubled in less than 20 minutes of it being launched. The new shareholders will hold 40 per cent of the shares while the previous stakeholders will retain 60 per cent of the shares once the offer concludes.

Private equity

Private equity is the money invested in a (private) company not listed on the Australian Securities Exchange (ASX). The aim of the private company (like the publicly listed companies who sell ordinary shares) is to raise capital to finance future expansion/investment of the business.

on Resources

Weblinks Austrade
Australian Investment Council

KEY IDEAS

- Internal finance refers to funds that are generated from inside the business. For example, profits can be retained to finance expansion.
- External finance is the funds provided by sources outside the business, such as financial institutions, governments and suppliers.
- External sources of finance are broadly categorised as either debt or equity — each will influence the financial management decision of a business.
- Debt finance can be short-term borrowings such as overdrafts, commercial bills and factoring; or long-term borrowings such as mortgages, debentures, unsecured notes and leasing.
- Equity refers to the cash raised by a company through:
  - issuing ordinary shares to the public for purchase through the ASX
  - private shares (equity) in companies not listed on the ASX.
- Different types of ordinary shares include:
  - new issue
  - rights issue
  - placements
  - share purchase plan.

13.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

13.2 Quick quiz on	13.2 Exercise	13.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 6, 8, 12, 17, 20, 22	3, 4, 5, 7, 9, 10, 11, 13, 14, 15, 16, 18, 19, 21, 23, 25	24, 26

13.2 Exercise

Revision

1. **Outline** the difference between internal sources and external sources of finance.
2. **Define** the term ‘retained profits’.

3. **Explain** why equity finance can be the most difficult type of finance to obtain.
4. **Why** do you think most businesses keep approximately half of their profit in the form of retained earnings?
5. Thomas, who owns a hairdressing business, prefers to use retained earnings to expand his business rather than taking on a new partner. **Interpret** the reasons for this.
6. **Identify** the main sources of external finance.
7. **Discuss** the use of an overdraft to meet short-term financial commitments.
8. **Clarify** the main features of commercial bills.
9. Identify and **explain** the sources of finance from the following balance sheet.

Current Assets		
Cash	$33 000	
Receivables	12 000	
Inventories	4 700	$49 700
Non-current Assets		
Land and buildings	98 000	
Plant and equipment	18 000	116 000
Total Assets		165 700
Current Liabilities		
Creditors	8 700	
Non-current Liabilities		
Borrowings	12 000	20 700
Net Assets		145 000
Owners' Equity		
Capital	140 000	
Profits	5 000	145 000

10. **a.** Define the term 'factoring'.
    b. Why has factoring become an important source of finance for business?
    c. Discuss factoring.
11. **Distinguish** between a debenture and an unsecured note.
12. **Define** the term 'leasing'.
13. 'Leasing is a cheap, flexible and important source of finance for businesses'. **Discuss** this statement, **outlining** the uses, advantages and disadvantages of leasing.
14. BJs Supermarket is considering whether to purchase or lease a new supermarket. The lease requires that BJs pays for maintenance, insurance and rates if the store is leased. The annual lease payment is $100 000 (payable in advance) for four years. The purchase price of the supermarket is $350 000 and funds would need to be borrowed if the store was purchased. **Construct** a report for BJs supermarket on the best alternative for the business, **outlining** the advantages and disadvantages of both leasing and purchasing the supermarket.
15. Leo has purchased a number of computers and new software for his photographic equipment business in anticipation of increasing sales on the internet. This has not occurred and Leo is having difficulties paying bills on time. **Recommend** to Leo the best sources of finance for the business to overcome the problems. **Justify** your answers.
16. **Construct** a concept map summarising the variations in the type or issue of ordinary shares.

Read the 'Internal funding preference for SMEs' case study and answer questions 17 and 18.

17. **Outline** reasons why SME owners are not using external sources of funds.
18. **Explain** why this reliance on internal funds is limiting the growth of SMEs.

Read the 'OSCAR Natural — factoring and invoice discounting' case study and answer questions 19 to 21.

19. **Discuss** factoring.
20. **Describe** invoice discounting.
21. **Explain** why Oscar prefers invoice discounting over factoring.

Read the 'Forbidden Foods launch on the ASX' case study and answer questions 22 to 24.

22. **Identify** the source of funds the owners used to begin their business.
23. **Why** did the owners decide to use equity?
24. **Assess** the use of equity financing for Forbidden Foods.

Extension

25. **Examine** the sources of funds provided by Austrade and the Australian Investment Council that are available to businesses. Use the weblinks in your Resources tab to help with your research.
26. **Analyse** a range of annual reports of businesses to determine their sources and applications of funds. Construct a table to summarise your findings.

13.2 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q12

Which of the following allows shareholders of a public company to acquire additional shares at a discount?

A. New issues
B. Placements
C. Private equity
D. Unsecured notes

Question 2 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q2

A business is purchasing a new property.

Which source of finance would be the most appropriate?

A. Shares
B. Mortgage
C. Debenture
D. Letter of credit

Question 3 (5 marks)

Source: HSC 2018 Business Studies Exam, Section II, Q24

A business has decided to expand into a larger factory and is now considering its financial options.

Discuss the use of leasing and the use of mortgages as a source of long-term finance for this business.

Question 4 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q6

A sole trader invests $500 000 into her business.

What is this an example of?

A. An overdraft
B. Retained profits
C. Internal debt finance
D. Internal equity finance

Question 5 (6 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q21b

Sue is a sole trader whose business is growing rapidly as sales are increasing. As a result of the growth, she needs to purchase stock worth $10 000.

Discuss ONE internal and ONE external source of finance for Sue's purchase of stock.

Question 6 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q6

What is a source of new capital for a public company?

A. Primary market of the Australian Securities Exchange
B. Secondary market of the Australian Securities Exchange
C. Primary market of the Australian Securities and Investment Commission
D. Secondary market of the Australian Securities and Investment Commission

More exam questions are available in your learnON title.

13.3 Financial institutions

SYLLABUS LINK In this subtopic you will learn about financial institutions, including banks, investment banks, finance companies, superannuation funds, life insurance companies, unit trusts and the Australian Securities Exchange.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Financial institutions collect funds and invest them in financial assets. They provide financial services and focus on dealing with financial transactions such as investments, loans and deposits. While most businesses acquire funds from a bank, finance is also available from a variety of other institutions, such as investment banks, finance companies, superannuation funds, life insurance companies, unit trusts and the Australian Securities Exchange.

13.3.1 Banks

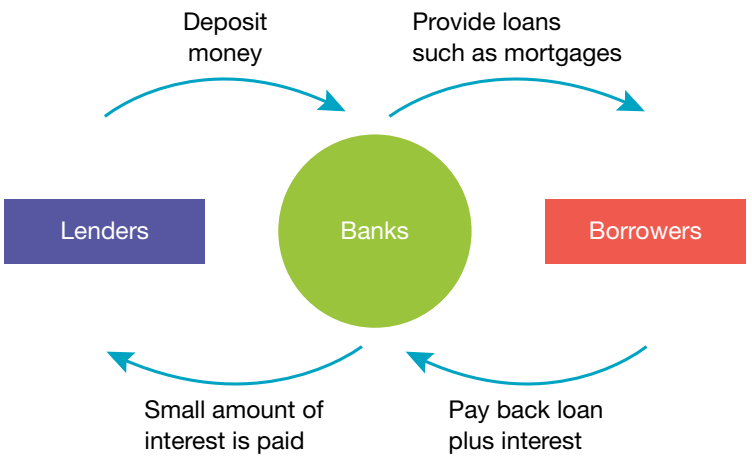
Banks are the major operators in financial markets and are the most important source of funds for businesses. Banks offer a wide range of financial products and services; for example, offering credit cards, cheques, overdrafts, insurance, investment and savings accounts, and lending money through personal and business loans and mortgages. Banks also provide other typical banking services such as internet banking, automatic teller machines (ATMs) and financial advice. Apart from traditional banking services, banks also provide business banking, trading in financial markets, stockbroking, insurance and funds management.

Banks receive savings as deposits from individuals, businesses and governments, and, in turn, make investments and loans to borrowers. A bank is a business that wants to make a profit, so it accepts money as savings (deposits) at a lower interest rate and lends that money at a higher interest rate. The difference between these two rates of interest is one of the ways a bank makes a profit.

BizFACT

There are currently 53 banks operating in Australia. The four largest banks are ANZ Banking Group, Commonwealth Bank of Australia, National Australia Bank and Westpac Banking Corporation.

FIGURE 13.8 Banks act as intermediaries between lenders and borrowers



13.3.2 Investment banks

Investment banks provide services in both borrowing and lending, primarily to the business sector, for example, Macquarie Bank. They provide a wide variety of different types of loans for businesses and can therefore customise loans to suit the business's specific needs. Investment banks sometimes impose conditions when providing loans. For example, they may require some equity in the business borrowing the funds. Investment banks:

- trade in money, securities and financial futures
- arrange long-term finance for company expansion
- provide working capital
- arrange project finance
- advise clients on foreign exchange cover
- advise on mergers and takeovers
- provide portfolio investment management services
- underwrite corporate and semi-government issues of securities
- operate unit trusts including cash management trusts, property trusts and equity trusts
- arrange overseas finance.

13.3.3 Finance companies

Finance companies are non-bank financial intermediaries that specialise in smaller commercial finance. They provide mainly short-term and medium-term loans to businesses through consumer hire-purchase loans, personal loans and secured loans. They are also the major providers of lease finance to businesses. Some finance companies specialise in factoring or cash flow financing.

Finance companies raise money through share issues (debentures). Debentures are for a fixed term and carry a fixed rate of interest. Lenders have the security of priority over the firm's assets in the event of liquidation. In other words, the finance company is entitled to sell the assets of the business to recover the initial loan if the business fails. Finance companies can provide businesses with quick access to funds, although the interest rate will usually be higher.

BizFACT

There are currently 144 registered finance companies in Australia.

13.3.4 Life insurance companies

Life insurance companies are also non-bank financial intermediaries who provide cover and a lump sum payment in the event of death. Policy holders pay regular premiums and the insurer guarantees to pay the designated beneficiary a sum of money upon death of the insured person or under other circumstances specified in the contract.

Life insurance companies provide both equity and loans to the corporate sector through receipts of insurance premiums, which provide funds for investment. The funds received in premiums, called reserves, are invested in financial assets.

FIGURE 13.9 While COVID-19 saw a reduction in health insurance and car accident claims, there has been a surge in life insurance claims related to income protection and total permanent disability as chronic mental conditions such as depression increase in the community. Data from a Financial Services Council-led report showed a rising trend in mental health claims, with life insurers paying out $750 million in mental health claims to almost 7000 Australians in 2019. There has been a 53 per cent rise in mental health-related disability income payouts in the last five years.



13.3.5 Superannuation funds

Superannuation funds have grown rapidly in Australia over the past 25 years due to tax incentives and compulsory superannuation, which was introduced by the government in 1992. **Superannuation** is a scheme set up by the federal government, which requires all employers to make a financial contribution to a fund that will provide benefits to an employee when they retire.

Employers are required by the government to make superannuation contributions for all employees aged between 18 and 69 who are paid more than $450 before tax in a calendar month. They are also obligated to make contributions for people under 18 who work more than 30 hours a week (and still earn more than $450 in the calendar month). Employers must pay an amount equal to 9.5 per cent of their employee's salary into a super fund account. This is on top of the employee's salary or wages. Over the course of their working life, these contributions add up.

Superannuation funds invest the money received from superannuation contributions in many things, such as company shares, property and managed funds. They do this so that their members will earn investment returns on the money.

superannuation a scheme set up by the federal government, which requires all employers to make a financial contribution to a fund that will provide benefits to an employee when they retire

FIGURE 13.10 The Australian Prudential Regulation Authority (APRA) is the prudential regulator of the Australian financial services industry. It oversees banks, credit unions, building societies, general insurance and reinsurance companies, life insurance, friendly societies and most members of the superannuation industry. APRA is funded largely by the industries that it supervises.



SNAPSHOT

Case study: Future plans for the superannuation guarantee

For nearly 30 years, Australian governments have been working to get the percentage of your wage that employers must contribute to your retirement savings to 12 per cent.

But with the Government gearing up for the final stretch of increases, the plan is at risk of coming off the rails.

The superannuation guarantee is the minimum amount of your earnings that your boss, or you if you're self-employed, has to set aside for when you retire.

It means workers have forced savings to help them pay for those later years when they do not have an income, and it takes pressure off the age pension, which the Government pays to help retirees who don't have other savings to fall back on.



The age pension and other income support schemes for seniors are forecast to cost the federal budget more than $50 billion this financial year. They are the most expensive welfare measures on the federal books. And an increasing life expectancy means the cost is likely to grow quickly over the coming decade.

At the moment the superannuation guarantee is 9.5 per cent of a person's wage. But it's legislated to rise to 10 per cent next July, with follow-up staggered increases to 12 per cent by 2025. (It was legislated to increase to 10 per cent on 1 July 2021, but this is still yet to be officially confirmed by the Federal Government.)

Here's what that looks like:

Period	General super guarantee (per cent)
July 1, 2002 – June 30, 2013	9
July 1, 2013 – June 30, 2014	9.25
July 1, 2014 – June 30, 2021	9.5
July 1, 2021 – June 30, 2022	10
July 1, 2022 – June 30, 2023	10.5
July 1, 2023 – June 30, 2024	11
July 1, 2024 – June 30, 2025	11.5
July 1, 2025 – June 30, 2026	12

Scott Morrison has committed to this plan

Paul Keating's government made the superannuation guarantee a law back in 1992. At the time, it was just 3 per cent of income, with baked-in increases that would take it to 12 per cent by 2001.

When the Coalition came to power, the Howard government intervened and froze the rate, until Labor returned to government and passed a 2011 law to increase it to 12 per cent by last financial year.

But with another change of government, so too came a freeze on increases, this time in 2014 under Tony Abbott's prime ministership.

The Coalition pushed out the timeframe to achieve the 12 per cent share to 2025, which Prime Minister Scott Morrison took to last year's federal election

Why are some people opposed to increasing the super guarantee?

Within the Coalition, there has long been a group of people who are vocally opposed to further increases to superannuation.

Some government politicians have little faith in the entire superannuation system, which they argue is unfairly stripping wage earners of immediate access to their own money.

This group argues it should be up to individuals to decide whether they will put money aside for retirement, and to choose how much they want to save.

Boosting their campaign is the coronavirus-induced recession that Australia has plunged into this year, with some politicians arguing now is not the time for companies to have to contribute more money to employees' superannuation.

Even before the pandemic forced more than 1 million Australians into unemployment, public policy think tank The Grattan Institute released a paper in February that found workers effectively paid for increasing the super guarantee with lower wages.

It argued the rise to 12 per cent should be abandoned.

Could retirement incomes be 'smashed' further?

Labor maintains if Mr Morrison changes his Government's position now, it will break an election commitment he took to voters last year.

Shadow Treasurer Jim Chalmers said a further freeze on contribution increases would 'smash retirement incomes'.

When the coronavirus pandemic hit, the Federal Government opened up the option for cash-strapped Australians to take money out of their superannuation accounts.

More than $33 billion has already been withdrawn, and it's estimated about half a million Australians have cleaned out their entire superannuation account in the process.

'Now more than ever, Australians need the legislated increase in the super guarantee to rebuild their retirement balances,' Mr Chalmers said.

The architect of the compulsory super scheme, Mr Keating, recently put it a little more bluntly, saying people were 'ratting on their own savings'.

The Association of Superannuation Funds of Australia (ASFA) says many of the people who have drained their super accounts completely are under the age of 35.

ASFA argues moving to a higher superannuation guarantee is 'critical' to helping many young people facing long-term unemployment.

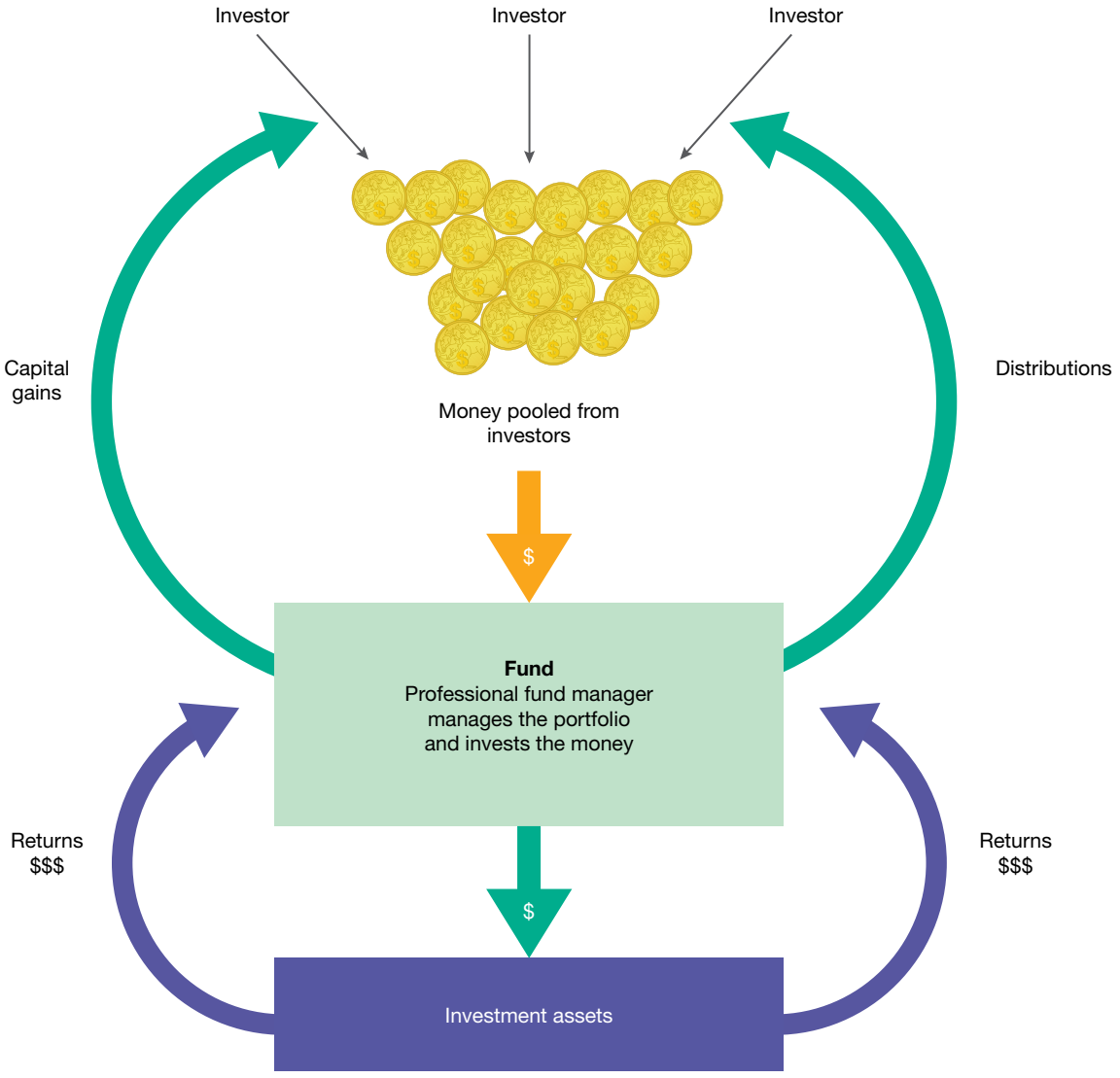
The association, which represents players in the $3 trillion superannuation industry, maintains the higher contributions will help ensure people aren't left to rely solely on the age pension when they retire.

Source: Anna Henderson, 'Contributions to your super are set to get a boost next year — but coronavirus could send the plan off the rails', www.abc.net.au, 18 August 2020.

13.3.6 Unit trusts

Unit trusts (also known as mutual funds) take funds from a large number of small investors and invest them in specific types of financial assets. Unit trusts invest in any mixture of cash, Australian or international shares, fixed interest securities (such as government bonds) or property. In recent years some unit trusts have also invested in gold, silver, oil and gas. Unit trusts are usually connected to a management firm that manages a diversified investment portfolio for its investors.

FIGURE 13.11 How unit trust funds work



13.3.7 Australian Securities Exchange

The **Australian Securities Exchange (ASX)** was created by the merger of the Australian Stock Exchange and the Sydney Futures Exchange in July 2006 and is the primary stock exchange group in Australia. The ASX is a market where shares are bought and sold.

The ASX functions as a market operator, clearing house and payments system facilitator. It oversees compliance with its operating rules and promotes standards of corporate governance among Australia's listed companies. The ASX offers products and services including:

- shares
- futures
- exchange traded options
- warrants
- contracts for difference
- exchange traded funds
- real estate investment trusts
- listed investment companies
- interest rate securities.

Australian Securities Exchange (ASX) the primary stock exchange group in Australia

primary market deals with the new issue of debt instruments by the borrower of funds

secondary market deals with the purchase and sale of existing securities

The biggest stocks traded on the ASX include BHP Billiton, CBA, Rio Tinto, CSL and Westpac.

Importantly for businesses, the ASX acts as a **primary market**. This primary market enables a company to raise new capital through the issue of shares and through the receipt of proceeds from the sale of securities.

The ASX also operates as a **secondary market**. The secondary market is where pre-owned or second-hand securities, such as shares, are traded between investors who may be individuals, businesses, governments or financial institutions. Transactions in this market do not increase the total amount of financial assets — the secondary market increases the liquidity of financial assets and, therefore, influences the primary market for securities.

FIGURE 13.12 The most common way to buy and sell shares is on the share market using a full service broker, an online trading account or from the company itself when it offers shares through a public float. An online broking service allows investors to make their own investment decisions for lower fees. A full service broker will charge more; however, they can also give advice on what to buy and sell.



Resources

Weblink National Australia Bank (NAB)

KEY IDEAS

- The main financial institutions are:
  - banks
  - investment banks
  - finance companies
  - life insurance companies
  - superannuation funds
  - unit trusts
  - Australian Securities Exchange.
- Banks are the major operators in financial markets and are the most important source of funds for business.
- Investment banks provide services in both borrowing and lending, primarily to the business sector.
- Finance companies are non-bank financial intermediaries that specialise in smaller commercial finance.
- Life insurance companies are also non-bank financial intermediaries who provide cover and a lump sum payment in the event of death.
- Superannuation funds are able to invest the contributions of members into a range of short- and long-term investments with the aim of maximising a return.
- The business sector increasingly uses superannuation funds for long-term investment in growth and development.
- The ASX acts as both a primary and secondary market for the sale of shares to the public.

13.3 Activities

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13.3 Quick quiz | **13.3 Exercise** | **13.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 8	2, 4, 5, 6, 7	9, 10, 11, 12

13.3 Exercise

Revision

1. Draw a table, as indicated below, to **summarise** the major participants in financial markets.

Financial institution	Financial instruments	Characteristics

2. Choose three financial instruments. **Investigate** current interest rates, maturity dates, and terms and conditions from a range of four institutions.
3. Using the internet, **identify** five investment banks that are currently operating in Australian financial markets.
4. **Explain** the role of financial markets in meeting the needs of businesses.
5. **Distinguish** between primary and secondary markets.
6. **Examine** an area of business banking that interests you, for example, superannuation at the National Australia Bank (NAB). Prepare a list of five points summarising what you learnt.
7. **Explain** how superannuation works.

Read the 'Future plans for the superannuation guarantee' case study and answer questions 8 and 9.

8. **Define** the superannuation guarantee.
9. **Assess** the impacts of increasing the superannuation guarantee on individuals, employers and the government.

Extension

10. It has been said that financial markets drive the financial and investment decisions of businesses. **Analyse** the accuracy of this statement.
11. Choose one of the major participants in financial markets. Examine the services offered to businesses. **Determine** current interest rates for borrowing and investing for businesses. Compare your investigations with those of other students.
12. Investigate the role of technology in improving financial market interactions for businesses. **Create** a report to management to explain how changing technology in financial markets can improve financial and investment decisions.

13.3 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q4

A business requires new manufacturing equipment.

Which of the following would provide leasing for this equipment?

A. Unit trusts
B. Property trusts
C. Finance companies
D. Superannuation funds

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q14

Which of the following is an example of a unit trust?

A. An investor purchases shares in a public company.
B. Investors lend money directly to businesses and receive interest in return.
C. Investors pool their money together and it is invested in the property market.
D. An investor deposits money with a financial institution and receives a fixed rate of interest.

Question 3 (4 marks)

Source: Adapted from HSC 2009 Business Studies Exam, Section II, Q24a

Describe ONE advantage and ONE disadvantage for a business obtaining finance through the Australian Securities Exchange.

Question 4 (1 mark)

Source: Adapted from HSC 2006 Business Studies Exam, Section I, Q6

What is the main role of the Australian Securities Exchange?

A. Conducting a public market in shares and debentures
B. Buying and selling securities in Australian businesses
C. Providing prudential supervision of financial institutions
D. Ensuring investors create economic growth and employment prospects

Question 5 (3 marks)

The Australian Securities Exchange (ASX) is a source of finance used by many businesses. Describe the primary and secondary finance role of the ASX.

More exam questions are available in your learnON title.

13.4 Influence of government

SYLLABUS LINK In this subtopic you will learn about the influence of government on financial management, including the impact of the Australian Securities and Investments Commission and company taxation.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The government influences a business's financial management decision making with economic policies such as those relating to the monetary and fiscal policy, legislation and the various roles of government bodies or departments who are responsible for monitoring and administration. The following outlines the importance of two governmental influences on financial management for businesses.

13.4.1 The Australian Securities and Investments Commission (ASIC)

ASIC is an independent statutory commission accountable to the Commonwealth parliament. It enforces and administers the *Corporations Act 2001* and protects consumers in the areas of investments, life and general insurance, superannuation and banking (except lending) in Australia.

FIGURE 13.13 ASIC enforces laws to protect Australian businesses, finance professionals and consumers.



The aim of ASIC is to assist in reducing fraud and unfair practices in financial markets and financial products. ASIC ensures that companies adhere to the law, collects information about companies and makes it available to the public. This includes the financial information that companies must disclose in their annual reports.

ASIC have been given a wide range of powers to enforce the Corporations Act. If a business breaches the law, ASIC will investigate the matter and determine an appropriate remedy. They are able to pursue a variety of remedies depending on the seriousness of the misconduct, such as imprisonment and monetary penalties. Failure to comply with the Corporations Act also generates negative publicity for the business.

BizFACT

ASIC regulates insolvent companies. New measures relating to insolvency were introduced in March 2020 to help businesses through the COVID-19 pandemic. The federal government amended the *Corporations Act 2001* to grant temporary relief for financially distressed businesses. Under the changes, creditors are unable to issue statutory demands or bankruptcy notices unless the debt totals $20 000 or more, up from $2000 and $5000 respectively. Directors are also protected from personal liability under insolvent trading rules if debts are incurred, except where they break the law.

13.4.2 Company taxation

All Australian businesses that have been incorporated — that is, all private and public companies — are required to pay company tax on profits. This tax is levied at a flat rate, unlike personal income taxes, which use a progressive scale. Prior to 2017, the company tax rate was 30 per cent for all companies; however in 2016, the company tax rate was reduced to 27.5 per cent for some businesses.

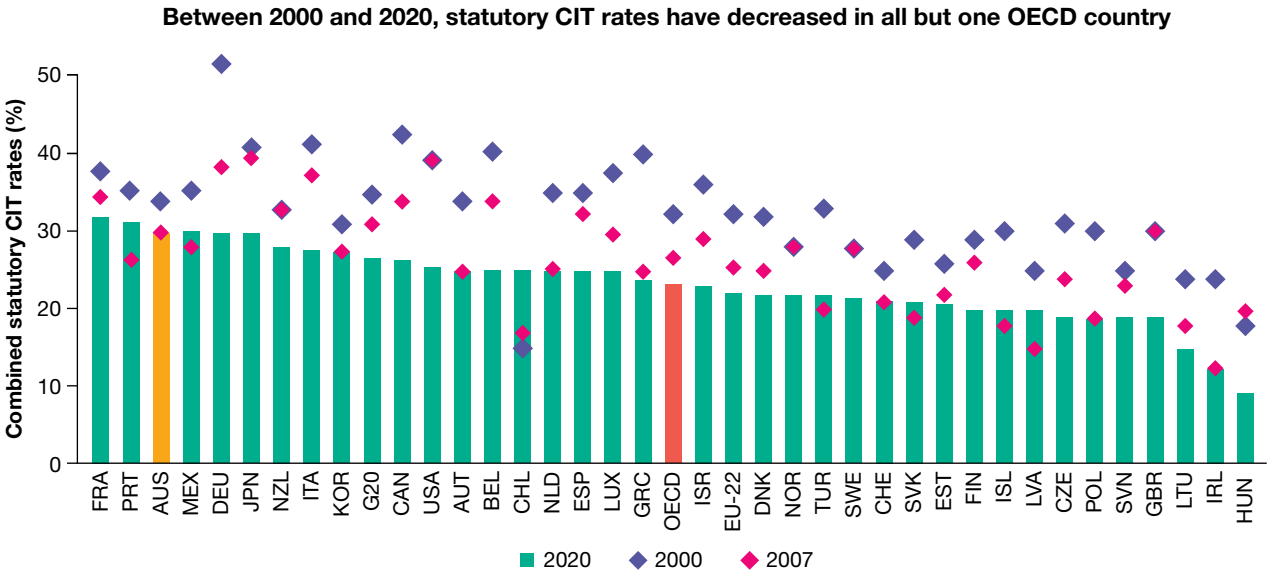
In order to be eligible for the lower company tax rate, the company has to have a turnover of less than $50 million. This rate was scheduled to reduce to 26 per cent in the 2020–21 income year and 25 per cent in the 2021–22 income year, however, the federal government has abandoned its plans to reduce the rate to 25 per cent for all businesses. Company tax is paid before profits are distributed to shareholders as dividends.

The Australian government has undertaken this process of reform of the federal tax system in order to improve Australia's international competitiveness and make Australia an even more attractive place to invest, thereby driving long-term economic growth. This will mean more jobs and higher wages for working Australians. The Australian company tax rate was previously reduced from 36 to 34 per cent in 2000–01 and then to 30 per cent in 2001–02.

BizFACT

Research into global company tax rates released by the OECD in July 2020 showed that between 2000 and 2020, the average global company tax rate fell to 23.1 per cent from 30.8 per cent. The OECD found Australia's effective marginal tax rate for businesses was the highest of the world's rich nations (see figure 13.14)

FIGURE 13.14 Australia's company tax rate in comparison to other OECD countries



Source: The Organisation for Economic Co-operation and Development (OECD), https://stats.oecd.org/Index.aspx?DataSetCode=TABLE_II1

Resources

Weblink Australian Securities and Investments Commission (ASIC)

KEY IDEAS

- The government influences the financial management of business through the implementation of economic policies (fiscal and monetary), and through the implementation of current and changing legislation.
- The Australian Securities and Investments Commission (ASIC) aims to reduce fraud and unfair practices in financial markets and financial products.
- All Australian businesses that have been incorporated are required to pay company tax on profits. This is levied at a flat rate of either 27.5 or 30 per cent of net profit depending on the business.

13.4 Activities

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13.4 Quick quiz | **13.4 Exercise** | **13.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 5	1, 2, 4	6, 7

13.4 Exercise

Revision

1. Describe the role of ASIC and briefly **discuss** its importance as a regulator of financial markets.
2. **Explain** the influence of company tax on financial management.

Refer to the graph in figure 13.14 to answer questions 3 to 5.

3. **Identify** the OECD country that has the lowest company tax rate.
4. **Compare** Australia's tax rate to that of other OECD countries.
5. **Identify** which country has the highest company tax rate. What is the tax rate?
6. **Assess** the impact a reduction in company tax to 25 per cent would have on businesses and the government.

Extension

7. Research nations that have lower company tax rates as well as the advantages and disadvantages of reducing the company tax rate to 25 per cent. Prepare a report **analysing** the effect a lower tax rate will have on Australia.

13.4 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q16

Which independent federal body ensures that businesses adhere to government regulations, maintain appropriate financial information and provide consumer protection?

A. Reserve Bank of Australia
B. Australian Securities Exchange
C. Australian Prudential Regulation Authority
D. Australian Securities and Investment Commission

Question 2 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q18

Which organisation ensures that Barb's Batteries Pty Ltd operates in a financially responsible manner?

A. Australian Securities and Investments Commission
B. Australian Prudential Regulation Authority
C. Australian Securities Exchange
D. Reserve Bank of Australia

Question 3 (4 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q24b

Explain government influences on the financial management of businesses.

Question 4 (1 mark)

Which government organisation is responsible for the enforcement of corporate laws?

A. Australian Prudential Regulation Authority
B. Australian Securities Exchange
C. Australian Securities and Investments Commission
D. Australian Competition and Consumer Commission

Question 5 (4 marks)

All businesses need to deal with government influences when managing their finances. Identify TWO government influences and clarify their influence on financial management of businesses.

More exam questions are available in your learnON title.

13.5 Global market influences

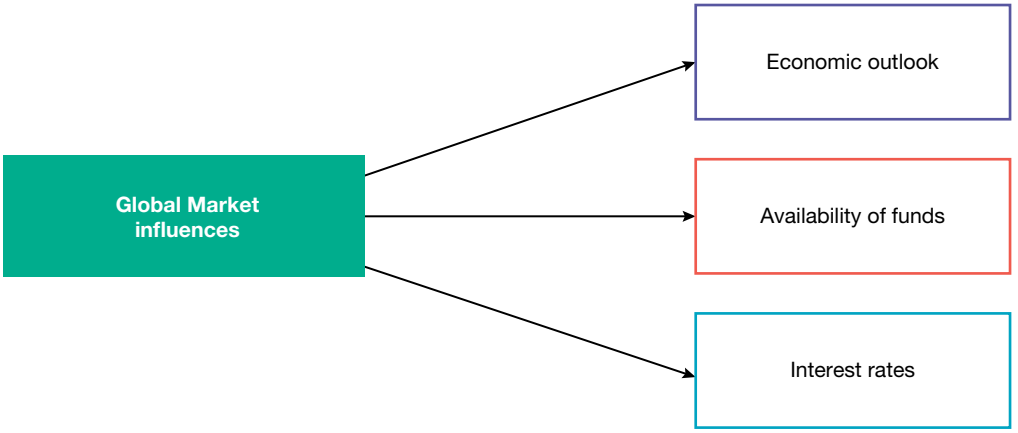
SYLLABUS LINK In this subtopic you will learn about global market influences including economic outlook, availability of funds and interest rates. You will also learn to analyse the influence of government and the global market on financial management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Financial risks associated with global markets are greater than those encountered domestically, but such risk-taking is necessary to implement a business strategy.

Largely uncontrollable financial influences include the availability of funds, interest rates and the global economic outlook. 'Uncontrollable' means that these influences are part of the external business environment and may not be significantly controlled by the business. However, a business can put in place appropriate financial management strategies to minimise the negative effects.

FIGURE 13.15 Global influences on financial management



One very significant influence in the past two decades is the impact of globalisation on world financial markets. Globalisation has created more interdependence between economies and their business (and financial) sector which relies on trade for expansion and increased profits.

13.5.1 Global economic outlook

The **global economic outlook** refers specifically to the projected changes to the level of economic growth throughout the world. If the outlook is positive (that is, world economic growth is to increase) then this will have an impact on the financial decisions of a business. This may include:

- increasing demand for products and services. For a country such as Australia, this would mean businesses will need to increase production to meet demand and therefore require funds to purchase equipment, employ or train staff, or expand the size of the business.
- a decrease in the interest rates on funds borrowed internationally from the financial money market. This results mainly from a decrease in the level of risk associated with repayments. As business sales increase, so too do profits. (Although, increased demand for funds can actually cause interest rates to rise!)

However, a poor economic outlook will have an impact on financial decisions of a business in the opposite way to those mentioned previously.

global economic outlook the projected changes to the level of economic growth throughout the world

The COVID-19 pandemic has had a detrimental impact on economies all around the world. Australia has suffered its deepest economic contraction since the Great Depression of the 1930s. In September 2020 the Australian Bureau of Statistics confirmed the nation's first recession since 1990–91 with the economy decreasing by 6.3 per cent over the past 12 months. Household consumption fell by 12.7 per cent in the June 2020 quarter, discretionary spending dropped 25 per cent and spending on services fell 17.6 per cent.

Because of Australia's early success in controlling the virus, our performance actually compares favourably with other nations who have experienced up to more than twice the size of Australia's economic contraction. For example, the United States' economy contracted by 31.7 per cent, Britain's by 20.4 per cent, Canada's by 11.5 per cent and Germany's shrank by 9.7 per cent.

As of June 2020, it was predicted that the COVID-19 recession would cost the Australian economy at least $170 billion. The world economy is facing a five-year financial hit of between $25 trillion, if the virus is contained, and $51.8 trillion if nations fail to control the spread. Investment, employment and consumer spending are all expected to take more than a year to recover the ground lost due to the virus.

13.5.2 Availability of funds

The **availability of funds** refers to the ease with which a business can access funds (for borrowing) on the international financial markets. The international financial markets are made up of a range of institutions, companies and governments that are prepared to lend money to individuals, companies or governments who may need to raise capital. Various conditions and rates apply and these will be based primarily on:

- risk
- demand and supply
- domestic economic conditions.

The Australian financial system was deregulated in the 1970s and 1980s. Ever since barriers to cross-border financial flows were dismantled, the Australian economy became more integrated with the global financial system. As a result, Australians are free to borrow and invest in financial assets overseas, and foreigners can do likewise in Australian markets. These developments have had a lot of benefits for businesses, including increasing the availability of funds.

Since the global financial crisis of 2008–09, access to credit has been one of the biggest challenges facing businesses. This has been made worse by the COVID-19 pandemic, which has had a negative impact on the availability of funds. The reluctance of banks to lend money has had a greater impact on small businesses. Part of the reason why banks are hesitant to lend to businesses is the fact that so many businesses have failed and are experiencing difficulties meeting their current repayments.

13.5.3 Interest rates

Interest rates are the cost of borrowing money. The higher the level of risk involved in lending to a business, the higher the interest rates. A business that plans to either relocate offshore or expand domestic production facilities to increase direct exporting will normally need to raise finance to undertake these activities. Traditionally, Australian interest rates tend to be above those of other countries, such as the United States and Japan. Therefore, Australian businesses could be tempted to borrow the necessary finance from an overseas source to gain the advantage of lower interest rates. However, the real risk here is exchange rate movements. Any adverse currency fluctuation could see the advantage of cheaper overseas interest rates quickly eliminated. In the long term, the 'cheap' interest rates may end up costing more.

During the global financial crisis of 2008–09, central banks around the world slashed interest rates and bought bonds and mortgages in an attempt to keep their economies afloat. More than a decade later, those 'emergency' measures are still in place and interest rates dropped even lower in response to the COVID-19 pandemic.

availability of funds refers to the ease with which a business can access funds (for borrowing) on the international financial markets

interest rates the cost of borrowing money

Since COVID-19, central bank interest rates around the world are at either ultra-low levels or in negative territory. As nations went into lockdown, global economies were flooded with cheap credit and deferred interest and repayments. Interest rates in Japan and Europe are negative and US rates are historically low.

13.5.4 Analyse the influence of government and the global market on financial management

The government has a significant impact on businesses and their financial management. For example:

- Legislation introduced by the government will influence the decisions businesses make about their finances as well as their cash flow.
- Government policies impact on the choice of legal structure as different obligations are imposed on different types of businesses.
- Businesses that don't comply with government regulations can face a number of penalties, which in turn will impact on their finances as well as their reputation.
- Taxation regulations will affect business's financial decisions.
- New government policies can affect the amount of financial assistance businesses receive.

The government introduced a wide range of measures during the COVID-19 pandemic that significantly impacted on the financial management strategies of businesses:

- *JobKeeper Payment* — businesses affected by COVID-19 may be eligible to access this payment to help them continue paying their employees
- *Relief for commercial tenants* — the federal government introduced a range of measures to help commercial tenants and SMEs affected by COVID-19. This includes a temporary hold on evictions and a mandatory code of conduct for commercial tenancies.
- *Boosting cash flow for employers* — the federal government provided temporary cash flow support to SMEs that employ staff during the economic downturn. The ATO provided eligible businesses with a tax-free cash flow boost of between $20 000 and $100 000 delivered through credits in the business activity statement system.
- *Increasing the Instant Asset Write-Off* — this provides cash flow benefits for businesses that will be able to immediately deduct purchases of eligible assets costing less than $150 000.
- *Supporting apprentices and trainees* — businesses that employ an apprentice or trainee may be eligible for a wage subsidy of 50 per cent of their wage.
- *Coronavirus SME Guarantee Scheme* — under this scheme, the federal government will provide a guarantee of 50 per cent to eligible SME lenders for new unsecured loans to be used for working capital. This will enhance lenders' willingness to provide credit to SMEs, which will enable them to access additional funding.
- *Temporary relief for financially distressed businesses* — the federal government temporarily increased the threshold at which creditors can issue a statutory demand on a company and the time companies have to respond. They also increased the threshold for a creditor to initiate bankruptcy proceedings.

The global market also has a significant impact on the financial strategies of businesses, especially during this current climate. For example:

- The global economic outlook has a direct effect on the demand for Australian exports; that is, a positive outlook will increase demand for Australian products whereas a negative outlook will decrease demand.
- The availability of funds will impact on whether Australian businesses can access the money they need to expand. Since the Australian financial system was deregulated, Australians have been able to borrow and invest in financial assets overseas.
- Overseas interest rates will affect Australian businesses who borrow funds offshore. If interest rates and/or exchange rates change, this could lead to an increase or decrease in repayments and this in turn will affect profits.
- The global recession has led to a decrease in household consumption and discretionary spending, which in turn will affect business's profitability. Many businesses have had to implement a variety of financial management strategies to meet these challenges.

Resources

Video eLesson Floating Intrepid Travel (eles-1045)

KEY IDEAS

- Globalisation has created more interdependence between economies and their business (and finance) sectors, which relies on trade for expansion and increased profits.
- Global market influences increasingly affect business financial decisions, and this is specifically evident in the availability of funds for loans and the interest rates charged for these loans.
- The changes to the global economic outlook relate specifically to changes in the economic growth rates of individual economies throughout the world.
- The COVID-19 pandemic has had a detrimental impact on the global economic outlook.
- The need to maximise profits and the capacity to source funds internationally will affect financial management decisions.

13.5 Activities

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13.5 Quick quiz | **13.5 Exercise** | **13.5 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 6	2, 5	7, 8, 9

13.5 Exercise

Revision

1. **a.** **Identify** three global market influences.
   b. Why are these influences considered ‘uncontrollable’?
2. **How** could a negative global outlook affect the financial decisions of a business?
3. **Outline** factors that will affect a business’s ability to access funds globally.
4. **Outline** the risk to Australian businesses of borrowing finance from an overseas source to gain the advantage of lower interest rates.
5. **Explain** the impact of the global market on the financial management decisions of businesses throughout the world. Use examples in your response.
6. **Summarise** the implications for businesses in relation to the influences of government and the global market.

Extension

7. Use the internet to **determine** three financial impacts of the COVID-19 pandemic on business.
8. **Create** a timeline of the history of interest rates in Australia.
9. **Assess** the impact the COVID-19 pandemic has had on the global economic outlook.

13.5 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q8

What effect would a global downturn in the economic outlook have on Australia's unemployment, output and exchange rates?

	Unemployment	***Output***	***Exchange rates***
A.	Increase	Increase	Decrease
B.	Decrease	Increase	Increase
C.	Decrease	Decrease	Increase
D.	Increase	Decrease	Decrease

A. Option A
B. Option B
C. Option C
D. Option D

Question 2 (1 mark)

The Chinese and Indian markets are demanding more consumer products. In response, Titan Technology is selling their knowledge and expertise to businesses wishing to export to these markets. Which global market influence is providing this opportunity for Titan Technology?

A. Interest rates
B. Government policies
C. Economic outlook
D. Regulatory differences

Question 3 (1 mark)

Bonus Buying is an investment company that is making investments in South-East Asia. It has cited potential growth in manufacturing as the reason. This investment is the result of which global influence?

A. Regulatory differences
B. Interest rates
C. Cheaper resources
D. Economic outlook

Question 4 (1 mark)

'We want to build in Vietnam. We use their finance, their labour and their goodwill!' The reason for using finance provided by Vietnam would most likely be the result of which global influence on financial management?

A. Interest rates
B. Economic outlook
C. Local laws
D. Cheaper labour

Question 5 (4 marks)

'We need the capital to make this takeover bid. I do not care where you get it from, but get it now. Get it from anywhere, just get it now!' These are the instructions from the CEO to the financial management team of a global food and beverage provider. Describe TWO global influences that may influence the source of this finance.

More exam questions are available in your learnON title.

13.6 Review

13.6.1 Summary

Sources of finance — internal and external

- Internal finance refers to funds that are generated from inside the business. For example, profits can be retained to finance expansion.
- External finance is the funds provided by sources outside the business, such as financial institutions, governments and suppliers.
- External sources of finance are broadly categorised as either debt or equity — each will influence the financial management decision of a business.
- Debt finance can be short-term borrowings such as overdrafts, commercial bills and factoring; or long-term borrowings such as mortgages, debentures, unsecured notes and leasing.
- Equity refers to the cash raised by a company through:
  - issuing ordinary shares to the public for purchase through the ASX
  - private shares (equity) in companies not listed on the ASX.
- Different types of ordinary shares include:
  - new issue
  - rights issue
  - placements
  - share purchase plan.

Financial institutions

- The main financial institutions are:
  - banks
  - investment banks
  - finance companies
  - life insurance companies
  - superannuation funds
  - unit trusts
  - Australian Securities Exchange.
- Banks are the major operators in financial markets and are the most important source of funds for business.
- Investment banks provide services in both borrowing and lending, primarily to the business sector.
- Finance companies are non-bank financial intermediaries that specialise in smaller commercial finance.
- Life insurance companies are also non-bank financial intermediaries who provide cover and a lump sum payment in the event of death.
- Superannuation funds are able to invest the contributions of members into a range of short- and long-term investments with the aim of maximising a return.
- The business sector increasingly uses superannuation funds for long-term investment in growth and development.
- The ASX acts as both a primary and secondary market for the sale of shares to the public.

Influence of government

- The government influences the financial management of business through the implementation of economic policies (fiscal and monetary), and through the implementation of current and changing legislation.
- The Australian Securities and Investments Commission (ASIC) aims to reduce fraud and unfair practices in financial markets and financial products.
- All Australian businesses that have been incorporated are required to pay company tax on profits. This is levied at a flat rate of either 27.5 or 30 per cent of net profit depending on the business.

Global market influences

- Globalisation has created more interdependence between economies and their business (and finance) sectors, which relies on trade for expansion and increased profits.
- Global market influences increasingly affect business financial decisions, and this is specifically evident in the availability of funds for loans and the interest rates charged for these loans.
- The changes to the global economic outlook relate specifically to changes in the economic growth rates of individual economies throughout the world.
- The COVID-19 pandemic has had a detrimental impact on the global economic outlook.
- The need to maximise profits and the capacity to source funds internationally will affect financial management decisions.

13.6.2 Key terms

Australian Securities Exchange (ASX) the primary stock exchange group in Australia
availability of funds refers to the ease with which a business can access funds (for borrowing) on the international financial markets
commercial bills primarily short-term loans issued by financial institutions, for larger amounts (usually over $100 000) for a period of generally between 30 and 180 days
debenture a promise issued by a company to repay a loan for a fixed rate of interest and for a fixed period of time
debt finance relates to the short-term and long-term borrowing from external sources by a business
dividend a distribution of a company's profits (either yearly or half-yearly) to shareholders, calculated as a number of cents per share
equity as an external source of funds, refers to the finance raised by a company through inviting new owners
external finance funds provided by sources outside the business, including banks, other financial institutions, government, suppliers or financial intermediaries
factoring the selling of accounts receivable for a discounted price to a finance or factoring company
financial decision making requires relevant information to be identified, collected and analysed to determine an appropriate course of action
global economic outlook the projected changes to the level of economic growth throughout the world
interest rates the cost of borrowing money
internal finance funds generated from inside the business; for example, profits can be retained to finance expansion
leasing the payment of money for the use of equipment that is owned by another party
mortgage a loan secured by the property of the borrower (business)
overdraft when a bank allows a business or individual to overdraw their account up to an agreed limit and for a specified time, to help overcome a temporary cash shortfall
primary market deals with the new issue of debt instruments by the borrower of funds
secondary market deals with the purchase and sale of existing securities
superannuation a scheme set up by the federal government, which requires all employers to make a financial contribution to a fund that will provide benefits to an employee when they retire
unsecured note a loan from investors for a set period of time. Unsecured notes are not secured against the business's assets.

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Digital documents	Key terms glossary (doc-35648) Chapter crossword (doc-36219)
Interactivity	Chapter crossword (int-7167)
Exam question booklet	Chapter 13 Exam question booklet (eqb-0035)

13.6 Activities

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Exercise 1: Multiple choice questions

1. Which of the following financial institutions takes funds from a large number of investors and invests those funds in a variety of assets?
   - **A.** Unit trust
   - **B.** Investment bank
   - **C.** Finance company
   - **D.** Australian Securities Exchange
2. Which of the following is an external source of equity?
   - **A.** Debentures
   - **B.** Retained profits
   - **C.** Ordinary shares
   - **D.** Commercial bills
3. Steady Saddles produces horseriding supplies. They are well established and are looking to source funds to buy more efficient saddle-making equipment, without relying on debt. What would be the most appropriate source of finance?
   - **A.** Overdraft
   - **B.** Retained profits
   - **C.** Factoring
   - **D.** Leasing
4. Which of the following is a source of finance that provides large amounts of funds, is short term but able to be paid in full at the end of the term?
   - **A.** Overdraft
   - **B.** Unsecured notes
   - **C.** Debentures
   - **D.** Commercial bills
5. A business awaiting payment of a large amount of accounts receivable can raise funds quickly by selling them at a discount to a finance company who will manage collection. What is this form of debt known as?
   - **A.** Factoring
   - **B.** Unsecured notes
   - **C.** Debentures
   - **D.** Leasing
6. What is the name of the organisation which functions as a market where shares are bought and sold?
   - **A.** Unit trust
   - **B.** Australian Taxation Office
   - **C.** Australian Securities Exchange
   - **D.** Australian Securities and Investments Commission
7. Which of the following are both examples of short-term borrowing?
   - **A.** Factoring and commercial bills
   - **B.** Commercial bills and debentures
   - **C.** Debentures and overdraft
   - **D.** Overdraft and leasing
8. Never-fail Nightlights is hoping to raise funds through inviting new owners. This can be achieved through which of the following?
   - **A.** Factoring
   - **B.** Leasing
   - **C.** Debentures
   - **D.** Ordinary shares

9. Compulsory payments made by employers to employees aged 18 to 69, earning over $450 a month, which are invested over a long-term period are known as which of the following?
   A. Futures
   B. Insurance
   C. Superannuation
   D. Debentures

10. Which type of ordinary shares are offered to existing shareholders in a listed company, allowing them to purchase more shares in that company without brokerage fees?
   A. New issue
   B. Rights issue
   C. Placements
   D. Share purchase plan

Exercise 2: Exam practice questions

Question 1 (3 marks)
Describe ONE influence of government on financial management.

Question 2 (2 marks)
Define an overdraft.

Question 3 (9 marks)
An Australian company is considering taking over and purchasing a Japanese company.
a. **Explain** how TWO global market influences could impact on the planned acquisition. **(5 marks)**
b. **Recommend** ONE long-term source of funds the business can use for the planned acquisition. **(4 marks)**

Question 4 (6 marks)
DrinkUp Ltd is a successful Australian beverage manufacturer that is considering expanding its operations overseas. The managers are currently considering various options for sourcing finance.

Recommend ONE source of debt finance and ONE source of equity finance for this business.

Question 5 (6 marks)
Analyse the impact a new issue would have on the business as well as on existing owners.

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14 Processes of financial management

14.1 Overview

LEARNING SEQUENCE

14.1 Overview
14.2 Planning and implementing
14.3 Debt and equity financing
14.4 Matching the terms and source of finance to business purpose
14.5 Monitoring and controlling
14.6 Financial ratios
14.7 Identify the limitations of financial reporting
14.8 Ethical issues related to financial reports
14.9 Review

14.1.1 Introduction

An important part of financial management is establishing effective financial processes to monitor the financial health of the business and ensure the organisation meets its objectives.

FIGURE 14.1 The main processes of financial management



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Digital document Key terms glossary (doc-35650)
Exam question booklet Chapter 14 Exam question booklet (eqb-0036)

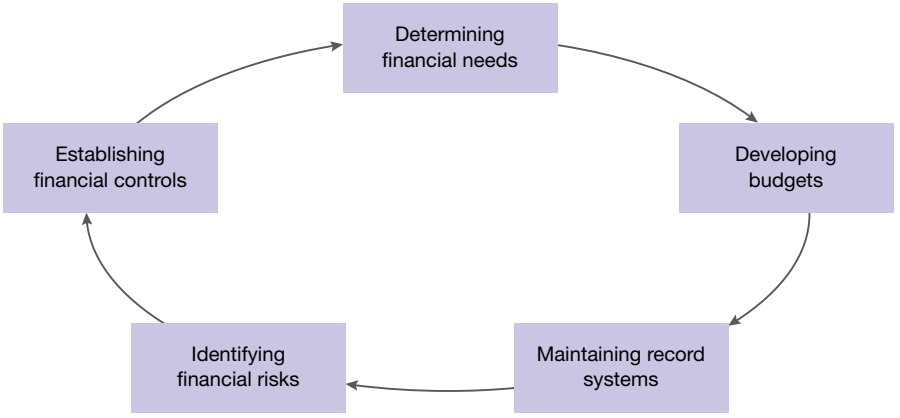
14.2 Planning and implementing

SYLLABUS LINK In this subtopic you will learn about planning and implementing processes of financial management, including; financial needs, budgets, record systems, financial risks and financial controls.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Financial planning is essential if a business is to achieve its goals. Financial planning determines how a business's goals will be achieved. Figure 14.2 shows the process of financial planning and implementing.

FIGURE 14.2 The planning and implementing cycle



14.2.1 Financial needs

To determine where a business is headed and how it will get there, it is important to know what its needs are. Important financial information needs to be collected before future plans can be made. This financial information includes balance sheets, income statements, cash flow statements, sales and price forecasts, budgets, bank statements, weekly reports from departments, break-even analysis, reports from financial ratio analysis and interpretation.

The financial needs of a business will be determined by:

- the size of the business
- the current phase of the business cycle
- future plans for growth and development
- capacity to source finance — debt and/or equity
- management skills for assessing financial needs and planning.

A business plan might be used when seeking finance or support for a project from a bank or other financial institution or other potential investors. These institutions need a guarantee that their financial commitment to the business will be successful. A business plan sets out how much finance is required, the proposed sources of finance and a range of financial statements. The type of financial information that is included in a business plan depends on the audience — employees, owners, lenders or potential investors. Financial information is needed to show that the business can generate an acceptable return for the investment being sought and should, therefore, include an analysis of financial performance, income statement, cash flow statement, balance sheet and financial ratio analysis reports.

14.2.2 Budgets

A **budget** is a financial document used to estimate future revenue and expenses over a period of time. A budget should provide an accurate picture of income and expenses and should be used to drive important business decisions such as whether to increase marketing, hire staff, cut expenses or purchase new assets.

Budgets reflect the strategic planning decisions and help managers allocate resources, evaluate performance and formulate plans. They provide financial information for a business's specific goals and are used in strategic, tactical and operational planning.

Budgets enable constant monitoring of objectives and provide a basis for administrative control, direction of sales effort, production planning, control of stocks, price setting, financial requirements, control of expenses and of production cost.

FIGURE 14.3 Budgets are important financial management tools. They enable managers to plan for the future, monitor past and present performance, and coordinate the plans made by different sections of the business.



BizFACT

Budgets provide the facts and figures for planning and decision making, and enable constant monitoring of progress and problem areas. They signal where things are not going according to plan so that adjustments can be made, and show where achievement towards objectives has occurred.

Budgets are used in both the planning and the control aspects of a business. As a control measure, planned performance can be measured against actual performance and corrective action taken as needed.

A budget is an important part of the planning process and various factors need to be considered in preparing it, such as:

- review of past figures and trends, and estimates gathered from relevant departments in the business
- potential market or market share, and trends and seasonal fluctuations in the market
- proposed expansion or discontinuation of projects
- proposals to alter price or quality of products
- current orders and plant capacity
- considerations from the external environment — for example, financial trends from the external environment, availability of materials and labour.

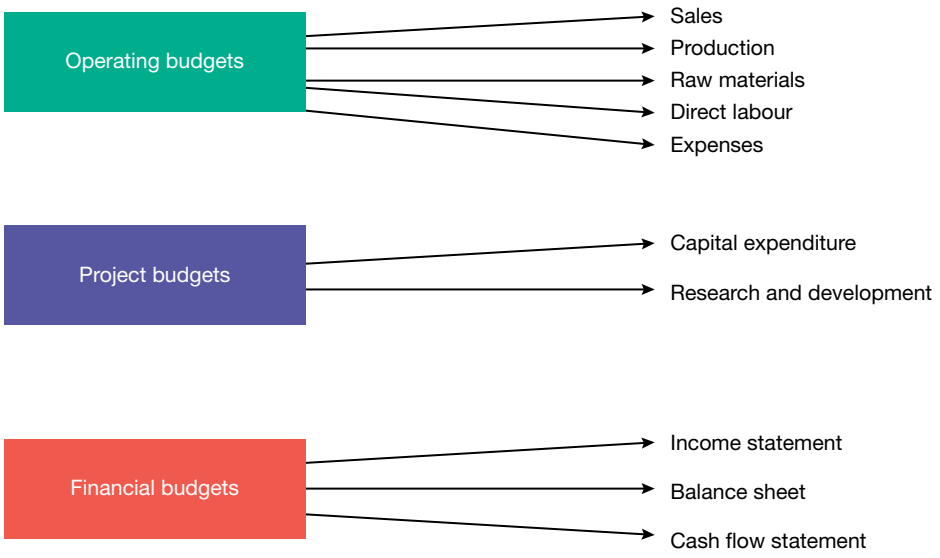
Budgets are often prepared to predict a range of activities relating to short-term and longer-term plans and activities. There are many different types of budgets (see figure 14.4).

Operating budgets relate to the main activities of a business and may include budgets relating to sales, production, raw materials, direct labour, expenses and cost of goods sold. Information from operating budgets is used in preparing budgeted financial statements.

budget a financial document used to estimate future revenue and expenses over a period of time

operating budgets relate to the main activities of a business and may include budgets relating to sales, production, raw materials, direct labour, expenses and cost of goods sold

FIGURE 14.4 Operating, project and financial budgets



Project budgets relate to capital expenditure, and research and development. Capital expenditure budgets in a business's strategic plan include information about the purpose of the asset purchase, life span of the asset and the revenue that would be generated from the purchase. Information from project budgets is included in the budgeted financial statements.

Financial budgets relate to the financial data of a business. The predictions of the operating and project budgets are included in the budgeted financial statements. Financial budgets include the budgeted income statement, balance sheet and cash flows. The income statement and balance sheet reflect the results of operating activities and the cash flow statement shows the liquidity of a business.

FIGURE 14.5 Budgeted income statement including sales and expense predictions

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Year
Product 1 (price $50)	3 000	3 500	4 000	6 000	16 500
Product 2 (price $70)	5 000	5 800	6 500	7 000	24 300
Total sales	**$500 000**	**$581 000**	**$655 000**	**$790 000**	**$2 526 000**

14.2.3 Record systems

Managers need to set up a record system that allows them to record all the information they need. **Record systems** are the mechanisms employed by a business to ensure that data are recorded and the information provided is accurate, reliable, efficient and accessible (see the following case study). Management bases its decisions on the information when needed and must have guarantees that the information is accurate and reliable.

project budgets relate to capital expenditure, and research and development

financial budgets relate to financial data of a business and include the budgeted income statement, balance sheet and cash flows

record systems the mechanisms employed by a business to ensure that data are recorded and the information provided is accurate, reliable, efficient and accessible

BizFACT

According to statistics released by ASIC, poor record keeping is a major cause of business failure. This is why it is so important that businesses use an accounting program to manage records well.

Maintaining accurate records is not only an obligation of the business, but also serves as an invaluable tool for decision making. Without accurate records, an owner has a restricted understanding of how the business is performing and where improvements need to be made. Furthermore, investors and financial institutions are unlikely to invest in or make loans to a business that cannot demonstrate its financial position.

Businesses are required by law to keep records of their financial transactions for at least five years for tax purposes. This includes all documents relating to income and expenses such as tax invoices, receipts and bank statements, as well as other important documents such as employee contracts. While the Australian Taxation Office (ATO) allows businesses to keep all such information electronically, it is important that businesses keep their electronic information backed up and secure. While maintaining accurate records can be a time-consuming and daunting task, having the right systems and strategies in place can cut down and simplify the workload significantly.

SNAPSHOT

Case study: Record keeping — financial management



Good business records help owners manage their business and make sound business decisions. In fact, record keeping isn't just good business practice; it's also a legal requirement. Businesses are required by the Australian Taxation Office (ATO) to keep certain records for a minimum of five years.

Businesses need to create a record-keeping system that is simple, reliable, accurate and able to provide information in an accessible format when they need it. They can choose to operate a manual or electronic system.

Manual record-keeping systems consist of paper-based journals. The journals are divided into separate sections for receipts, payments, bank reconciliation, wages and superannuation, inventory and others. Under this system, financial managers record business transactions manually in the appropriate sections for each month. Manual record keeping is less expensive to set up and data loss is less of a risk.

Businesses can also choose to record financial information electronically, using an electronic spreadsheet or a software accounting package. Electronic record keeping systems are a more efficient way of keeping financial records. Computer programs allow financial managers to easily generate orders, reports, invoices, financial statements, pay records, and so on.

A variety of accounting software programs has been developed to assist businesses with their records. Many accounting programs also allow users to email and send financial information to clients, suppliers or the ATO. Electronic systems require less storage space and make it easier for businesses to meet their tax and legal obligations.

Businesses that use electronic record systems should ensure that their records are secure and that they create a backup system to ensure their records are not lost. They also need to be familiar with accounting principles and may need training to understand how the software works.

14.2.4 Financial risks

Financial risk refers to the possibility of financial loss to businesses. Every business is subject to a degree of financial risk and not all financial risks are able to be controlled; for example, changes in interest rates. Some of the most common financial risks for businesses include:

- **Credit risk** — this is the danger associated with borrowing money. Businesses need to ensure they always have sufficient funds to meet their repayments when they fall due, otherwise they can incur severe penalties. Credit risk also refers to the risk businesses may face by extending credit to customers who may be unable to pay for their goods or services. When businesses borrow money, they are also faced with interest rate risks, i.e. the risk of movements in interest rates which will affect their financial performance by increasing interest expenses.
- **Market risk** — this involves the risk of changing conditions in the specific marketplace in which a company competes for business; for example, the increasing number of consumers shopping online or increasing competition. A business market is subject to changing conditions, and this can affect its profitability.
- **Liquidity risk** — this refers to a business's cash flow and whether the business has sufficient funds to meet their financial obligations. It refers to how easily a business can convert their assets into cash should they need funds. Cash flow management is critical to business success as there are many consequences for businesses who find themselves in a situation where they don't have enough cash to pay their expenses.
- **Operational risk** — this refers to the various dangers faced during the day-to-day management of a business. Potential operational risks include legal problems, fraud risk, human resource issues, and business model risk, which is the risk that a business's marketing or growth plans may prove to be inaccurate or inadequate. Businesses can experience operational risk when they have poor management.

14.2.5 Financial controls

Financial controls are the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources.

The policies and procedures of a business are designed to ensure they are followed by management and employees. Control is particularly important in assets such as accounts receivable, inventory and cash. Some common policies and procedures that promote control within a business are:

- clear authorisation and responsibility for tasks in the business
- separation of duties — for example, one person is responsible for ordering and another for receiving inventories
- placing certain qualification restrictions and employing only certified and qualified staff for certain roles
- control of cash, such as the use of cash registers, cash banked daily, no money kept on premises overnight, payments made by card not cash
- protection of assets — for example, buildings are kept locked, a registry of assets is maintained, regular checks of inventory are carried out and security surveillance systems are installed
- control of credit procedures, such as following up overdue accounts and customer credit checks.

Budgets and variance reporting are financial controls used in businesses. As previously outlined, budgets are an important planning tool as they assist a business to estimate resource requirements for a specified future period to predict what will be achieved by a business. For example, preparing a cash budget enables a business to predict cash shortages.

financial risk the possibility of financial loss to businesses

financial controls the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources

KEY IDEAS

- Financial planning is essential if a business is to achieve its goals. Financial planning determines how a business's goals will be achieved.
- The financial planning and implementing process consists of: determining financial needs, developing budgets, maintaining record systems, identifying financial risks and establishing financial controls.
- Financial needs are essential in order for a business to identify where it is headed and how it will get there.
- Budgets are financial documents used to estimate future revenue and expenses over a period of time.
- Budgets are often prepared to predict a range of activities relating to short-term and longer-term plans and activities.
- Budgets can be classified as operating, project or financial budgets.
- Record systems are the mechanisms employed by a business to ensure that data are recorded and the information provided by records systems is accurate, reliable, efficient and accessible.
- Financial risk refers to the possibility of financial loss to businesses.
- Some of the most common financial risks for businesses include credit, market, liquidity and operational risks.
- Financial controls are the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources.

14.2 Activities

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14.2 Quick quiz on | **14.2 Exercise** | **14.2 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5, 7, 10, 12	3, 6, 8, 9, 11, 13, 15, 16, 17	14, 18, 19

14.2 Exercise

Revision

1. **Outline**, with examples, the financial elements of the planning cycle.
2. **Identify** the factors that determine businesses' financial needs.
3. **Explain** why the preparation of financial information is essential as part of the business plan.
4. **Identify** the financial information that should be collected by a business when determining its future financial needs.
5. **Summarise** the different types of budgets and their importance in financial planning.
6. **Explain** the importance of record keeping to a business's financial success.
7. **State** the relationship between risk and the level of borrowings by a business.
8. **Recommend** reasons for implementing financial controls.
9. Write an email to the manager of a web design company **explaining** how budget and variance analysis will assist the business.
10. **Summarise** some of the most common financial risks for businesses.
11. Study the comparative report below and answer the following questions. (Note that a variance of 10 per cent is acceptable for this business.)
    From the information in the comparative report, **recommend** where you think the performance of the business can be improved. **Justify** your recommendations.

Comparative report — receipts and payments

	Budgeted $	Actual $	Variance $
Receipts			
Sales			
– Cash	3 000	3 000	–
– Accounts receivable	8 000	8 800	+10%
Total receipts	11 000	11 800	+ 7%
Payments			
Purchases			
– Cash	1 500	1 400	– 6%
– Accounts receivable	2 000	2 400	+20%
Wages	500	600	+20%
Insurance	100	100	–
Advertising	300	350	+17%
Total payments	4 400	4 850	+10%

Read the 'Record keeping — financial management' case study and answer questions 12 to 14.

12. **Outline** the benefits of a good record-keeping system.
13. **Distinguish** between a manual and an electronic record-keeping system.
14. **Create** a table summarising the advantages and disadvantages of both manual and electronic record-keeping systems.

Extension

15. Complete the folllowing sales budget by **calculating** the missing figures.

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Year
Product 1 (price $25)	2000	2600	3000	3300	?
Product 2 (price $15)	4000	4400	5000	5500	?
Total sales	?	?	?	?	?

16. 'Sound planning is crucial to achieving the financial objectives of a business.' **Discuss**.
17. Identify the stages in the planning cycle. **Investigate** and **demonstrate** each stage using examples from your own knowledge of local businesses.
18. Using the following information on Kennedy's Gardening Supplies, answer the questions below.

Kennedy's Gardening Supplies

	2018 $	2019 $	2020 $
Forecast cash position	85 000	150 000	185 000
Forecast profits	40 000	75 000	90 000
Forecast net assets	350 000	390 000	410 000

Kennedy's is requesting an increase of overdraft facility from 2017 of $80 000 and a loan of $50 000 to fund their expansion.

   a. **Determine** what further financial information you would require in the business plan of Kennedy's Gardening Supplies.
   b. Propose how Kennedy's might prepare their information for their funding application to the bank.
19. Computerised accounting software programs are able to streamline the accounting process. Examine one such program and **evaluate** its key features, including the type of data that need to be entered and the type of reports that can be produced.

14.2 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q14

Which of the following is the correct order for financial planning?

A. Developing budgets, determining financial needs, maintaining record systems, identifying financial risks, establishing financial controls
B. Determining financial needs, establishing financial controls, identifying financial risks, maintaining record systems, developing budgets
C. Determining financial needs, developing budgets, maintaining record systems, identifying financial risks, establishing financial controls
D. Developing budgets, maintaining record systems, identifying financial risks, establishing financial controls, determining financial needs

Question 2 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q12

A business has the following balance sheet.

Assets	$	*Liabilities*	$
Current assets	15 000	Current liabilities	12 000
Non-current assets	174 000	Non-current liabilities	85 000
		Owners equity	92 000
	189 000		189 000

Industry averages: Current ratio 2:1
Debt to equity ratio: 200%

Compared to the industry averages, this business has

A. better solvency and better liquidity.
B. better solvency and poorer liquidity.
C. poorer solvency and better liquidity.
D. poorer solvency and poorer liquidity.

Question 3 (1 mark)

Which of the following statements best describes financial control?

A. Setting budgets for business
B. Identifying the financial needs of the business
C. Reading financial statements
D. Evaluating the performance of the business

Question 4 (2 marks)

What are budgets and how are they used in financial management?

Question 5 (6 marks)

Evaluate the role of planning and implementing as a part of financial management in the success of a business.

More exam questions are available in your learnON title.

14.3 Debt and equity financing

SYLLABUS LINK In this subtopic you will learn about the advantages and disadvantages of debt and equity financing.

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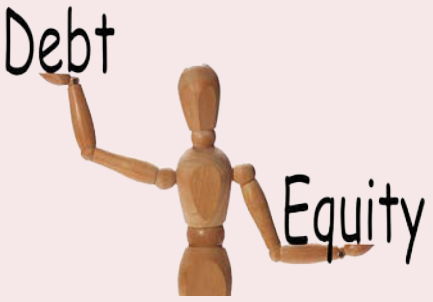
As outlined in chapter 13, the finance for a business comes from both internal and external sources, and most businesses use a combination of both. External or **debt finance** is a liability to a business as it is money owed to external sources. **Equity finance** relates to the internal sources of finance in the business. Businesses must carefully consider whether to use debt or equity finance and how much of each is needed.

debt finance short-term and long-term borrowing from external sources by a business

equity finance relates to the internal sources of finance in the business

BizFACT

A balancing act — how much debt is too much? Borrowing the right amount of debt can make the difference between a business struggling to survive and one that is able to respond to changes in the external business environment. While debt provides businesses with the necessary funds, too much debt can cripple a business. Factors to consider when determining how much debt businesses take on include the industry risk, projected income and an analysis of cash flow.



14.3.1 Debt finance

Debt can be attractive to businesses because funds are usually readily available and interest payments are tax deductible, therefore reducing the cost of debt financing. The amount of debt used by Australian businesses varies, but short-term borrowing (one year or less) is an important source of funding for businesses.

Risk and return must be carefully considered when determining whether debt or equity finance is used. For example, there is a greater level of risk associated with borrowing, and consideration has to be given to the impact of borrowing on the future profitability and financial stability of the business. Some advantages and disadvantages of debt finance are shown in table 14.1.

BizFACT

If a business uses a high level of debt finance it takes a greater risk than if it uses equity finance. The amount of risk is affected by how much the business has borrowed, when loans have to be repaid and the required level of current assets for the business. The higher the risk of an investment, the higher the return to the business. Risk and return are interrelated and determine what makes up the share prices of corporations.

TABLE 14.1 Advantages and disadvantages of debt finance

Advantages of debt	Disadvantages of debt
• Funds are usually readily available and can be acquired at short notice.	• There is an increased risk if debt comes from financial institutions because interest, bank charges and government charges may increase.
• Increased funds should lead to increased earnings and profits.	• Security is required by the business.
• Interest payments are tax deductible.	• Regular repayments have to be made.
• Flexible payment periods and types of debt are available.	• Lenders have first claim on any money if the business ends in bankruptcy.
• It will not dilute the current ownership in the business.	• Debt can be expensive, e.g. interest must be paid.

14.3.2 Equity finance

In the case of equity finance, shareholders' funds represent the highest proportion of total funds to finance business operations and assets. Equity finance is the most important source of funds for companies because it remains in the business for an indefinite time, because funds do not have to be repaid at a set date as with debt financing. Equity is generally safer than debt, but equity requires sufficient profits to be made so that the business can continue to operate. Equity funds provide confidence to creditors and lenders, who are more willing to lend to a business if there are equity funds. They act as a safety net for unexpected downturns or changes in the business's activities. The advantages and disadvantages of equity finance are shown in table 14.2.

TABLE 14.2 Advantages and disadvantages of equity finance

Advantages	Disadvantages
Does not have to be repaid unless the owner leaves the business	Lower profits and lower returns for the owner
Cheaper than other sources of finance as there are no interest payments	The expectation that the owner will have about the return on investment (ROI)
The owners who have contributed the equity retain control over how that finance is used	Long, expensive process to obtain funds this way
Low gearing (uses resources of the owner and not external sources of finance)	Ownership is diluted, i.e. the current owners will have less control
Less risk for the business and the owner	

When deciding which type of finance to use, businesses will firstly compare debt with equity finance (see table 14.3) and then take into account what the finance is needed for: its purpose. That is, they must match the terms and sources of finance to business purpose.

TABLE 14.3 Comparison of debt and equity finance

Debt	Equity
• Lenders have prior claim in the event of liquidation.	• Shareholders have a residual claim on assets.
• Debt must be repaid by periodic repayments.	• Equity has no maturity date.
• Interest payments are tax deductible.	• Dividends are not tax deductible.
• Lenders usually require a lower rate of return.	• Shareholders require higher return due to higher risk.
• Interest payments are fixed.	• Dividend payments are not fixed and may be reduced through lack of funds.
• Debt providers have no voting rights.	• Equity holders have voting rights.

BizFACT

According to the ABS in 2017–18, the most common types of finance obtained by small businesses were new credit cards and bank overdrafts.

FIGURE 14.6 According to the Australian Banking Association, SMEs are very reluctant to seek debt financing. In 2017–18 only 12 per cent of micro businesses sought finance, compared with 20 per cent of small businesses, 23 per cent of medium-sized businesses and 34 per cent of larger businesses.



SNAPSHOT

Case study: Flowrite Plumbing — self-financing a business



No matter what line of business you go into, you will need start-up capital to get your business going. While many entrepreneurs use some form of debt to finance their operations, self-financing is also commonly used by some business owners. This is where entrepreneurs invest their own money into the business without external help or credit. This is often referred to as 'bootstrapping', from the famous saying about pulling yourself up by your bootstraps.

After many years of experience in the plumbing industry, Anthony Daoud and John Franji decided to take the risk of starting their own business. They began Flowrite Plumbing in 2015. Rather than get a loan, they both decided to save up and use their own funds to pay for their establishment costs.

> 'If you have the resources to do it, you will benefit from complete financial and creative control over your business. You don't have to worry about periodic loan repayments, interest or creditors chasing you for money, especially if it takes a while for your business to start generating a positive cash flow. It's also very hard to get funding when you're starting out and don't have a history. We didn't want to waste time putting together a formal glossy business plan to convince lenders to give us money and we didn't want to use our personal assets as security and put our personal assets at risk. Funding the business yourself means that you get to keep all the profits. The only disadvantage is that your budget and growth is dictated by your own personal finances.'

In the beginning, they each contributed just over $10 000 each, which they used to pay for tools, computers, office equipment and two vans. They distributed payments for other expenses, such as workers compensation and car insurance, and set up monthly repayments. They then waited until they started to have a positive cash flow to purchase more items, for example, they bought more tools, uniforms and signage with the cash that was generated from retained profits.

> 'If you fund a business yourself, you're forced to live within your means and you only purchase things like new equipment etcetera when you're sure you can afford them. It ensures you keep your business operating at a sustainable level and since it's your own money, you tend to be more careful and avoid excessive spending.'

The only form of short-term debt they use is trade creditors to purchase materials. Trade credit is an agreement between the supplier and the business which allows a business to delay payment for goods and services that have already been delivered. They use four different suppliers for their materials who each give them 30 days' credit. John and Anthony use this source of finance to better manage their cash flow. They purchase the materials they need for a job on credit and then give their customers only 14 days to pay them. This ensures they are paid before their own repayments are due to their suppliers, meaning they don't have to use any of their own money to make the repayments.

KEY IDEAS

- Finance for a business can come from either external or internal sources.
- External (or debt finance) is a liability as it is owed to sources external to the business. Equity finance relates to internal sources of finance.
- Most businesses have a combination of both internal and external finance.
- Although repayments of interest to an external provider of funds are costs to the business, debt finance can be attractive as it is readily available and interest payments can be tax deductible.
- Equity finance is the most important source of funds for a business as it remains in the business for an indefinite time and does not need to be repaid on a set date.

14.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

14.3 Quick quiz on	14.3 Exercise	14.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 5	1, 3, 4, 6, 7	8

14.3 Exercise

Revision

1. **Distinguish** between debt and equity finance.
2. **Clarify** the relationship between risk and the source of finance.
3. **To what extent** do the advantages outweigh the disadvantages with regard to (a) debt finance and (b) equity finance?
4. **Why** is equity finance considered the least risky source of funds for companies?

Read the 'Flowrite Plumbing — self-financing a business' case study and answer questions 5 to 7.

5. **Define** bootstrapping.
6. **Discuss** self-financing.
7. **Explain** trade credit.

Extension

8. Miguel operates a small graphic art business from home, but, with increased business activity, he is ready to expand into larger premises. He anticipates he will need $100 000 for the expansion. **Explain** to Miguel, in an email, the risk and return factors involved in expanding his business.

14.3 Exam questions

Question 1 (6 marks)

Source: HSC 2019 Business Studies Exam, Section II, Q22b & c

a. Explain ONE advantage of debt financing. **(3 marks)**
b. Explain ONE disadvantage of equity financing. **(3 marks)**

Question 2 (1 mark)

Source: HSC 2008 Business Studies Exam, Section I, Q16

Which of the following best matches source of finance to business purpose?

A. Increasing bank overdraft to buy a delivery van
B. Applying for a government grant to pay creditors
C. Using retained earnings to expand into new markets
D. Selling accounts receivable to replace furniture and fittings

Question 3 (1 mark)

Which of the following is an advantage of debt finance?

A. Usually quick to organise
B. Reduces gearing
C. Always improves liquidity
D. Helps efficiency

Question 4 (4 marks)

A farmer wishes to purchase another property. He would like to understand the differences between debt and equity finance. Compare debt and equity finance.

More exam questions are available in your learnON title.

14.4 Matching the terms and source of finance to business purpose

SYLLABUS LINK In this subtopic you will learn about matching the terms and source of finance to business purpose.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Small businesses regularly face a number of decisions related to achieving their financial objectives; for example, the purchase of new equipment, stock and premises. Small businesses must find the source of finance that is most appropriate to fund the activities arising from these decisions.

BizFACT

Small businesses have a number of sources available when seeking debt finance, but the range of sources is not as great as with larger businesses because lenders are concerned about risk and security. The larger the equity capital on a business, the more secure the financial structure of the business and the more likely will be the opportunities to borrow. Lenders prefer to lend to firms with strong equity capital because this is an indication of the stability of the business and the commitment of the owners.

The terms of finance must be suitable for the purpose for which the funds are required. The use of short-term finance to fund long-term assets, for example, causes financial problems because the amount borrowed must be repaid before the long-term assets have had time to generate increased cash flow. The use of long-term finance to fund short-term situations or assets means the business is still paying the mortgage long after the situation is resolved or the stock has been sold, and profits will be reduced.

Therefore, finance managers should match the length or term of the loan with the economic lifetime of the asset the finance is being used to purchase. This means that short-term finance should be used to purchase short-term assets and long-term finance should be used for long-term assets. For example, inventory, which is a current or short-term asset, could be purchased with trade credit whereas a new building, which is a non-current asset, should be purchased with a mortgage (see figure 14.7).

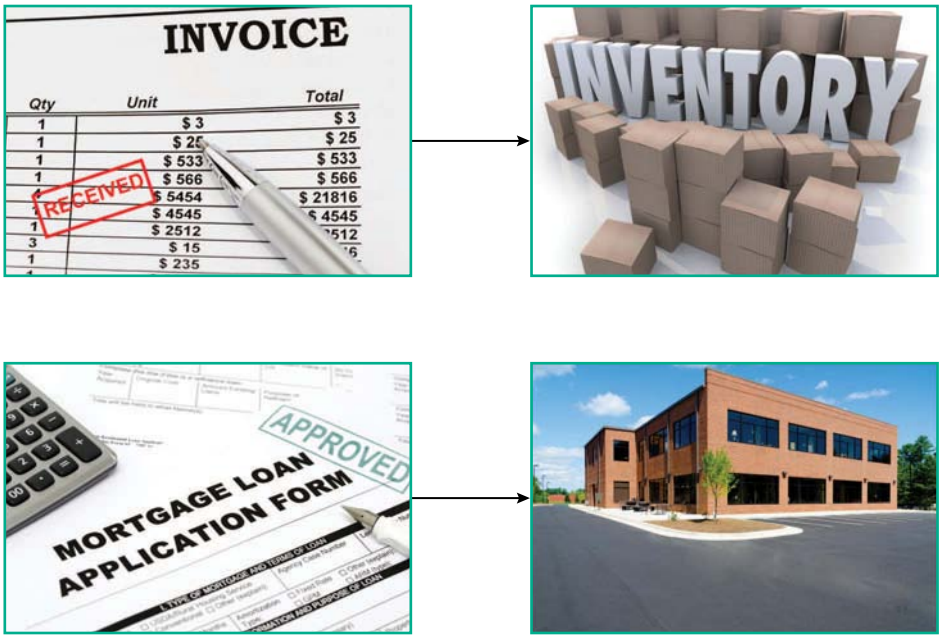
BizFACT

The structure of the business will also influence decisions about finance. For example, companies can raise funds by issuing shares to the public or by issuing debentures, whereas unincorporated businesses cannot.

BizFACT

Availability of finance is affected by a business's credit rating because the credit rating indicates the business's 'track record' in meeting its financial commitments. The higher the credit rating, the greater number of available sources. Banks are more willing to supply funds for businesses with a high credit rating.

FIGURE 14.7 When matching the terms and sources of finance to business purpose, finance managers should use short-term finance for short-term assets and long-term finance for long-term assets.



KEY IDEAS

- Businesses must find the source of finance that is most appropriate to fund their activities.
- When a business identifies and plans to meet its financial objectives, it is necessary to match the terms of finance with its purpose.
- This means that short-term finance should be used to purchase short-term assets and long-term finance should be used for long-term assets.
- Finance managers should match the length or term of the loan with the economic lifetime of the asset the finance is being used to purchase.

14.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

14.4 Quick quiz on	14.4 Exercise	14.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
5	1, 2, 3, 4	6

14.4 Exercise

Revision

1. **Why** is it important to match the term of a loan to the life of the asset for which the finance was obtained?

2. **Recommend** the type of finance, debt or equity, you would suggest for the following. **Justify** your answer.
   a. Payment of inventory
   b. Purchase of a new motor vehicle
   c. Diversification of the business over the next five years
   d. Takeover of a competitor
   e. Expansion to double the volume of sales
   f. Purchase of new plant and equipment

Extension

3. Using information from websites, magazines, banks and other financial institutions, collect five advertisements offering different types of finance and funding. **Compare** them under the following headings. Share your results with other class members.

Source	Interest rate	Borrowing limit	Terms	Other advantages

4. **Examine** a range of annual reports and note some examples of the matching of sources of funds to expenditure.
5. **Outline** why using short-term finance to fund long-term assets would be problematic.
6. **Discuss** why long-term finance should be used to purchase non-current assets.

14.4 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q7

In which of the following are both sources of funds appropriate for a business purchasing extra stock before a busy trading period?

A. Debentures and factoring
B. Retained profits and unsecured notes
C. Debentures and bank overdraft
D. Retained profits and bank overdraft

Question 2 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q14

Why would a business choose debentures as a source of funding?

A. To reduce financial risk
B. To provide security over assets
C. To retain ownership and control
D. To obtain cheap, short-term finance

Question 3 (1 mark)

A farmer wishes to buy feed for her animals. Which would be the most appropriate source of finance for the farmer?

A. Debentures
B. Commercial bills
C. Increase existing mortgage
D. Unsecured notes

More exam questions are available in your learnON title.

14.5 Monitoring and controlling

SYLLABUS LINK In this subtopic you will learn about monitoring and controlling finance, including cash flow statements, income statements and balance sheets.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The process of monitoring and controlling is essential in all aspects of business functions, especially in the processes of financial management. This is because inconsistent methods of review and systems of control will have an immediate impact on the viability of the business and requires managements to monitor the internal and external factors that will impact financially on business operations. This may include changes to the economic outlook, internal production methods and changes to workplace laws.

The main financial controls used for monitoring include:

1. cash flow statements
2. income statements
3. balance sheets.

cash flow statement a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time

These statements indicate how effectively finance is being used in a business. They also provide information on whether the business has sufficient funds to meet unforeseen circumstances.

14.5.1 Cash flow statements

A **cash flow statement** is one of the key financial reports that are part of effective financial planning. It provides the link between the income statement and balance sheet, as it gives important information regarding a firm's ability to pay its debts on time.

The cash flow statement indicates the movement of cash receipts and cash payments resulting from transactions over a period of time. It can also identify trends and can be a useful predictor of change.

Users of cash flow statements include creditors and lenders of finance, as well as owners and shareholders, who can assess the ability of the business to manage its cash. Potential shareholders check that a business has had positive cash flows over a number of years. A fluctuating pattern of cash flows might point to difficulties in the business.

FIGURE 14.8 Cash flow is important because a business needs cash as payment for goods and services that ensures the business continues to operate. Without cash flow, a business would be unable to maintain payments to creditors and to ensure that other obligations, such as wages, utilities expenses and tax, can be covered. According to statistics released by ASIC, 49 per cent of small businesses that failed stated that inadequate cash flow was the driving factor.



Cash flows can be a better predictor of a business's status than profitability. A statement of cash flows can show whether a firm can:

- generate a favourable cash flow (inflows exceed outflows)
- pay its financial commitments as they fall due — for example, interest on borrowings, repayment of borrowings, accounts payable
- have sufficient funds for future expansion or change
- obtain finance from external sources when needed
- pay drawings to owners or dividends to shareholders.

In preparing a cash flow statement, the activities of a business are generally divided into three categories — operating, investing and financing activities.

Operating activities are the cash inflows and outflows relating to the main activity of the business — that is, the provision of goods and services. Income from sales (cash and credit) make up the main operating inflows plus dividends and interest received. Outflows consist of payments to:

- suppliers
- employees
- other operating expenses (insurance, rent, advertising, etc.).

Investing activities are the cash inflows and outflows relating to the purchase and sale of non-current assets and investments. These assets and investments are used to generate income for the business. Examples include the selling of an old motor vehicle, purchasing new plant and equipment or purchasing property.

Financing activities are the cash inflows and outflows relating to the borrowing activities of the business. Borrowing inflows can relate to equity (issue of shares or capital contribution from owner) or debt (loans from financial institutions). Cash outflows relate to the repayments of debt and cash drawings of the owner or payments of dividends to shareholders.

A cash flow statement is usually prepared from the income statement and balance sheet, as these summarise the transactions of the business. Remember that only cash transactions are included in the cash flow statement. An example of a cash flow statement is given in figure 14.9.

FIGURE 14.9 An example of a cash flow statement. Brackets ( ) are used to show cash payments.

Burgess Enterprises Ltd
Cash Flow Statement for year ended 30 June 2021

Cash flows from operating activities	
Receipts from customers	30 000
Payments to suppliers and employees	(25 000)
Dividends received	4 000
Interest received	8 000
Interest paid	(5 500)
Net cash provided by operating activities	11 500
Proceeds from sale of assets	85 000
Payment of plant and equipment	(150 000)
Net cash from investing activities	(65 000)
Cash flows from financing activities	
Proceeds from issues of shares	90 000
Proceeds from borrowings	40 000
Repayments of borrowings	(15 000)
Dividends paid	(25 000)
Net cash from financing activities	90 000
Net increase in cash	36 500
Cash at the beginning of the reporting period	15 000
Cash at the end of the reporting period	51 500

Add all the cash receipts from operating activities and subtract the cash payments.

Add all the cash receipts from investing activities and subtract the cash payments.

Add all the cash receipts from financing activities and subtract the cash payments.

Add net cash provided from operating activities + net cash provided from investing activities + net cash provided from financing activities.

Cash at beginning of year + net increase in cash (this amount will then become the new 'cash at the beginning of the year' for the next period).

14.5.2 Income statements

The **income statement** is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.

The income statement shows:

- operating income earned from the main function of the business, such as sales of inventories, services and non-operating revenue earned from other operations, such as interest, rent and commission
- operating expenses such as purchase of inventories, payment for services and other expenses incurred in the main operation of the business, such as advertising, rent, telephone and insurance.

The difference between the income and expenses is the profit or — if expenses exceed income — the loss. The first step in completing a statement of financial performance is to record the income earned by a business. A café, for example, earns income by selling food and drinks. The second step is to record the **cost of goods sold**, which is the money spent on purchases of raw materials or finished goods for resale, and to use this figure to calculate **gross profit**. The gross profit/loss is the amount remaining when the cost of goods sold is deducted from revenue. The third step is to calculate **net profit**. The word 'net' means all expenses have been deducted. A net profit/loss is the amount remaining when operating expenses are deducted from gross profit.

To earn revenue, a business will have a variety of **expenses**. Common expenses include wages and salaries, payments for telephone, electricity, postage, motor vehicle expenses and so on. Expenses can be broken down into three types, which are shown in table 14.4.

income statement a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.

cost of goods sold the value of stock that a business has sold to its customers

gross profit that part of a business's profit that represents operating income minus cost of goods sold

net profit the difference between the gross profit and expenses

expenses the costs incurred in the process of acquiring or manufacturing a good or service to sell and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service

TABLE 14.4 Income statement (or statement of financial performance) expense breakdown by type

Expenses*		
Selling	**Administrative**	**Financial**
• Commission • Salaries • Wages • Advertising • Delivery expenses • Electricity • Depreciation on shop fittings	• Stationery • Office salaries • Rent • Rates • Telephone • Depreciation on buildings • Audit fees • Accountant's fees • Insurances	• Interest payments • Lease payments • Dividends • Insurance payments
Selling expenses:	Costs related to the process of selling the good or service; can be directly traced to the need for sales	
Administration expenses:	Costs directly related to the general running of the business	
Finance expenses:	Costs associated with borrowing money from outside people or organisations and to minimising business risk	

*Costs of goods sold (COGS): this expense includes *only* the cost of stock sold and is shown separately in the income statement (or statement of financial performance).

An example of an income statement is given in figure 14.10.

FIGURE 14.10 An example of an income statement/revenue statement/profit and loss statement

Can also be referred to as Sales or Revenue. This represents the total value of all the goods/services sold.

Gross profit = Operating income/Sales – COGS

COGS = Opening stock + Purchases – Closing stock

Income Statement
for the year ended 30 June 2021

	2019 $	2020 $	2021 $
Operating income	81 200	83 500	78 800
Cost of goods sold			
Opening inventory	11 280	11 300	11 240
Purchases	53 000	55 200	48 000
	64 280	66 500	59 240
Closing inventory	11 300	11 240	11 100
	52 980	55 260	48 140
Gross profit	28 220	28 240	30 660
Expenses			
Selling	7 800	9 200	8 900
Administrative	4 400	4 400	7 000
Interest	3 000	3 500	3 000
	15 200	17 100	18 900
Operating profit before tax	13 020	11 140	11 760
Tax	4 500	3 900	4 100
Operating profit after tax	8 520	7 240	7 660
Extraordinary items (after tax)	4 300	4 600	3 900
Operating profit and extraordinary items after tax	12 820	11 840	11 560
Retained profits (1 July)	25 000	31 000	35 000
	37 820	42 840	46 560
Dividends paid	3 400	2 900	3 800
Retained profits (30 June)	34 420	39 940	42 760

Retained/Net profit = Gross profit – Expenses

By examining figures from previous income statements, managers can make comparisons and analyse trends before making important financial decisions. They can see whether expenses are increasing, decreasing or remaining the same, why profits have increased or decreased and in which areas there has been significant change.

BizFACT

The income statement shows the operating efficiency of the business. It can be used to answer the following questions:

- Is income high enough to cover expenses?
- Is the mark-up on purchases sufficient?
- Is the business making a good profit?
- Are the expenses in proportion to the revenue they are earning?
- Is inventory turnover appropriate for the business?

14.5.3 Balance sheets

A **balance sheet** represents a business's assets and liabilities at a particular point in time and represents the net worth (equity) of the business. It shows the financial stability of the business. The balance sheet is prepared at the end of the accounting period.

Typical items included in a balance sheet include the following.

- **Assets** are items of value owned by the business. Assets can be divided into:
  - *Current assets* — assets that a business can expect to use up, or turn over, within 12 months, e.g. cash, accounts receivable (debtors) and inventory (stock)
  - *Non-current assets* — those assets that have an expected life of longer than 12 months, e.g. land, buildings, machinery, vehicles, furniture, fixtures and fittings.
- **Liabilities** are items of debt owed to outside parties. Liabilities can be divided into:
  - *Current liabilities* — those debts which are expected to be repaid in less than 12 months, e.g. overdraft and accounts payable (creditors)
  - *Non-current liabilities* — long-term items of debt, e.g. mortgage, debenture.
- **Owners' equity** is the funds contributed by the owner(s) and represents the net worth of the business. Owners' equity can be comprised of capital (funds contributed by the owner/s) and retained profits.

An example of a balance sheet is given in figure 14.11.

The balance sheet shows the financial stability of the business. Analysis of the balance sheet can indicate whether:

- the business has enough assets to cover its debts
- the interest and money borrowed can be paid
- the assets of the business are being used to maximise profits
- the owners of the business are making a good return on their investment.

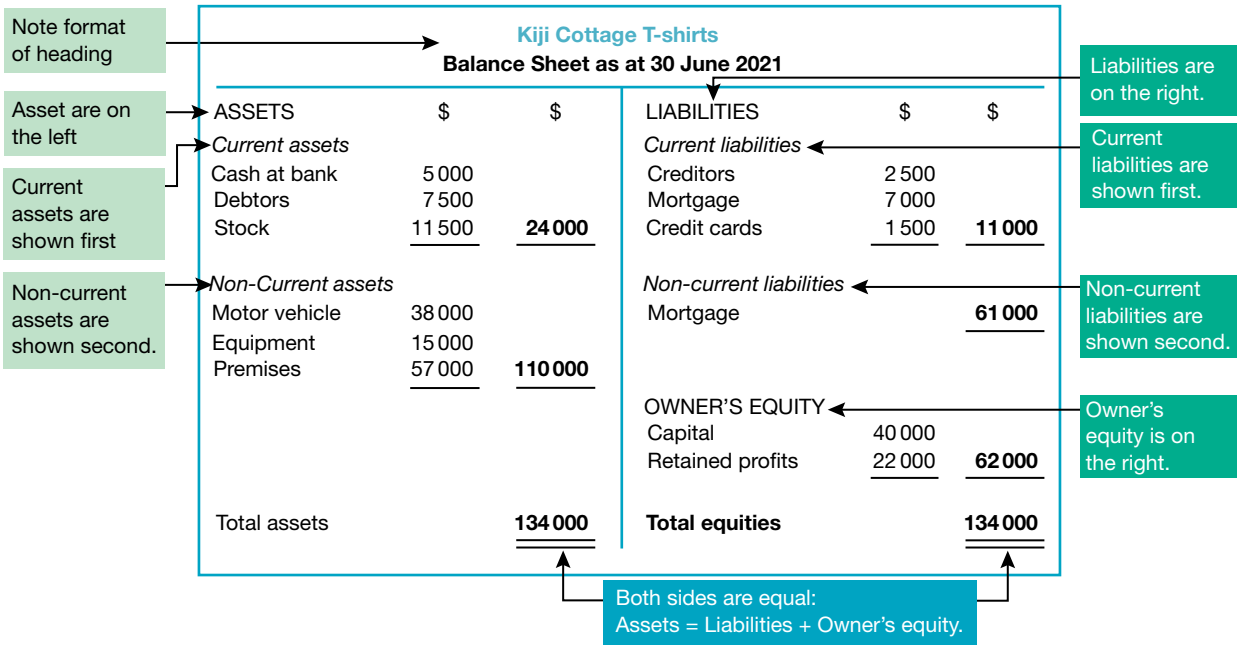
balance sheet a summary of a business's assets and liabilities at a particular point in time, expressed in money terms; represents the net worth of the business

assets items of value owned by a business

liabilities items of debt owed to outside parties

owners' equity the funds contributed by the owner(s); represents the net worth of the business

FIGURE 14.11 An example of a balance sheet



Kiji Cottage T-shirts
Balance Sheet as at 30 June 2021

ASSETS	$	$	LIABILITIES	$	$
Current assets			*Current liabilities*		
Cash at bank	5 000		Creditors	2 500	
Debtors	7 500		Mortgage	7 000	
Stock	11 500	**24 000**	Credit cards	1 500	**11 000**
Non-Current assets			*Non-current liabilities*		
Motor vehicle	38 000		Mortgage		**61 000**
Equipment	15 000				
Premises	57 000	**110 000**			
			OWNER'S EQUITY		
			Capital	40 000	
			Retained profits	22 000	**62 000**
Total assets		**134 000**	**Total equities**		**134 000**

The balance sheet shows the return on the owners' investment, the sources and extent of borrowings, the level of inventories, and so on. The figures also show whether the business has sufficient assets to continue to make profits in the longer term, how much of the assets are financed from outside borrowings, whether the business can expect to meet its financial obligations in the short and longer term, and how the year's figures compare with the previous year.

It is important that the presentation of figures in the balance sheet allows clear interpretation so that interested parties can draw meaningful conclusions and make important decisions about the business. Figures from previous years' balance sheets can also be analysed and presented to show the decision makers the trends and changes in the business that need to be investigated.

An example of a comparative balance sheet is given in figure 14.12.

FIGURE 14.12 An example of a comparative balance sheet

Balance Sheet as at 30 June 2021

	Consolidated	
	2020 $m	**2021 $m**
Current Assets		
Cash	4.8	20.6
Accounts receivable	102.0	81.6
Investments	14.9	-
Inventories	36.0	31.5
Total Current Assets	157.7	133.7
Non-current Assets		
Receivables	59.3	64.7
Investments	284.7	293.5
Inventories	17.3	79.5

(continued)

FIGURE 14.12 An example of a comparative balance sheet *(continued)*

Balance Sheet as at 30 June 2021		
Property, plant and equipment	831.4	882.9
Intangibles	5.1	5.6
Total Non-current Assets	1197.8	1326.2
Total Assets	1355.5	1459.9
Current Liabilities		
Creditors and borrowings	190.0	118.2
Provisions	59.6	51.7
Total Current Liabilities	249.6	169.9
Non-current Liabilities		
Creditors and borrowings	238.7	417.6
Provisions	210.2	208.4
Total Non-current Liabilities	448.9	626.0
Total Liabilities	698.5	795.9
Owners' Equity		
Capital	132.3	182.7
Reserves	228.3	235.1
Retained profits	161.9	111.7
Equity attributable to owners of the chief entity	522.5	529.5
Reserve account	134.5	134.5
Total owners' equity	657.0	664.0

Balance sheet — the accounting equation and relationships

The **accounting equation**, which forms the basis of the accounting process, shows the relationship between assets, liabilities and owners' equity.

accounting equation a equation that shows the relationship between assets, liabilities and owners' equity, which forms the basis of the accounting process

Assets are what is owned by a business; liabilities and owners' equity are what is owed by a business. The business and the owner are separate; therefore, owners' equity is what is to be repaid (hopefully with increased profits) by the business to the owner. The accounting equation shows that the assets of the business may be financed by either the owners or by parties external to the business.

The balance sheet shows the outcome of the accounting process. The accounting equation can be represented in different ways but, because it is an equation, it must always be equal.

$$\text{Assets} = \text{Liabilities} + \text{Owners' equity}$$
$$\text{Owners' equity} = \text{Assets} - \text{Liabilities}$$
$$\text{Liabilities} = \text{Assets} - \text{Owners' equity}$$

The balance sheet can be displayed in different forms to show the different ways of expressing the accounting equation. In the first example (figure 14.13), the balance sheet represents the accounting equation Assets = Liabilities + Owners' equity.

FIGURE 14.13 A balance sheet showing Assets = Liabilities + Owners' equity

Balance sheet as at 30 June 2021

	$	$		$	$
Current Assets			**Current Liabilities**		
Cash	30 400		Accounts payable		82 000
Inventories	4 100		**Non-current Liabilities**		
Accounts receivable	58 000	92 500	Loan	25 000	25 000
Non-current Assets			**Owners' Equity**		
Plant and equipment	68 000		Capital	100 000	
Land and buildings	85 000	153 000	Net profit	38 000	138 500
		$245 500			**$245 500**

BizFACT

It is important to remember that the accounting entity assumption means that financial information records for a business are kept separate from those of the owner.

KEY IDEAS

- Monitoring and controlling is essential for maintaining business viability, and affects all aspects of business operations — especially financial management.
- The main financial controls used for monitoring include cash flow statements, income statements and balance sheets.
- A cash flow statement provides the link between the income statement and the balance sheet. It provides information about a firm's ability to pay its debts on time.
- The cash flow statement specifically records the movement of cash receipts and cash payments that result from transactions over a given time, for example a month.
- Creditors, lenders, owners and shareholders all use a cash flow statement to assess the ability of the business to manage its cash and identify trends in cash flow over time.
- The income statement is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.
- Profit is the difference between revenue and expenses.
- A balance sheet represents a business's assets and liabilities at a particular point in time, expressed in money terms, and represents the net worth of the business.
- The accounting equation, which forms the basis of the accounting process, shows the relationship between assets, liabilities and owners' equity.

14.5 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

14.5 Quick quiz on	14.5 Exercise	14.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 3, 4, 5, 9, 11	1, 6, 8, 10, 12, 13, 14, 15, 16, 17, 18	7, 19, 20

14.5 Exercise

Revision

1. **Why** must businesses monitor and control all business functions?
2. **Identify** the three main financial controls.
3. **Identify** three stakeholders who would most likely view a cash flow statement. **Outline** the key information they would be looking for.
4. **Summarise** the three categories of activities of a cash flow statement.
5. **Clarify** the purpose of income statements.
6. If the income statement shows operating efficiency, **explain** the relationship between income and expenses regarding this financial control.
7. Answer the questions using the balance sheet below.

Balance sheet of Biq & Son as at 30 June 2021			
Current Assets		**Current Liabilities**	
Cash at bank	3 000	Accounts payable	9 500
Inventories	2 500	**Non-Current Liabilities**	
Accounts receivable	8 500	Loan	50 000
Non-Current Assets			
Furniture	2 500	**Owners' Equity**	
Vehicle	16 500	Capital	100 000
Land and buildings	140 000	Profit	13 500
	173 000		173 000

   a. **Explain** why the balance sheet is written 'as at 30 June 2021'.
   b. **State** who the business owners are and what their original investment was.
   c. **What** is the value of the owners' investment on 30 June 2021?
   d. **Propose** how the assets of the business were financed.
   e. **Determine** how much is owed by the business.
   f. **Recommend** how the business will pay its debts.
   g. Would you offer credit to this business? **Justify** your response.
8. **Distinguish** between a balance sheet and an income statement.
9. **Outline** the difference between an asset and a liability.

10. Your friends Tony and Yung have a small business making novelty party accessories. They have been running the business for three months and it appears to be going well. They want to know if they are making a profit or a loss. You agree to help them. They provide you with the following information. **Construct** an income statement to **calculate** their profit or loss.
    - Raw materials and supplies to make the novelties cost them $2000.
    - At the end of the month they still have $700 worth of raw materials and supplies.
    - During the month, they sold 1000 of their novelty products for $5 each.
    - They paid their friends Sandy and Max $300 to help them.
    - They sent flyers to department stores advertising their product, and this cost them $220.
    - They paid the telephone bill ($340) and courier for delivery ($90).
11. **Identify** the most appropriate terms to complete the following accounting equation.
    Assets = _____+ _____
12. **Why** is the accounting equation important?
13. **Calculate** the missing amounts in the following table (financial year is 1 July–30 June).

	Business A	Business B	Business C
Assets 1 July	275 000	221 000	–
Liabilities 1 July	135 000	–	353 000
Owners' Equity 1 July	–	114 000	206 000
Assets 30 June	293 000	–	481 000
Liabilities 30 June	141 000	153 000	–
Owners' Equity 30 June	–	189 000	242 000
Sales	484 000	521 000	–
Cost of goods sold	385 000	–	292 000
Gross profit	–	174 000	145 000
Expenses	–	135 000	105 000
Net profit	39 000	–	–

14. Using the information from question 13, answer the following questions. **Justify** your answers.
    a. Which owner is making the highest gross profit?
    b. Which owner is making the highest net profit?
    c. In which business would you invest and why?
    d. In what information would employees be interested?
    e. Each business has applied for a loan of $50 000 from a bank. Which business is most likely to be successful in their application?
15. Given the following information for July 2021, **construct** a cash flow statement for Eat Well Pty Ltd.

Closing cash balance at end of June	$15 400
Monthly wages	$ 3 200
Weekly rent	$ 500
Fortnightly loan repayment	$ 550
Proceeds from issue of shares	$75 650
Receipts from customers	$32 440
Payments to suppliers	$ 5 800
Interest received	$ 2 600
Proceeds from sale of equipment	$18 700
Dividends paid	$24 000

16. **Calculate** the value of purchases, the gross profit, cartage (expenses related to freight, loading and unloading) and net profit for the income statement below.

Income Statement for the year ended 30 June 2021		
	$	$
Operating income		258 400
Cost of goods sold		
Opening inventory	57 300	
Purchases	–	
Closing inventory	12 700	154 500
Gross Profit		–
Expenses		
Selling:		
– Advertising	22 300	
– Cartage	–	
Administrative		
– Rent	14 000	
– Insurance	3 000	
Financial		
– Bad debts	2 200	50 200
Net Profit		–

17. Using the balance sheet below, **calculate** the value of Total Non-Current Assets, Debtors and the Mortgage.

Balance sheet as at 30 June 2021			
	$		$
Current Assets		**Current Liabilities**	
Cash	7 800	Creditors	2 500
Debtors	–	Overdraft	4 670
Stock	17 600	Credit cards	4 750
Total Current Assets	28 650	**Total Current Liabilities**	11 920
Non-Current Assets		**Non-Current Liabilities**	
Property	579 460	Mortgage	–
Equipment	8 600		
Total Non-Current Assets	–	**Total Non-Current Liabilities**	
		Owner's Equity	
		Capital	53 000
	–	Retained profits	75 340
Total Assets	6 16 710	**Total Owner's Equity**	128 340

Extension

18. Financial management is concerned not so much with what has happened in the past but with what is going to happen in the future. **Discuss** this statement.
19. Examine the financial reports of a number of businesses. Identify for which business you would be most interested in working. **Determine** what other information you might need to help you make a decision.

20. **Create** a list of questions to which the following groups of people might seek answers from a business. The first one is done for you.

Group	Questions
Creditors	Is your cash flow sufficient to pay your account on time?
Bank	
Employee	
Owner	
Investor	
Customer	

14.5 Exam questions

Question 1 (1 mark)

Source: Adapted from HSC 2017 Business Studies Exam, Section I, Q20

The table shows information supplied by a business.

Sales	?
Cost of goods sold	?
Gross profit	4 00 000
Expenses	?
Net profit	?
Gross profit ratio (gross profit ÷ sales)	66.7%
Net profit ratio (net profit ÷ sales)	50%

Which of the following options shows the sales and net profit for this business?

A. Sales: $66 700, Net profit: $50 000
B. Sales: $200 000, Net profit: $100 000
C. Sales: $600 000, Net profit: $200 000
D. Sales: $600 000, Net profit: $300 000

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q11

Balance Sheet for Steve's Lawn Services as at 30 June 2016

Current assets	$	*Current liabilities*	$
Cash	15 000	Accounts payable	5 000
Accounts receivable	3 000	Overdraft	5 500
Stock	?		
Non-current assets		*Non-current liabilities*	
Plant and equipment	40 000	Long-term loan	100 000
Goodwill	85 000		
		Total equity	
		Capital	22 700
		Net profit	12 800

Industry standard current ratio: 1.9: 1

If Steve is a sole trader, how much equity does he have in the business?

A. $12 800
B. $35 500
C. $135 500
D. $146 000

Question 3 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q10

The table shows cash flow information for a business.

	Jan	Feb	March	April
Opening balance ($)	4000			
Cash in ($)	20000	20000	20000	24000
Cash out ($)	14000	50000	24000	26000

What is the opening cash balance for April?

A. –$24 000
B. –$18 000
C. –$16 000
D. –$12 000

Question 4 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q10

Which of the following would be found on an income statement?

A. Accounts payable
B. Gross profit
C. Intangibles
D. Net assets

Question 5 (2 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q24ai & ii

The table shows an extract from a cash flow statement for a business.

	Jan	Feb	March	April	May	June
Cash in ($)	6000	5000	3000	2000	4000	3000
Cash out ($)	3000	3000	8000	8000	3000	2000

The opening cash balance for January is $5000.

a. Calculate the opening cash balance for March. **(1 mark)**
b. In which month did the business start with a negative cash balance? **(1 mark)**

More exam questions are available in your learnON title.

14.6 Financial ratios

SYLLABUS LINK In this subtopic you will learn about financial ratios, including:

- liquidity — current ratio (current assets ÷ current liabilities)
- gearing — debt to equity ratio (total liabilities ÷ total equity)
- profitability — gross profit ratio (gross profit ÷ sales); net profit ratio (net profit ÷ sales); return on equity ratio (net profit ÷ total equity)
- efficiency — expense ratio (total expenses ÷ sales), accounts receivable turnover ratio (sales ÷ accounts receivable)
- comparative ratio analysis — over different time periods, against standards, with similar businesses.

You will also learn to assess business performance using comparative ratio analysis.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Many important questions cannot be answered by simply 'looking' at the financial statements of a business. Financial statements summarise the activities of a business over a period of time and must be analysed to increase understanding of the implications of those activities.

Analysis is an important part of the accounting process. It involves working the financial information into significant and acceptable forms that make it more meaningful and highlighting relationships between different aspects of a business. Analysis involves comparing similar items in the income statement and balance sheet.

The main types of analysis are vertical, horizontal and trend analysis.

- Vertical analysis compares figures within one financial year; for example, expressing gross profit as a percentage of sales and comparing debt to equity.
- Horizontal analysis compares figures from different financial years; for example, comparing 2020 and 2021.
- Trend analysis compares figures for periods of three to five years.

analysis working financial information into significant and acceptable forms that make it more meaningful, and highlighting relationships between different aspects of a business

interpretation making judgements and decisions using the data gathered from analysis

The methods of analysis involve calculations of figures, percentages and ratios. Ratios are one of the main tools used to analyse financial information and assist in answering more clearly the questions relating to profits, solvency, efficiency, growth and liquidity. But analysis without **interpretation** is meaningless. Interpretation is making judgements and decisions using the data gathered from analysis.

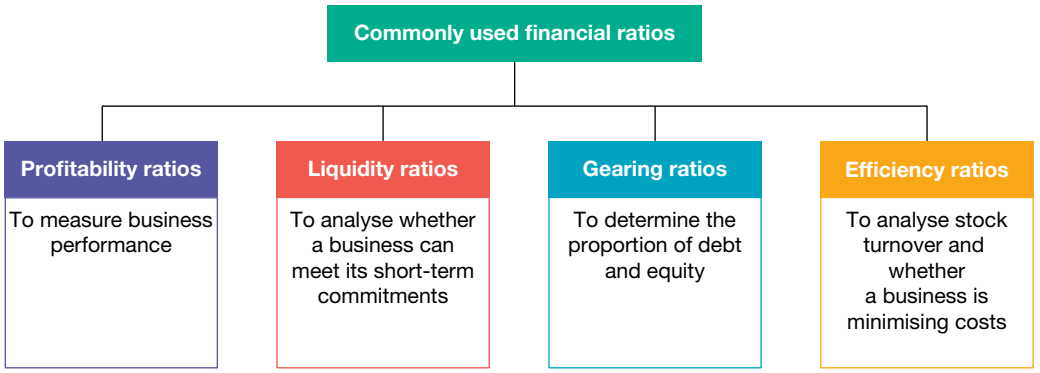
BizFACT

Careful analysis can provide signals regarding the success of the business or impending problems. For example, management may be interested to know:

- how effectively assets have been used in a business
- why an increase in advertising expenses has not generated more sales revenue than anticipated
- why sales have decreased over the past two years
- why overdrafts have continued to increase.

The type of analysis chosen will depend on the reasons that the information is required and the decisions to be made from the information. Users of information may be interested to compare figures, percentages or ratios for departments, different products, different branches or against the industry. They may also wish to monitor trends over a number of years or make comparisons between items within a financial statement, selling expenses and sales. Figure 14.14 summarises the most commonly used financial ratios.

FIGURE 14.14 Commonly used financial ratios



14.6.1 Liquidity

Liquidity is the extent to which the business can meet its financial commitments in the short term, which usually refers to a period of less than 12 months. The business must have sufficient resources to pay its debts and enough funds for unexpected expenses. To assess a business's liquidity, its managers must assess whether the business can pay its debts when they are due. Is there sufficient cash or a level of assets and inventories that can be converted to cash quickly to repay the firm's debts — that is, the firm's accounts payable, interest and loans?

The holding of outstanding debts means the business has less cash to earn revenue. The quicker the firm receives cash from its accounts receivable, the quicker those funds can be used to earn revenue. Current assets and current liabilities determine the liquidity or short-term financial stability of a business. The firm must be careful to ensure that it has enough current assets that could be used to generate cash quickly, but not so much that the resources are not being used for producing revenue.

There are a number of ratios to show liquidity (short-term financial stability), calculated from balance sheet figures. An example is the current ratio (or working capital ratio).

liquidity the extent to which a business can meet its financial commitments in the short-term (less than 12 months)

BizFACT

Current assets and current liabilities determine the liquidity or short-term financial stability of a business.

Current ratio (working capital)

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

The current ratio measures a business's ability to pay back its current liabilities with its current assets. The higher the current ratio, the more capable the business is of meeting its short-term obligations.

It is generally accepted that a ratio of 2:1 indicates a sound financial position for a firm. That is, the firm should have double the amount of current assets to cover its current liabilities. However, an 'acceptable' ratio will also depend on a number of factors, such as the type of firm, how other firms in the industry are operating and factors in the external environment (see the following BizFACT). In other words, the current ratio gives only a limited indication of the ability of the business to meet its short-term liabilities. The nature and composition of current assets may vary considerably. While low values for the current ratio indicate that a business may have difficulty

meeting its short-term obligations, if the current ratio is too high, this indicates that the business may be using its current assets inefficiently. For instance, the business may have a lot of cash that could be put to better use. A high current ratio may also indicate problems in working capital management.

FIGURE 14.15 Examples of current ratio

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$
$$= \frac{300\,000}{195\,000}$$
$$= 1.54$$

Comment: This firm has $1.54 of current assets to cover $1 of current liabilities. A ratio of less than **2:1** indicates there are insufficient assets to pay current commitments or liabilities. If this firm has previously operated successfully, it may find a ratio of 1.54:1 acceptable. However, if this is not the case, the firm may have to sell non-current assets to cover liabilities, which will reduce its capacity to earn profits; or it may have to borrow in the short term and incur higher interest repayments. In most instances, a firm would be unwise to allow this ratio to fall below 1.5:1.

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$
$$= \frac{450\,000}{150\,000}$$
$$= 3 : 1$$

Comment: This firm has $3 of current assets for every $1 of current liabilities. This indicates that the firm is in a sound financial position — that is, it is liquid and will be able to pay for its debts in the short term. If the firm has a high demand for its product, for example, food products, there may be reason to reduce the level of its current ratio. Even for a firm that has a low demand, for example, jewellery, its working capital may be too high. Too high a ratio can mean that current assets are not being used fully. Action is needed to ensure that sufficient use is being made of the assets in the business.

A variety of strategies can improve a business's liquidity. Subtopic 15.3 on working capital management examines these strategies in greater detail. Other strategies businesses could use to improve liquidity include factoring, selling non-essential non-current assets and using those funds to reduce current liabilities, or injecting more equity into the business to pay off liabilities.

BizFACT

Many firms operate successfully with current ratios of less than 2:1. Firms that sell finished goods and keep large levels of inventories need a higher ratio than firms selling on credit rather than cash. Large businesses in the food industry, for example, Woolworths, use a lower ratio of approximately 0.6:1. Businesses in service industries, such as doctors and dentists who rely on cash payments for their services, also do not need as high a ratio and operate on ratios of less than 2:1.

14.6.2 Gearing (solvency)

The capital structure of a business is determined by the mix of debt and equity, and the proportion of each is known as gearing (or solvency).

Gearing ratios determine the firm's **solvency** — that is, its ability to meet its financial commitments in the longer term. Potential investors and creditors are interested in gearing ratios, as they show whether the creditors will be paid or whether investors can expect a good return on their money.

Gearing measures the relationship between debt and equity. Gearing is the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. The degree of gearing depends on the type of industry and management of the business. An industry that carries higher risk but is likely to generate large profits (for example, mining) may have a higher debt to equity ratio — that is, it is highly geared. Manufacturing industries with strong markets often have high debt as the potential for profit is greater.

Gearing is an important consideration for businesses as the more highly geared the business (that is, those that have a higher proportion of debt to equity), the greater the risk for the business but the greater potential for profit.

Debt affects stakeholders and potential investors because the high risk involved may discourage investment.

The business's level of gearing is an important decision. Factors such as risk, return and degree of control over the enterprise influence the level of leverage that is appropriate for a business.

In balancing the gearing of a business, consideration must be given to the level of control by owners. For example, profits earned must be sufficient to cover interest payments. If funds are not available to meet interest charges and accounts are not paid, lenders and creditors have the right to claim payment from the business.

There is no optimal level of gearing for a business, although it is rare for a company to have no gearing.
A business must consider:

- return on investment
- cost of debt
- size and stability of the business's earning capacity
- liquidity of the business's assets (the greater the cash flow and the more liquid the assets, the more likely the interest charges will be paid)
- purposes of short-term debt.

A number of ratios show solvency (long-term financial stability), calculated from balance sheet figures. An example is the debt to equity ratio.

FIGURE 14.16 An average debt to equity ratio depends on economic factors and the industry in which a company operates. Most companies on the ASX have a gearing ratio between 0.25 and 0.35.



solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)

gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.

Debt to equity ratio

$$\text{Debt to equity ratio} = \frac{\text{Total liabilities}}{\text{Total equity}}$$

The debt to equity ratio shows the extent to which the firm is relying on debt or outside sources to finance the business. This ratio is an important control aspect for management because the relationship between debt and equity must be carefully balanced. A ratio of greater than 1 means that the business has less equity than debt. A ratio of between 0 and 1 means that the business has more equity than debt.

The higher the ratio, the less solvent the firm. That is, the higher the ratio of debt to equity, the higher the risk. The firm must look carefully at interest rates, business confidence and economic indicators to determine if the balance between debt and equity is appropriate for its particular business or industry. A highly geared firm — a firm that uses more debt than equity — carries more risk with regard to longer term financial stability. Investors would be less attracted to a firm with a higher debt to equity ratio because this indicates a greater financial risk.

SNAPSHOT

Case study: Harvey Norman's gearing strategy

In 2019, Gerry Harvey, the executive chairman of Harvey Norman, anticipated there would be a recession in the near future which would lead to around 10 to 20 per cent of retailers going broke. To ensure his company would not go broke and to help the business be in a strong position in the event of a downturn, Gerry Harvey planned to raise $173 million through a rights issue.



Existing shareholders were offered one new share for every 17 shares they already owned for $2.50 a share, which was a massive 46 per cent discount on the company's current share price at the time of $4.67. Harvey Norman's debt to equity ratio was 19.4 per cent when this offer was made.

The business ended up selling 66 million shares at $2.50 a share which enabled them to raise an extra $165.6 million. Approximately 3 million shares went unsold. The proceeds of the rights issue went towards reducing their debt and better positioning the company for an impending downturn.

To improve a business's gearing, they will need to look at ways of either reducing their debt or increasing equity. In an attempt to decrease debt businesses could sell non-essential assets to pay off their debts, or they could even re-negotiate their loans to spread their payments over a longer period. Alternatively, the business could lease assets as opposed to purchasing them. Strategies to increase equity include retaining more profits, or injecting more equity funding by either selling more shares (if a public company) or inviting new owners.

The type of business will determine how highly geared a business can be. For example, a business that is less influenced by economic fluctuations can be more highly geared. A shop selling essential food items will not be affected by economic downturns so it can carry more debt than a business that sells luxury items.

BizFACT

The financial sector as a whole has one of the highest debt to equity ratios. This is because banks borrow large amounts of funds to then loan large amounts of money. A debt to equity ratio of higher than 2:1 is quite common in this industry. Other industries that have a higher debt to equity ratio are capital-intensive industries, such as large manufacturing companies and the airline industry, who commonly use high levels of debt.

An interesting question is posed by the debt to equity ratio. Should the owners of a business have as much at stake as the creditors (that is, should the ratio be at least 1:1)? Different firms have different financial structures and the attitude of the owners to financial risk determines what levels of debt to equity are appropriate for the business. The debt to equity ratio also has a direct effect on the short-term and immediate solvency of a business. The greater the owners' financial interest in the business, the more solvent in the short term the business is likely to be. Ultimately, the level of solvency in a business reflects its financial structure — that is, its control of debt and equity. This is important for the long-term survival of the business.

FIGURE 14.17 An example of a debt to equity ratio

Balance Sheet for Young's Store as at 30 June 2021

	$	$
Current Assets		
Cash	20 000	
Accounts receivable	50 000	
Inventories	80 000	150 000
Non-current Assets		
Delivery vehicles		50 000
		200 000
Current Liabilities		
Accounts payable		20 000
Non-current Liabilities		
Mortgage		30 000
Owners' Equity		
Capital	140 000	
Add net profit	10 000	150 000
		200 000

$$\text{Debt to equity ratio} = \frac{\text{Total liabilities}}{\text{Owners' equity}}$$
$$= \frac{50\,000}{150\,000}$$
$$= 0.3 : 1 \text{ or } 33\frac{1}{3}\%$$

Comment: The firm has $0.33 in external debt (liabilities) for every $1 of internal debt (owners' equity). A ratio of 1:1 indicates a sound financial position so this company is in a safe position. Depending on the type of firm, the industry and past trends, the firm could possibly increase its rate of external debt.

14.6.3 Profitability

Profitability is the earning performance of the business and indicates its capacity to use its resources to maximise profits. Profitability depends on the revenue earned by a business and the ability of the business to increase selling prices to cover purchase costs and other expenses incurred in earning income. The ability of the business to generate profits is its most important financial objective.

A number of parties are interested in a business's profitability:

- Owners and shareholders want to know whether the firm is earning an acceptable return on their investment.
- Creditors want to know whether they will be paid and should offer credit in the future.
- Lenders want to know whether the principal on the loan and interest will be repaid and whether to lend to the firm in the future.
- Management uses profitability to decide on the need for adjustments to policies.

The amount of profit is determined by a number of factors, such as the volume of sales, the mark-up on purchases and the level of expenses. Financial information must be examined to see where changes have occurred and where changes need to be made in the future.

The income statement is used to measure the profitability or earning capacity of the firm. Three profitability ratios are the:

- gross profit ratio
- net profit ratio
- return on equity ratio.

Gross profit ratio

Gross profit is the difference between sales revenue and the direct cost of goods sold. It represents the amount of sales that is available to meet expenses resulting in net profit. A fall in the rate of gross profit may mean a fall in the amount of net profit. The amount of that decrease depends on such factors as price reductions due to specials or sales, mark-downs on out-of-date stock, theft of stock, errors in determining prices, changes in the mark-up policies or changes in the mix of sales.

The gross profit ratio (shown below) gives the percentage of sales revenue that results in gross profit. It is one way that a business can measure profitability. A business's gross profit must be sufficient to pay the expenses of the business and still provide a profit for the owner. It is important to note that the gross profit ratio is only calculated by businesses that sell stock and not service businesses; that is, it is only used by those businesses that purchase goods from suppliers and sell them at a higher price to customers.

$$\text{Gross profit ratio} = \frac{\text{Gross profit}}{\text{Sales}}$$

The gross profit ratio shows changes from one accounting period to another, and indicates the effectiveness of planning policies concerning pricing, sales, discounts, the valuation of stock and so on. If the ratio is low, alternative suppliers may need to be sourced and competitors investigated. Since all the other expenses incurred by businesses such as wages, electricity and advertising are deducted from the gross profit to determine net profit, the net profit ratio therefore gives a more accurate indication of the profitability of a business.

Net profit ratio

Net profit represents the profit or return to the owners, which is revenue less expenses. For sole traders and partnerships, net profit represents a return on their contribution to the business. It is usual for a company to return part of net profit to shareholders as dividends and retain a part for future expansion.

$$\text{Net profit ratio} = \frac{\text{Net profit}}{\text{Sales}}$$

The net profit ratio shows the amount of sales revenue that results in net profit. The costs or expenses after gross profit must be low enough to generate a net profit. The amount of sales must be sufficiently high to cover the costs or expenses of the firm and still result in a profit. Since businesses vary greatly, there is no set figure for profit ratios. A business would be aiming at a higher gross and net profit ratio. Comparisons need to be made with a business's past performance, their competitors and the industry average.

BizFACT

According to IBISWorld, the industries with the highest profit margins in Australia in 2020 were superannuation funds, iron ore mining, car sharing providers and electricity distributors.

Strategies to improve the gross profit and net profit ratios are examined in greater detail in subtopic 15.4 on profitability management. Businesses need to focus on strategies to reduce costs and increase revenue.

FIGURE 14.18 Examples of profitability ratios

This means that for every dollar of sales revenue the business earned, it retained 20 cents as gross profit. Another way of looking at this ratio is that cost of goods sold consumed 80 cents of every dollar of sales revenue.

Income Statement for Young's Corner Store, 2021

	$	$
Revenue	100 000	
less Cost of goods sold	80 000	
Gross profit		20 000
less Selling expenses	3 000	
less Administrative expenses	1 500	
less Financial expenses	500	5 000
Net profit		15 000

$$\text{(a) Gross profit ratio} = \frac{\text{Gross profit}}{\text{Sales}} = \frac{20\,000}{100\,000} \times 100 = 20\%$$

$$\text{(b) Net profit ratio} = \frac{\text{Net profit}}{\text{Sales}} = \frac{15\,000}{100\,000} \times 100 = 15\%$$

This means that for every dollar of sales revenue the business earned, it retained 15 cents as net profit.

Return on equity ratio

$$\text{Return on equity ratio} = \frac{\text{Net profit}}{\text{Total equity}}$$

The return on equity ratio shows how effective the funds contributed by the owners have been in generating profit, and hence a return on their investment. The return for the owners has to be better than any return that could be gained from alternative investments, such as bank investments. If return on equity rises due to increased leverage (debt) the improved result should be seen as carrying increased risk.

Owners are interested not only in the return for the current year but also in comparing the current year's return with previous years and against industry averages. It is also useful to compare the return with alternative investment considerations; for example, interest earned through a financial institution.

The higher the ratio or percentage, the better the return for the owner. If returns compare favourably, owners might consider expansion or diversification of the business. If the return is unfavourable, the owners would consider alternative options, including selling off the business.

FIGURE 14.19 An example of a return on equity ratio

$$\text{Return on equity} = \frac{\text{Net profit}}{\text{Total equity}}$$
$$= \frac{15\,000}{150\,000} = 0.1\% \text{ or } 10\%$$

Comment: This means that for every $1 of equity contributed by the owners, they receive 10 cents in return. In this example, a return of 10 per cent would be seen as a reasonable investment. Depending on other information, the owner would need to consider alternatives for investment, such as bank interest rates.

BizFACT

As a general rule, most investors would want at least 10 per cent return. This is because most investors would not risk investing in a business when they could get the same return by investing their money in a bank or in government bonds, for example.

14.6.4 Efficiency

Efficiency refers to the ability of a business to use its resources effectively in ensuring financial stability and profitability of the business. Efficiency relates to the effectiveness of management in directing and maintaining the goals and objectives of the firm. The more efficient the firm, the greater its profits and financial stability.

efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets

Expense ratio

$$\text{Expense ratio} = \frac{\text{Total expenses}}{\text{Sales}}$$

The expense ratio compares total expenses with sales. The ratio indicates the amount of sales that are allocated to individual expenses, such as selling, administration, cost of goods sold and financial expenses. The expense ratio indicates the day-to-day efficiency of the business. A business aims to keep expenses at a reasonable level.

Management use this ratio to determine where the highest expenses are from and why the ratio has either increased or decreased. For example, if the selling expense ratio has increased, it may be that advertising costs have not generated the expected increase in sales. Alternatively, a decline in the financial expense ratio may be a result of lower interest rates or less debt being used by the firm.

As businesses vary greatly, there is no rule of thumb for the expense ratio. The expense ratio should be examined carefully. Businesses need to compare their results with their past performance and industry averages. Obviously the lower the percentage, the better. If the expense ratio is too high, then the business would need to look at ways of monitoring and controlling their expenses and avoiding unnecessary expenses.

Accounts receivable turnover ratio

$$\text{Accounts receivable turnover ratio} = \frac{\text{Sales}}{\text{Accounts receivable}}$$

Accounts receivable turnover ratio measures the effectiveness of a firm's credit policy and how efficiently it collects its debts. It measures how many times the accounts receivable balance is converted into cash or how quickly debtors pay their accounts. By dividing the ratio into 365, businesses can determine the average length of time it takes to convert the balance into cash. If a firm's accounts receivable turnover is 84 days but its credit policy allows 30 days before payment, the firm would need to examine its cash flow, its credit policies, its credit collection procedures and costs, and its policies relating to doubtful debts.

If a business is not efficient in collecting their accounts receivable they need to implement strategies to improve this, such as charging interest on overdue payments, offering discounts for early payments or being more selective when granting credit.

BizFACT

The average time taken by Australian businesses to pay their invoices is 44.4 days.

FIGURE 14.20 Examples of efficiency ratios

Income Statement for Young's Corner Store, 2021		
	$	$
Revenue	100 000	
less Cost of goods sold	80 000	
Gross profit		20 000
less Selling expenses	3 000	
less Administrative expenses	1 500	
less Financial expenses	500	5 000
Net profit		15 000
Additional information: Accounts receivable = $10 000		

$$\text{(a) Expense ratio (selling expenses)} = \frac{\text{Selling expenses}}{\text{Sales}}$$

$$= \frac{3000 \times 100}{100\,000} = 3\%$$

$$\text{(b) Expense ratio (administrative expenses)} = \frac{\text{Administrative expenses}}{\text{Sales}}$$

$$= \frac{1500 \times 100}{100\,000} = 1.5\%$$

$$\text{(c) Expense ratio (financial expenses)} = \frac{\text{Financial expenses}}{\text{Sales}}$$

$$= \frac{500 \times 100}{100\,000} = 0.5\%$$

$$\text{(d) Accounts receivable turnover ratio} = \frac{\text{Sales}}{\text{Accounts receivable}}$$

$$= \frac{10\,000}{10\,000} = 10$$

$$= \frac{365}{10} = 36.5 \text{ days}$$

Comment: Depending on the type of business and past trends, the firm has made a reasonable gross and net profit and their expense ratios are quite low. For every $1 returned as sales, 3 cents is absorbed by selling expenses, 1.5 cents by administrative expenses and 0.5 cents by financial expenses. While this is quite low, these figures would need to be compared to previous years' results.

Debt collection figures indicate relative efficiency in the collection of debts. Debts are being repaid on an average of 36.5 days (assuming that the firm has a billing cycle of 30 days). There is no meaningful average for this ratio, mainly because credit terms differ among businesses. Businesses should therefore compare this result to their credit policy to see if customers are taking too long to pay. As a general rule, however, a high accounts receivable turnover ratio can be improved by demanding payment of overdue accounts.

TABLE 14.5 Types of financial ratio

Ratio	Formula	Analysis of which aspect of the financial statement	What does analysis of this ratio show about a business?	Interpretations of ratio results
Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$	Liquidity	Shows the short-term financial stability of a business (i.e. its ability to meet its short-term financial commitments)	It is generally accepted that a ratio of 2:1 indicates a sound financial position (i.e. a firm should have double the amount of assets to cover its liabilities).
Debt to equity ratio	$\frac{\text{Total liabilities}}{\text{Total equity}}$	Gearing (Solvency)	Shows the extent to which the firm is relying on debt or outside sources to finance the business	The higher the ratio, the less solvent the firm (i.e. the higher the ratio of debt to equity, the higher the business risk).
Gross profit ratio	$\frac{\text{Gross profit}}{\text{Sales}}$	Profitability	Shows the percentage of sales revenue that results in gross profit	The higher the ratio, the better. If the ratio is low, alternative suppliers may need to be sourced and competitors investigated.
Net profit ratio	$\frac{\text{Net profit}}{\text{Sales}}$	Profitability	Represents the profit or return to the owners	A firm will be aiming for a high net profit ratio. A low net profit ratio indicates strategies to reduce expenses and increase revenue need to be investigated.
Return on equity ratio	$\frac{\text{Net profit}}{\text{Total equity}}$	Profitability	Shows how effective the funds contributed by the owners have been in generating profit and so the return on investment (ROI)	The higher the ratio or percentage, the better the return for the owner, although comparisons need to be made with alternative investments.
Expense ratio	$\frac{\text{Total expenses}}{\text{Sales}}$	Efficiency	Each of the categories of expenses is compared with sales. The ratio indicates the amount of sales that are allocated to individual expenses such as selling, administration, COGS and financial expenses.	Expense ratios indicate day-to-day efficiency of the business. Expense ratios need to be kept at a reasonable level, and management must monitor each type of expense in relation to sales. Higher expense ratios may be the result of poor management.
Accounts receivable turnover ratio	$\frac{\text{Sales}}{\text{Accounts receivable}}$	Efficiency	Measures the effectiveness of a firm's credit policy and how efficiently it collects its debt	High turnover ratios indicate the business has efficient debt collection.

14.6.5 Assess business performance using comparative ratio analysis

Figures, percentages and ratios do not provide a complete picture for analysis. For analysis to be meaningful, comparisons and benchmarks are needed. Judgements are then made by comparing a firm's analysis against other figures, percentages and ratios. This is known as comparative ratio analysis and is important for firms. Comparisons can be made in a number of ways. Businesses could compare ratios with their results from previous years, with similar businesses and against common industry standards or benchmarks.

BizFACT

Comparisions can be made over different time periods, against standards, or with similar businesses.

Ratios provide a 'snapshot' at a particular point in time and should be used carefully along with other information. Sales and stock levels may vary significantly throughout a year so financial information will also vary. It is important to look at trends in the financial information over several years. Figures from at least the previous two years can indicate directions or trends and make ratio analysis more meaningful.

Analysis can also include budget figures so that predicted figures can be compared against actual figures, usually over short time periods such as per month. This information is usually available for interested parties within a firm rather than for external stakeholders.

Comparison with other businesses and benchmarking — comparing results against standards that have been developed for a particular industry — are common. However, care must be taken to ensure that the same things are compared. Also, each firm has differences, and finding comparable firms may be difficult. Benchmarks are useful but are merely a guide. For example, financial gearing is often used to compare firms, so that if the industry average of debt to equity was 80 per cent and a particular firm had 40 per cent, then it would need to examine the risks and analyse the reasons for the differences.

In the past, Australian businesses have mainly used Australian standards but, with the globalisation of business, world standards are more commonly used for benchmarking.

FIGURE 14.21 An example of profitability trends over a number of years

Income Statement						
	2019		2020		2021	
	$	%	$	%	$	%
Sales	100 000	100	120 000	100	150 000	100
less Cost of goods sold	40 000	40	40 000	33	50 000	30
Gross profit	60 000	60	80 000	67	100 000	67
less Other expenses	20 000	20	30 000	25	45 000	30
Net profit	40 000	40	50 000	42	55 000	37

Although sales have increased steadily, cost of goods sold has risen only slightly over the three-year period. Cost of inventories may have decreased due to the suppliers being used or more efficient stock control methods being developed. Expenses have shown no great variation, with figures of 20 per cent, 25 per cent and 30 per cent of sales for the three-year period, resulting in a steady profit percentage (40 per cent, 42 per cent and 37 per cent respectively).

FIGURE 14.22 An example of comparing budget to actual figures

Income Statement				
	Actual		Budget	
	$	%	$	%
Sales	75 000	100	100 000	100
less Cost of goods sold	42 000	56	55 000	55
Gross profit	33 000	44	45 000	45
less Other expenses	20 000	26	35 000	35
Net profit	13 000	17	10 000	10

Although actual sales is considerably less than budget, the reduced amount for expenses has led to an increased profit against sales (17 per cent rather than 10 per cent).

Inter-business comparisons are useful and firms may access relevant business statistics from a number of sources, including the Australian Bureau of Statistics. They must ensure information is up to date and accurately reflects industry norms.

KEY IDEAS

- The financial statements of a business must be analysed to gain a thorough understanding of the activities of a business. The analysis involves comparing similar figures contained in the financial statements and balance sheets.
- The main types of analysis include: vertical (within one year), horizontal (between different years) and trend (over a period of 3 to 5 years).
- The analysis of financial statements is usually aimed at the areas of financial stability (liquidity and gearing), profitability and efficiency.
- Liquidity is the extent to which the business can meet its financial obligations in the short term. This means a business must have enough resources to pay its debt and cover unexpected expenses.
- Current assets and current liabilities determine the liquidity or short-term financial stability of a business.
- A current ratio of 2:1 indicates a sound financial position.
- Gearing measures the relationship between debt and equity.
- Gearing is the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business.
- Profitability is the earning performance of the business and indicates its capacity to use resources to maximise profit.
- The income statement is used to measure the profitability or earning capacity of the business. Figures from this statement are used to calculate the gross profit and net profit ratios.
- The return on equity ratio shows how effective the funds contributed by the owners have been in generating profit, and hence a return on their investment.
- Efficiency is the ability of the business to use its resources effectively to ensure financial stability and profitability. It relates specifically to management's ability to achieve its goals and objectives.
- The two main ways to calculate efficiency include the expense ratio and the accounts receivable turnover ratio.
- The expense ratio indicates the amount of sales allocated to individual expenses. The accounts receivable turnover ratio measures how effective a business is in collecting its debts.
- Figures, percentages and ratios do not provide a complete picture for analysis. For analysis to be meaningful, businesses need to make comparisons with their past performance, similar businesses and against common industry standards.

14.6 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

14.6 Quick quiz on	14.6 Exercise	14.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 15	1, 3, 7, 8, 9, 12, 13, 14, 17, 18	4, 5, 6, 10, 11, 16, 19, 20

14.6 Exercise

Revision

1. **How** are financial reports analysed and interpreted?
2. **Describe** the purposes of analysing financial ratios.
3. **Construct** a table listing the types of financial ratios under the following headings (the first one has been completed for you).

Financial management objective	Type of ratio	Financial statement	Purpose
Liquidity	Current ratio	Balance sheet	Short-term financial stability

4. **Determine** the ratio that would help to answer the following questions.
   a. Are assets being used efficiently?
   b. Is the business able to pay its debts in the short term?
   c. Is the business able to pay its debts in the long term?
   d. Are owners/shareholders receiving value for their investment?
   e. Are credit policies of the business being used effectively?
   f. How is the business being financed?
5. Using the information below, **create** a report for Bobbie and Lee at the end of their first year in business as 'T-shirts and More', commenting on:
   a. return on owners' equity (Bobbie and Lee invested $50 000 in the business)
   b. gross profit ratio
   c. net profit ratio.

Income Statement for T-shirts and More, 2021			
	$	$	$
Sales of T-shirts			40 000
less Cost of goods sold			25 000
Gross profit			15 000
less Selling expenses			
Advertising	1 000		
Wages	3 300	4 300	
less Administrative expenses			
Telephone	1 400		
Rent of premises	1 500	2 900	7 200
Net profit			7 800

6. Using the following information, **create** a report commenting on the efficiency of accounts receivable of Blossoms Tyres. Comment on the trend. **Determine** what comment you would make if the business was Blossoms Trucks rather than Blossoms Tyres.

Average days sales uncollected			
2018	**2019**	**2020**	**2021**
104 days	110 days	120 days	120 days

7. The following ratios were calculated for Ventura Ltd. **Outline** what trends are indicated by the ratios and **propose** possible causes of the trends.

	2020	2021
Current ratio	2:1	1.5:1
Profit %	15	12%
Debt: equity	1:1	1.5:1%
Accounts receivable turnover	35 days	50 days

8. Using the information from the income statement below, answer the following questions.
   a. **Calculate** and comment on the expense ratio for 2020 and 2021.
   b. **Recommend** what expenses (if any) you would cut in 2022. Give reasons.
   c. **Describe** what the trend in advertising expenses has been as a percentage of sales over the last two years.
   d. **Discuss** the profitability of the business for the past two years.

Income Statement for year ended 30 June 2021		
	2020 $	2021 $
Sales	130 000	135 000
less Cost of goods sold	80 000	82 000
Gross profit	50 000	53 000
less Expenses		
Advertising	20 000	23 500
Rent	13 000	13 500
Interest – short term	1 200	1 200
Motor vehicle expenses	8 500	10 100
Net profit	7 300	4 700

9. Look at the income statement and balance sheet for Business Z.
   a. **Discuss** the profitability of Business Z.
   b. **Discuss** the gearing of Business Z.
   c. **Summarise** your recommendations for the following year.

Income Statement, Business Z			
	2019	**2020**	**2021**
Sales	80 000	74 000	95 000
less Cost of goods sold	57 500	54 000	73 800
Gross profit	22 500	20 000	21 200
less Administrative and finance expenses	16 500	15 000	16 500
Net profit	6 000	5 000	4 700

Balance Sheet, Business Z			
	2019	**2020**	**2021**
Inventory	80 000	72 500	87 500
Non-Current Assets	70 000	77 500	62 500
	150 000	**150 000**	**150 000**
Overdraft	35 000	38 000	32 000
Other Current Liabilities	35 000	32 000	38 000
Capital	80 000	80 000	80 000
	150 000	**150 000**	**150 000**

10. Use the balance sheet and the industry averages below to answer the questions that follow.

Balance Sheet as at June 2021		
Current Assets		
Cash	300	
Accounts receivable	1 200	
Inventory	3 000	4 500
Non-current Assets		5 500
		10 000
Current Liabilities		
Accounts payable		1 000
Non-current Liabilities		5 000
Owners' Equity		
Contributed capital	1 000	
Retained earnings	3 000	4 000
		10 000

Industry averages
Current ratio 2 : 3
Debt: equity 2 : 3
Accounts receivable turnover 55 days
Return on owners' equity 30%

a. **Calculate** the current ratio, debt to equity ratio, return on equity ratio and accounts receivable ratio (sales $15 000 of which 60 per cent were on credit).

b. Using the industry averages, **identify** the strengths and weaknesses of the firm's financial position and **determine** where improvements would need to be made.

11. You have been given the following analysis of the financial reports of JY Enterprises. **Create** a report for management giving your interpretation of the data under the headings 'Liquidity', 'Gearing' and 'Profitability'.

	2018	2019	2020	2021
	$	$	$	$
Current Assets				
Inventory	90 000	100 000	100 000	150 000
Accounts receivable	120 000	140 000	150 000	150 000
Non-current Assets	250 000	250 000	300 000	200 000
Total Assets	**460 000**	**490 000**	**550 000**	**500 000**
Current Liabilities				
Overdraft	40 000	50 000	60 000	60 000
Accounts payable	80 000	100 000	110 000	120 000
Non-current Liabilities	100 000	120 000	150 000	150 000
Total Liabilities	**220 000**	**270 000**	**320 000**	**330 000**
Owners' Equity				
Capital	150 000	150 000	150 000	150 000
Retained earnings	90 000	70 000	80 000	20 000
	240 000	**220 000**	**230 000**	**170 000**
Current ratio	210 000	240 000	250 000	300 000
	120 000	150 000	170 000	180 000
	= 1.75	= 1.6	= 1.48	= 1.67
Debt to equity ratio	220 000	270 000	320 000	330 000
	240 000	220 000	230 000	170 000
	= 0.92	= 1.22	= 1.4	= 1.94
Return on equity ratio	90 000	70 000	80 000	20 000
	240 000	220 000	230 000	170 000
	= 0.38	= 0.32	= 0.35	= 0.12

12. **Why** is it difficult to compare businesses over time?
13. **Why** do businesses compare their results with industry standards and benchmarks?
14. **Explain** why it is often difficult to compare ratios for businesses with industry averages.

Read the 'Harvey Norman's gearing strategy' case study and answer questions 15 and 16.

15. **Outline** what a rights issue is.
16. **Assess** the impact of this rights issue.

Extension

17. 'The objectives of financial management often conflict with one another.' **Explain** this statement.
18. 'Financial analysis is the beginning of an investigation of a business.' **Discuss**.
19. **Examine** a range of financial reports from a business.
    a. **Calculate** liquidity, gearing, profitability and efficiency ratios using figures from the reports.
    b. **Create** a report commenting on the ratios.
20. Use the internet to find the most recent annual report and financial statements of three companies.
    a. **Determine** their operating profit (or loss), total assets and total liabilities.
    b. Print screenshots of the sites where you found the results and share them with others in the class. **Compare** your results.

14.6 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q20

Extract from balance sheet for a business as at June 2020

	($)
Current assets	1700
Non-current assets	8650
Current liabilities	1100
Non-current liabilities	6500

Additional information
Financial data 2019
Debt to equity ratio = 2 : 1 or 200%
Current ratio = 1.25 : 1 or 125%

Industry averages for 2019–2020
Debt to equity ratio (total liabilities ÷ total equity) = 1 : 1 or 100%
Current ratio (current assets ÷ current liabilities) = 2 : 1 or 200%

The gearing for this business in 2020 indicates that it is

A. better than the industry average and has improved since 2019.
B. better than the industry average and has worsened since 2019.
C. worse than the industry average and has improved since 2019.
D. worse than the industry average and has worsened since 2019.

Question 2 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q17

A business provided the following financial information.

	2019 ($)	**2020** ($)
Sales	250 000	275 000
Cost of goods sold	145 000	145 000
Gross profit	?	?
Expenses	35 000	35 000
Net profit	?	?

Which of the following shows the gross profit and the net profit ratio for this busines in 2020?

	Gross profit	*Net profit ratio* (net profit ÷ sales)
A.	$105 000	28.0%
B.	$105 000	42.0%
C.	$130 000	34.5%
D.	$130 000	47.0%

Question 3 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q15

Balance sheet as at 30 June 2019

	($)		($)
Current Assets		*Current Liabilities*	
Cash	10 000	Accounts payable	10 000
Accounts receivable	5 000	Overdraft	5 000
Stock	8 000		
Non-Current Assets		*Non-Current Liabilities*	
Plant and equipment	35 000	Mortgage	135 000
Land and buildings	292 000		
		Total equity	
		Capital	184 000
		Net Profit	16 000
	350 000		350 000

What is the gearing ratio (total liabilities ÷ total equity) for this business?

A. 0.67 : 1
B. 0.73 : 1
C. 0.75 : 1
D. 0.81 : 1

Question 4 (2 marks)

Source: HSC 2018 Business Studies Exam, Section I, Q19 & 20

A business provided the following financial information.

Sales	$600 000
Owner's equity	$320 000
Accounts receivable	$41 000
Cost of goods sold	$200 000
Expenses	$60 000

Additional information:
- Gross profit ratio = Gross profit ÷ sales
- Accounts receivable turnover ratio = sales ÷ accounts receivable

a. What is the gross profit ratio for the business? **(1 mark)**

A. 53%
B. 67%
C. 78%
D. 90%

b. What is the average number of days the business takes to collect its debts? **(1 mark)**

A. 15 days
B. 25 days
C. 29 days
D. 30 days

Question 5 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q12

Kevin is considering investing in a business.

To help Kevin determine which business to invest in, he should consider comparative ratio analysis because

A. cash flow is assessed.
B. market share is determined.
C. similar businesses are evaluated.
D. business sales growth is measured.

More exam questions are available in your learnON title.

14.7 Identify the limitations of financial reporting

SYLLABUS LINK In this subtopic you will learn about the limitations of financial reports, including normalised earnings, capitalising expenses, valuing assets, timing issues, debt repayments, and notes to the financial statements. You will also learn to identify the limitations of financial reporting.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Financial reports and ratio analysis provide information on the state of the business and indicate trends in its operations. However, caution needs to be exercised when analysing financial reports because they may not give a completely accurate assessment of a business's financial position. Businesses often work hard to make their financial reports look good. Therefore, investors need to exercise caution when examining these reports. Misleading information impacts on business decision making and puts the business at risk. The following issues must be considered when analysing financial reports.

14.7.1 Normalised earnings

Normalised earnings are earnings that have been adjusted to take into account changes in the economic cycle or to remove one-off or unusual items that will affect profitability. This is done to give a more accurate depiction of the true earnings of a company. This makes it easier to compare profitability figures for a business from one year to the next, and against other businesses. An example would be to remove a land sale from a retailer's financial statements, as selling products, not selling land, is the retailer's core business.

Many businesses experience one-off expenses, such as large lawyer fees, or earn one-off gains, such as the sale of an asset. In both of these cases, even though the costs and revenues are realised and affect the business's short-term cash flow, they are not indications of the business's long-term performance.

FIGURE 14.23 In the below example, imagine a company settled a lawsuit which cost them $250 000. The expenses associated with that lawsuit have been eliminated from that company's expenses. This adjustment raised the adjusted profit to the level expected if this company had not been sued.

	Reported	Non-recurring items	Normalised
Sales	1 800 000		1 800 000
COGS	580 000		580 000
Gross Profit	1 220 000		1 220 000
Expenses			
– Litigation settlement	250 000	(250 000)	0
– Selling expenses	100 000		100 000
– Administrative expenses	80 000		80 000
– General expenses	50 000		50 000
Net Profit	740 000		990 000

14.7.2 Capitalising expenses

Capitalising expenses refers to how a cost is treated on a business's financial statement. Businesses have two options when adding a cost to their financial statement. They can either expense it or capitalise it. If the business chooses to expense the cost, it is included as an expense on the income statement and will be subtracted from the business' revenue to determine the profit.

On the other hand, if a business capitalises a cost, it is going to count towards capital expenditures. This means it will be accounted for on the business's balance sheet as an asset. In this case, the income statement will only feature the appropriate depreciation of the asset.

FIGURE 14.24 In 2020 National Australia Bank (NAB) announced that its net profit for the first half of the year would be reduced by $1.14 billion, partly due to changes the bank made to the application of its software capitalisation policy. After reviewing the policy, changes were made to increase the minimum threshold at which software was to be capitalised from $2 million to $5 million. As a result, this will reduce the bank's capitalised software balance by nearly $1.06 billion.



Costs are usually capitalised (recorded as assets) when the costs have not been used up and have future economic value. Assume that a business purchases a van for $30 000. The van is expected to provide value over a period of 10 years. Instead of expensing the entire cost of the van when purchased, accounting rules allow companies to write off the cost of the asset over its useful life (10 years). The $30 000 cost should be capitalised since it will add future economic value. The $30 000 cost increased the company's assets, but will be reduced by depreciating the cost to expenses over the next 10 years.

14.7.3 Valuing assets

This is the process of estimating the value of assets when recording them on a balance sheet. This can be difficult for financial managers or accountants to estimate, especially for non-current assets.

Sometimes when an asset is recorded on a balance sheet, its value is written as its historical cost. Historical cost is an accounting method where assets are listed on a balance sheet with the value at which they were purchased. The main advantage of using the historical cost is that the cost can be verified. The disadvantage is that this value may distort the business's balance sheet, meaning that it will not accurately represent the true worth of the business's assets. This is because the original cost of an asset may be different from its current market value.

Some non-current assets, such as land, typically increase in value over time. Other non-current assets, such as vehicles or machinery, may actually lose value over time. This is known as depreciation.

With assets that typically lose value over time, businesses have to estimate how much value they lose every year. Financial managers are allowed to depreciate assets using accounting standards so that the value of the assets on the balance sheet presents a more accurate picture of the business. While there are rules governing how depreciation is calculated, financial managers are free to choose from several methods, which may mislead some investors. This is therefore a limitation when interpreting financial reports because the depreciation rate is an estimate, and this may give a false impression about how much the business is actually worth.

Another limitation of financial reports is that some assets are very difficult to value. Intangible assets are items of value to a business, but they do not physically exist; for example, goodwill, trademarks, patents and brand names. While these assets are of value to the business, sometimes they are not included on a balance sheet because their value is too difficult to work out since there is no set formula for their calculation. If financial managers decide to include these assets on the balance sheet, there may be a temptation to overvalue them to make the business appear more financially stable than it really is.

SNAPSHOT

Case study: Retail Food Group's valuation of goodwill



Retail Food Group (RFG), the franchising company which owns Gloria Jean's, Donut King, Crust Pizza, Michel's Patisserie and other well-known chains recently had the goodwill on their balance sheet called into question after suffering a massive decline in net profit.

RFG has been in crisis after being on the receiving end of negative publicity over a 12-month period. Their troubles began in 2017 when a Fairfax investigation revealed serious mistreatment of franchisees. Many of them claimed they were financially ruined by RFG, which led to several class actions against the company. The allegations from some dissatisfied franchisees included claims that RFG charged excessively high fees along with marketing and food costs. It was also revealed that RFG had directed some franchisees of Michel's Patisserie to sell food products after their use-by dates.

These revelations led to a parliamentary inquiry into the franchising sector. The committee's report singled out RFG for the harshest criticism due to their unethical practices. The franchise inquiry report recommended the ACCC, ASIC and the ATO investigate RFG and its former directors. The regulators were urged to look into a variety of areas. One area of concern was the valuation of the company's assets, including goodwill.

In 2019, RFG reported net profit of $15.4 million, a drop of over 50 per cent from the $33.3 million profit they achieved the year before. RFG conceded that the negative publicity affected sales, but they also blamed changing consumer trends and intense competition for the downturn in operations.

The franchise inquiry report called into question the goodwill on RFG's balance sheet and recommended that the decline in profits needed to be reflected in the company's goodwill – if a business has no anticipated profit, then the goodwill will be devalued because of the company's poor financial position. RFG responded by cutting their goodwill down from $270 million in 2017 to $52 million by the end of 2019.

BizFACT

Calculating, and adjusting, the value of a company's goodwill is the issue that takes up the most time and effort of auditors of ASX 200 listed firms. Research by KPMG found that the valuation, and possible impairment, of goodwill and other intangible assets such as brand value were listed as a key audit matters by around two-thirds of companies.

BizFACT

Intangible assets are difficult to quantify and put a value on. One of the most commonly valued intangible assets are brand names. In 2020, the world's top 5 most valuable brands according to *Forbes* were Apple, worth $241.2 billion, Google ranked second at $207.5 billion, then Microsoft ($162.9 billion), Amazon ($135.4 billion) and Facebook ($70.3 billion).

14.7.4 Timing issues

When analysing a financial report, limitations can arise due to timing issues. One of the basic accounting concepts is the matching principle. Under the matching principle, expenses incurred by a business must be recorded on the income statement for the accounting period in which the revenue to which those expenses relate is earned. In other words, when an accountant records revenue, they should also record at the same time any expenses that were directly related to that revenue. For example, a real estate agent may have sold a property in June. They receive a 2 per cent commission for sales, but their employer did not pay them until July. This expense should be recorded in June.

When this principle is followed, the revenue earned will match the costs that were incurred to earn that revenue. The matching principle results in the presentation of a more accurate representation of the financial position of a business.

14.7.5 Debt repayments

When analysing a financial report, the gearing ratio is often used to determine whether businesses are at risk of failing to meet their long-term financial commitments. A business that is highly geared may be alarming for some stakeholders. However, while a highly geared business has increased risk, their potential for profit is greater. For example, higher levels of debt to fund growth can lead to increased profits in the future. Financial reports, when considered in isolation, can therefore be limited.

Financial reports can be limited because they do not have the capacity to disclose specific information about debt repayments such as:

- how long the business has had or has been recovering the debt
- the capacity of the business or its debtor to repay the amount/s owed (What if a debtor is close to bankruptcy and will not be able to repay a debt?)
- the adequacy of provisions and methods the business has for the recovery of debt (Larger businesses have the ability to outsource debt recovery by hiring an agent to undertake this process, but smaller businesses may not have the resources to do the same as it is costly and time consuming.)

- what provision the business has in place for doubtful debts and how this is evident in the financial reports
- whether debt repayments have been held over until another accounting period, therefore giving a false impression of the situation
- when the debts are due.

The recording of debt repayments on financial reports can be used to distort the 'reality' of the business's status and this may be undertaken to provide a more favourable overview of the business at that point in time.

14.7.6 Notes to the financial statement

Notes to the financial statements report the details and additional information that are left out of the main reporting documents, such as the balance sheet, income statement and cash flow statement. They contain information that may be useful to stakeholders to help them make sense of these financial statements and to explain them. These notes contain important information such as the accounting methodologies used for recording and reporting transactions that can affect the bottom-line return expected from an investment in a company. They may also contain further details about how the figures in the financial statements were calculated and the procedures that were used to develop them.

KEY IDEAS

- There are limitations to financial reports. They can be misinterpreted and can be misleading, both of which will impact on the decision making of management and potentially put the business at risk.
- The limitations of financial reports are:
  - normalised earnings: earnings that have been adjusted to take into account changes in the economic cycle or to remove one-off or unusual items that will affect profitability
  - capitalising expenses: an accounting method where a business records an expense as an asset on the balance sheet rather than as an expense on the income statement
  - valuing assets: the difficulties in estimating the value of assets when recording them on a balance sheet
  - timing issues: when revenues and expenses are recorded
  - debt repayments: financial reports don't have the capacity to disclose specific information about debt repayments
  - notes to the financial statement: these report the details and additional information left out of the main reporting documents.

14.7 Activities

learnON

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14.7 Quick quiz on	14.7 Exercise	14.7 Exam questions

Select your pathway

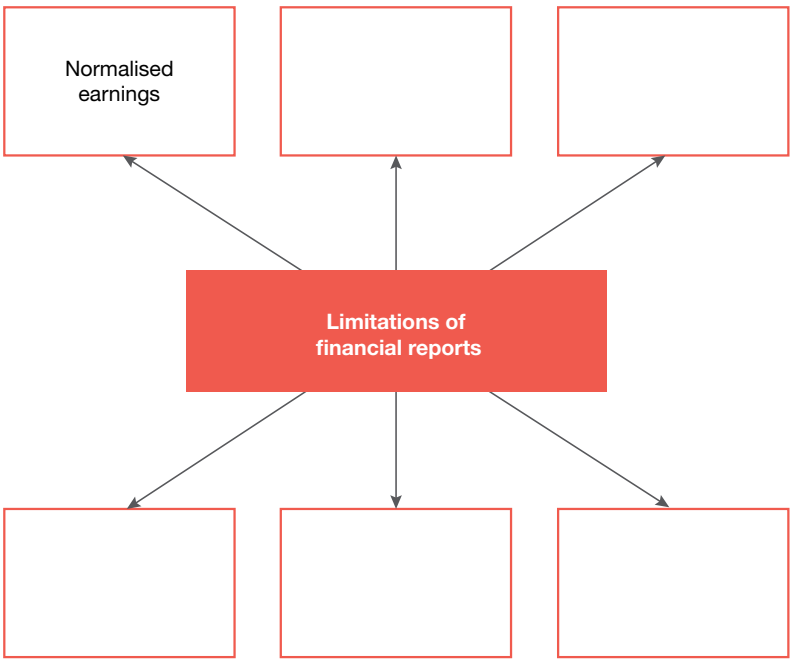
LEVEL 1	LEVEL 2	LEVEL 3
2, 3	1, 4, 5, 6	

14.7 Exercise

Revision

1. **Why** is it important for investors to be aware of the limitations of financial reports?

2. Complete the following concept map **identifying** the limitations of financial reports. Provide a brief **summary** of each. The concept map has been started for you.



Read the 'Retail Food Group's valuation of goodwill' case study and answer questions 3 and 4.

3. **Outline** the factors that led to a decrease in RFG's profits.
4. **Why** was RFG urged to re-evaluate the value of their goodwill?

Extension

5. 'Analysis of financial information identifies only symptoms, not causes.' Do you agree or disagree with this statement? **Justify** your response.
6. Use the internet to research and report on businesses who have been affected by any of the limitations of financial reporting. **Discuss** the impact this has had on the business.

14.7 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q14

A hairdresser includes proceeds of the sale of salon equipment in the business's income statement.

Which limitation of financial reporting is evident?

A. Timing issues
B. Valuing assets
C. Normalised earnings
D. Capitalising expenses

Question 2 (3 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q24a

The following is an extract from financial reports for Andrew's Discount Tyres as at 30 May 2015.

Current assets		*Current liabilities*	
Accounts receivable	1 000	Overdraft	2 000
Inventory	2 000	Accounts payable	1 000
Cash	2 000		
Non-current assets		*Non-current liabilities*	
Building	13 000	Mortgage	5 000
Fittings	1 000		
Research and development	5 000		
		Owner's Equity	16 000
Other information: Net profit for Andrew's Discount Tyres: $1000 Industry average gearing ratio (total liabilities ÷ total equity): 80%			

Explain ONE possible limitation of this financial report.

Question 3 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q16

Auditors have discovered that the value of legal fees paid has been included in the asset value of a new warehouse purchased by a business.

What limitation of financial reports does this show?

A. Capitalised expenses
B. Debt repayments
C. Normalised earnings
D. Timing issues

Question 4 (1 mark)

A business has bought the property next door to their current premises. The business will use the property for expansion in the future. Their current financial reports show an increased outflow as a result of the purchase. A member of the financial team is worried by these latest reports, though the manager is not so concerned.

Which limitation to financial reporting is described by this situation?

A. Normalised earnings
B. Valuing assets
C. Timing issues
D. Capitalising expenses

Question 5 (1 mark)

The CEO of a medium-sized business is concerned that the financial reports to be shown to other owners do not properly indicate the longer-term benefits of her strategies. She has decided to add a summary of her plans.

Which strategy is the manager using to overcome limits to financial reports?

A. Notes to financial statements
B. Timing issues of reports
C. Normalising earnings
D. Capitalising expenses

More exam questions are available in your learnON title.

14.8 Ethical issues related to financial reports

SYLLABUS LINK In this subtopic you will learn about ethical issues related to financial reports. Students will also learn to examine ethical financial reporting practices.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Financial managers and accountants who prepare financial reports should ensure the decisions they make are ethical and that they act with the highest standards. They have an ethical and legal obligation to ensure financial records are accurate. Any attempt to engage in creative accounting to portray a more favourable but inaccurate financial picture should always be avoided. In recent years, unethical practices have been highlighted and increasingly questioned (see figure 14.25).

FIGURE 14.25 In 2020, an investigation was launched into NSW workers compensation scheme, icare, after the company lost hundreds of millions of dollars a year due to financial mismanagement. As early as 2018, the State Insurance Regulatory Authority (SIRA) had become increasingly concerned about the company's financial viability and solvency. By 2020, the regulator warned that the fund's liabilities were greater than their assets by $459 million and cautioned that the company's solvency was at risk. SIRA referred the conduct to ICAC and a number of resignations followed the investigation.



It is generally accepted that financial management decisions must reflect the objectives of a business and the interests of owners and shareholders. For example, an area in which ethical considerations are important is in the valuing of assets, including inventories and accounts receivable. Such valuations influence the level of working capital and, hence, the short-term financial stability of a business. If inventories and accounts receivable are overvalued (the business makes no provisions for bad or doubtful debts), working capital will be high and indicate an untrue working capital figure for a business.

If debt funds are used extensively to finance activities in a business, although debt funds may be used to increase profits, there is added risk for shareholders. The impact of debt funds on risks to shareholders is an ethical issue that must be considered.

In preparing budgets, the expenditures and revenues are estimated. The common practice in business of overestimating expenditures and understating revenues to allow for unexpected and uncertain events is an ethical issue for a business.

Ethical considerations are closely related to legal aspects of financial management. Legislation is in place to guard against unethical business activity but there is often a time lag between the recognition of a problem and its implementation through law.

Laws relating to corporations include the responsibilities of directors and requirements for disclosure for corporations. For example, in relation to financial management, directors have a duty to:

- act in good faith
- exercise power for proper purpose in the name of the corporation
- exercise discretion reasonably and properly
- avoid conflicts of interest.

The Australian Securities Exchange (ASX) corporate governance council officiates the requirements of corporations listed with the ASX and their responsibilities in regard to compliance with law, disclosure and transparency of company details to shareholders and the public.

14.8.1 Examine ethical financial reporting practices

Some ethical issues related to financial reports include audited accounts, record keeping, GST obligations and reporting practices.

Audited accounts

In all activities of a business, the goals of the business remain paramount. Planning, monitoring, control and corrective action are all part of the process. The **audit** is an independent check of the accuracy of financial records and accounting procedures, and it has an important role in this process. The purpose of an audit is to obtain an independent opinion on the financial statements of a business and to ensure that records provide accurate information for users. Specifically, auditors establish whether the financial statements are fairly presented and in accordance with generally accepted accounting principles.

Potential users of information include financial institutions, owners and shareholders, and potential investors who rely on the independent check of the auditor before making decisions about the business.

Audits are an important part of the control function and are generally used to examine the financial affairs of a business. There are three types of audits:

1. *Internal audits*. These are conducted internally by employees to check accounting procedures and the accuracy of financial records.
2. *Management audits*. These are conducted to review the firm's strategic plan and to determine if changes should be made. The factors affecting the strategic plan may include human resources, production processes and finance.
3. *External audits.* Under the *Corporations Act 2001* (Cth), when a company becomes a large proprietorship they must have their annual financial report audited. The Australian Securities and Investments Commission (ASIC) defines a company as being 'large' if, at the end of the financial year, the company meets two of the following three criteria:
   - a consolidated revenue of $50 million or more
   - consolidated gross assets of $25 million or more
   - 100 or more employees.

   In small businesses, external auditors are usually only used if the business is for sale or as a check against theft and fraud. In an external audit, the business's financial reports are investigated by independentand specialised accountants to guarantee their authenticity. When they are satisfied, the auditor issues a statement indicating that the company's records are accurate, to the best of the auditor's knowledge, and give a true and fair view of the state of affairs, and that they comply with generally accepted accounting standards and practices.

In 2005, businesses were required to adopt new international accounting standards or international financial reporting standards (IFRS). These standards aimed for greater transparency and accountability for all businesses regardless of size. Globally standardised accounting also assists transnational corporations.

Internal and external audits assist in guarding against unnecessary waste, inefficient use of resources, misuse of funds, fraud and theft. Auditors check the control procedures of a business by physically checking assets. For example, cash is counted, the condition and amount of the inventory is checked, and accounts receivable and non-current assets are checked. Records are checked to see if they match the physical count.

audit an independent check of the accuracy of financial records and accounting procedures

FIGURE 14.26 In June 2019, Australia's financial crime watchdog AUSTRAC demanded an external audit of Afterpay in relation to its compliance with anti-money laundering and counter-terrorism financing laws. The independent auditor's report was completed by November of the same year. The report concluded that Afterpay's business model was inherently low risk in regards to its potential to be exploited by money launderers and terrorist financiers, and that the company had a strong compliance culture.



BizFACT

In September 2019, AUSTRAC ordered the appointment of an external auditor to examine ongoing concerns regarding PayPal Australia's compliance with anti-money laundering and counter-terrorism financing laws. The compliance audit was to examine rules that require businesses to report funds or property transferred to or from Australia.

Record keeping

All accounting processes depend on how accurately and honestly data are recorded in financial reports. Source documents must be created for every transaction, even those in which cash has changed hands. There is a temptation in some cases to receive payment in the form of notes and coins, and not record the transaction. If cash received in this way is not recorded, it will not show up as business revenue, and will reduce the business's profit for the year, possibly resulting in a lower tax burden. While reducing the tax burden in this way may be tempting, the Australian Taxation Office (ATO) regularly monitors business operators, and those found to be evading their taxation responsibilities can receive fines far in excess of the amount they may believe they have saved in tax. Prosecutions for tax evasion can harm the reputation of the business, and alienate customers who wish to deal with honest and ethical businesses.

BizFACT

Proper financial records must be kept for a minimum of five years.

FIGURE 14.27 A bill currently before Parliament proposes to make it a criminal offence for businesses to make or accept a cash payment of $10 000 or more by introducing penalties of up to two years of imprisonment and a $25 200 fine for individuals. It is predicted that this measure will help stop black economy behaviour and money laundering by ensuring that businesses cannot avoid scrutiny by making large payments in cash.



Reporting practices

Not only are accurate financial reports necessary for taxation purposes, but other stakeholders are entitled to access to a business's financial information. Shareholders in a private company are legally entitled to receive financial reports annually, even if the company is a small business and the shareholders are family members. To pretend that profit is lower than it should be is to attempt to defraud the ATO. This is not only illegal and unethical, but can have other negative consequences. Should the business wish to raise additional capital from existing shareholders or from a bank, understating profit may make it more difficult to persuade those sources of finance to lend to the business. If a business decided to sell the business as a going concern, any purchaser would want to see financial reports for a number of years prior to the sale. Understating profit or overstating the value of assets may prove counter-productive when a potential buyer subjects the reports to close scrutiny.

SNAPSHOT

Case study: ATO data reveals one-third of large companies pay no tax

About one-third of large companies have once again failed to pay a cent of tax, according to the Tax Office's latest corporate tax transparency report released on Thursday.

Of 2214 entities covered by the Australian Taxation Office (ATO) data for 2017–18, 710 did not pay any tax.

Many companies have claimed tax losses and concessions that often go back several years.

There were 1504 corporate entities in the 2017–18 data that reported tax payable of $52.3 billion — a net increase of $6.6 billion from the previous year.

The ATO's report noted the increase was primarily driven by the mining, energy and water segment, off the back of strong commodity prices, which were up 15 per cent in Australian dollar terms in 2017–18.

ATO deputy commissioner Rebecca Saint said groups that consistently reported losses or unusually low taxable incomes were more likely to attract the ATO's attention.

She told ABC News there were still instances of outright tax avoidance, in which multinationals attempted to shift profits outside of Australia to reduce their local taxable income, and these often resulted in the ATO's Tax Avoidance Taskforce specialist teams undertaking audits.



'The positive trend we are now observing is that many companies have ceased generating accounting losses, and are now offsetting profits by utilising losses from prior years,' Ms Saint said.

ATO says it takes 'strong action' against tax avoidance

Ms Saint said laws passed by the Federal Government were helping the ATO take 'strong action'.

She said more than $7 billion of sales income was now being booked in Australia as a result of companies, including Facebook and Google, restructuring in response to the Federal Government's tougher anti-avoidance laws, including the Multinational Anti-Avoidance Law (MAAL).

The Diverted Profits Tax (DPT) is also helping the agency get the information it needs if companies are deliberately obfuscating.

And previous stronger transfer pricing laws passed under the former Labor government have given the ATO an arsenal to fight companies it believes may be overstepping the line.

Of the 2214 corporate entities covered in the data, 1197 are foreign-owned companies with an income of $100 million or more.

Of the 1017 Australian public or private entities, 594 have an income of $100 million or more, and 423 have an income of $200 million or more.

Corporate entities with an income of more than $5 billion represent only 2 per cent of the corporate transparency population but are liable for 53 per cent ($27.9 billion) of the tax payable for the population.

This share of tax payable decreased slightly from 57 per cent in the previous year, the ATO report said.

Why companies did not pay any tax

The proportion of entities with nil tax payable has fallen over the past three years, from 36 per cent in 2015–16 to 34 per cent in 2016–17 and 32 per cent in 2017–18.

'And we have observed that companies can and do make losses as part of usual business practices.'

The reasons why 710 companies did not pay any tax in 2017–18 included:

- 269 entities that reported a taxable income but prior-year losses were available to deduct against that profit, so no tax was payable
- 242 entities reported an accounting loss
- 146 entities reported an accounting profit but reconciliation items (such as tax deductions allowed at higher rates than accounting permits) resulted in a tax loss
- 53 entities reported a taxable income but were also entitled to offsets (such as the research and development tax incentive) at least equal to the tax otherwise payable.

Source: Nassim Khadem, 'ATO data reveals one third of large companies pay no tax', www.abc.net.au, 2 January 2020.

Resources

Weblinks Auditing and Assurance Standards Board (AUASB)
KPMG

KEY IDEAS

- Businesses have an ethical and legal responsibility to provide accurate financial records.
- Laws relating to corporations regulate the conduct of directors and the requirement for disclosure of all information to be accurate.
- An audit is an independent check of the accuracy of financial and accounting procedures and is an important part of the control function of the business.
- All accounting processes depend on how accurately and honestly data is recorded in financial reports.
- Accurate financial reports are necessary for taxation purposes as well as for other stakeholders.

14.8 Activities

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14.8 Quick quiz	14.8 Exercise	14.8 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
4, 6, 7, 8, 9, 10	1, 2, 3, 5, 8, 14	11, 12, 13

14.8 Exercise

Revision

1. **Explain** the importance of ethics in financial management.
2. A business decides to undervalue its inventories and accounts receivable to indicate a favourable working capital ratio and, therefore, the short-term financial stability of the business. **Discuss** the advantages and disadvantages of this decision and its ethical implications.
3. Is it ethical to overestimate budgets to allow for uncertain or unknown risks? **Justify** your answer.
4. **Outline** the role of audits in financial management.
5. **Distinguish** between internal audits, management audits and external audits.
6. **Clarify** why financial record keeping should be accurate and honest.

Read the 'ATO reveals one-third of large companies pay no tax' case study and answer questions 7 to 10.

7. **Identify** how many large companies did not pay any tax in 2017–18.
8. **Outline** one of the main ways multinational companies avoided paying taxes.
9. **Outline** some measures the government has implemented to deal with the problem of tax avoidance.
10. **Summarise** four reasons why some large companies didn't pay any tax in 2017–18.

Extension

11. In pairs, use the internet to research and report on businesses that are involved in some form of legal action due to their unethical financial management practices. **Determine** how the business may have avoided this litigation if it had acted ethically.
12. 'Timely and valid internal and external audits are a primary safeguard against unethical financial behaviour.' **Assess** the accuracy of this statement.

13. Outline the role of Auditing and Assurance Standards Board (AUASB) Australia using the internet to find information. **Determine** why the federal government would be involved in maintaining auditing assurance standards.
14. KPMG is one of the world's leading professional services companies specialising in audit, taxation and business advice. Use the internet to **examine** KPMG's financial statement audit services.

14.8 Exam questions

Question 1 (2 marks)

Source: HSC 2019 Business Studies Exam, Section II, Q22a

Outline ONE ethical issue related to the preparation of financial reports.

Question 2 (1 mark)

Source: HSC 2009 Business Studies Exam, Section I, Q17

Which of the following is an ethical business practice?

A. Transferring funds to tax havens
B. Using company funds for personal use
C. Taking over a company to strip its assets
D. Independent checking of financial records

Question 3 (1 mark)

A large business has decided to ensure that all its reports meet community expectations. Which of the following best describes this action?

A. Notes to financial reports
B. Legal issues of financial reports
C. Auditing
D. Ethical issues of financial reports

Question 4 (4 marks)

'We want to be known as the business that people can trust. I want to start by ensuring the highest ethical standards in financial reporting.' This was the statement delivered at the annual general meeting by Cherry Chase, the managing director of Body and Soul Health Resorts. Explain ways for Cherry Chase to achieve ethical financial reporting.

More exam questions are available in your learnON title.

14.9 Review

14.9.1 Summary

Planning and implementing

- Financial planning is essential if a business is to achieve its goals. Financial planning determines how a business's goals will be achieved.
- The financial planning and implementing process consists of: determining financial needs, developing budgets, maintaining record systems, identifying financial risks and establishing financial controls.
- Financial needs are essential in order for a business to identify where it is headed and how it will get there.
- Budgets are financial documents used to estimate future revenue and expenses over a period of time.
- Budgets are often prepared to predict a range of activities relating to short-term and longer term plans and activities.
- Budgets can be classified as operating, project or financial budgets.
- Record systems are the mechanisms employed by a business to ensure that data are recorded and the information provided by records systems is accurate, reliable, efficient and accessible.
- Financial risk refers to the possibility of financial loss to businesses.
- Some of the most common financial risks for businesses include credit, market, liquidity and operational risks.
- Financial controls are the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources.

Debt and equity financing

- Finance for a business can come from either external or internal sources.
- External (or debt finance) is a liability as it is owed to sources external to the business. Equity finance relates to internal sources of finance.
- Most businesses have a combination of both internal and external finance.
- Although repayments of interest to an external provider of funds are costs to the business, debt finance can be attractive as it is readily available and interest payments can be tax deductible.
- Equity finance is the most important source of funds for a business as it remains in the business for an indefinite time and does not need to be repaid on a set date.

Matching the terms and source of finance to business purpose

- Businesses must find the source of finance that is most appropriate to fund their activities.
- When a business identifies and plans to meet its financial objectives, it is necessary to match the terms of finance with its purpose.
- This means that short-term finance should be used to purchase short-term assets and long-term finance should be used for long-term assets.
- Finance managers should match the length or term of the loan with the economic lifetime of the asset the finance is being used to purchase.

Monitoring and controlling

- Monitoring and controlling is essential for maintaining business viability, and affects all aspects of business operations — especially financial management.
- The main financial controls used for monitoring include cash flow statements, income statements and balance sheets.
- A cash flow statement provides the link between the income statement and the balance sheet. It provides information about a firm's ability to pay its debts on time.
- The cash flow statement specifically records the movement of cash receipts and cash payments that result from transactions over a given time, for example a month.
- Creditors, lenders, owners and shareholders all use a cash flow statement to assess the ability of the business to manage its cash and identify trends in cash flow over time.

- The income statement is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.
- Profit is the difference between revenue and expenses.
- A balance sheet represents a business's assets and liabilities at a particular point in time, expressed in money terms, and represents the net worth of the business.
- The accounting equation, which forms the basis of the accounting process, shows the relationship between assets, liabilities and owners' equity.

Financial ratios

- The financial statements of a business must be analysed to gain a thorough understanding of the activities of a business. The analysis involves comparing similar figures contained in the financial statements and balance sheets.
- The main types of analysis include: vertical (within one year), horizontal (between different years) and trend (over a period of 3 to 5 years).
- The analysis of financial statements is usually aimed at the areas of financial stability (liquidity and gearing), profitability and efficiency.
- Liquidity is the extent to which the business can meet its financial obligations in the short term. This means a business must have enough resources to pay its debt and cover unexpected expenses.
- Current assets and current liabilities determine the liquidity or short-term financial stability of a business.
- A current ratio of 2:1 indicates a sound financial position.
- Gearing measures the relationship between debt and equity.
- Gearing is the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business.
- Profitability is the earning performance of the business and indicates its capacity to use resources to maximise profit.
- The income statement is used to measure the profitability or earning capacity of the business. Figures from this statement are used to calculate the gross profit and net profit ratios.
- The return on equity ratio shows how effective the funds contributed by the owners have been in generating profit, and hence a return on their investment.
- Efficiency is the ability of the business to use its resources effectively to ensure financial stability and profitability. It relates specifically to management's ability to achieve its goals and objectives.
- The two main ways to calculate efficiency include the expense ratio and the accounts receivable turnover ratio.
- The expense ratio indicates the amount of sales allocated to individual expenses. The accounts receivable turnover ratio measures how effective a business is in collecting its debts.
- Figures, percentages and ratios do not provide a complete picture for analysis. For analysis to be meaningful, businesses need to make comparisons with their past performance, similar businesses and against common industry standards.

Identify the limitations of financial reporting

- There are limitations to financial reports. They can be misinterpreted and can be misleading, both of which will impact on the decision making of management and potentially put the business at risk.
- The limitations of financial reports are:
  - normalised earnings: earnings that have been adjusted to take into account changes in the economic cycle or to remove one off or unusual items that will affect profitability
  - capitalising expenses: an accounting method where a business records an expense as an asset on the balance sheet rather than as an expense on the income statement
  - valuing assets: the difficulties in estimating the value of assets when recording them on a balance sheet
  - timing issues: when revenues and expenses are recorded
  - debt repayments: financial reports don't have the capacity to disclose specific information about debt repayments

- notes to the financial statement: these report the details and additional information left out of the main reporting documents.

Ethical issues related to financial reports

- Businesses have an ethical and legal responsibility to provide accurate financial records.
- Laws relating to corporations regulate the conduct of directors and the requirement for disclosure of all information to be accurate.
- An audit is an independent check of the accuracy of financial and accounting procedures and is an important part of the control function of the business.
- All accounting processes depend on how accurately and honestly data is recorded in financial reports.
- Accurate financial reports are necessary for taxation purposes as well as for other stakeholders.

14.9.2 Key terms

accounting equation a equation that shows the relationship between assets, liabilities and owners' equity, which forms the basis of the accounting process
analysis working financial information into significant and acceptable forms that make it more meaningful, and highlighting relationships between different aspects of a business
assets items of value owned by a business
audit an independent check of the accuracy of financial records and accounting procedures
balance sheet a summary of a business's assets and liabilities at a particular point in time, expressed in money terms; represents the net worth of the business
budget a financial document used to estimate future revenue and expenses over a period of time
cash flow statement a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time
cost of goods sold the value of stock that a business has sold to its customers
debt finance short-term and long-term borrowing from external sources by a business
efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets
equity finance relates to the internal sources of finance in the business
expenses the costs incurred in the process of acquiring or manufacturing a good or service to sell and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service
financial budgets relate to financial data of a business and include the budgeted income statement, balance sheet and cash flows
financial controls the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources
financial risk the possibility of financial loss to businesses
gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.
gross profit that part of a business's profit that represents operating income minus cost of goods sold
income statement a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.
interpretation making judgements and decisions using the data gathered from analysis
liabilities items of debt owed to outside parties
liquidity the extent to which a business can meet its financial commitments in the short-term (less than 12 months)
net profit the difference between the gross profit and expenses
operating budgets relate to the main activities of a business and may include budgets relating to sales, production, raw materials, direct labour, expenses and cost of goods sold
owners' equity the funds contributed by the owner(s); represents the net worth of the business
project budgets relate to capital expenditure, and research and development
record systems the mechanisms employed by a business to ensure that data are recorded and the information provided is accurate, reliable, efficient and accessible
solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)

Resources

Digital documents	Key terms glossary (doc-35650) Chapter crossword (doc-36220)
Interactivity	Chapter crossword (int-7169)
Exam question booklet	Chapter 14 Exam question booklet (eqb-0036)

14.9 Activities

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Exercise 1: Multiple choice questions

1. Which ratio can be used to measure a business's efficiency?
   - **A.** Expense ratio
   - **B.** Net profit ratio
   - **C.** Debt to equity ratio
   - **D.** Return on equity ratio

2. Amara's Antiques is analysing its financial statements to determine if the business has sufficient resources to pay upcoming debt repayments and a buffer for unforeseen expenses. What would be the best way to determine this?
   - **A.** Calculating the efficiency of the company using an expense ratio
   - **B.** Calculating the level of gearing of the business using a debt to equity ratio
   - **C.** Calculating the solvency of the firm using a debt to equity ratio
   - **D.** Calculating the liquidity of the business using the current ratio

3. Supreme Skis is planning an expansion into snowboards, and the owners would like to know the return that they are making on their investment in the business to see if that is the best use of their funds. The best way to determine this is through looking at which of the following?
   - **A.** Profitability of the firm using a return on equity ratio
   - **B.** Profitability of the firm using a net profit ratio
   - **C.** Profitability of the firm using a gross profit ratio
   - **D.** Profitability of the firm using a debt to equity ratio

4. What is the opening cash balance for April?

	Jan	Feb	Mar	Apr
Opening balance	3 000			
Cash in ($)	25 000	24 000	23 000	24 000
Cash out ($)	14 000	14 000	13 000	15 000

   - **A.** $9000
   - **B.** $10 000
   - **C.** $34 000
   - **D.** $155 000

5. Which ratio would give a good indication about the effectiveness of a business's credit policy?
   - **A.** Expense ratio
   - **B.** Debt to equity ratio
   - **C.** Return on equity ratio
   - **D.** Accounts receivable turnover ratio

6. Terms and sources of finance for a business must be matched to their purpose. That means which of the following?
   - **A.** Finance should be matched with an asset that has a similar lifetime; for example, short-term finance should be used to buy short-term assets.
   - **B.** Finance managers should match the term of the finance with the type of asset, so small loans should be used to purchase low-cost assets.
   - **C.** Finance should be matched with assets that have a shorter lifetime; for example, long-term finance should be used to purchase assets that have a shorter lifetime.
   - **D.** Finance managers should match the finance to the value of the asset, so short-term finance is used to purchase a single asset, whereas long-term finance is for multiple assets.

7. What is an advantage of equity finance?
   - **A.** Dividends must be paid
   - **B.** A lower level of gearing
   - **C.** Interest payments are tax deductable
   - **D.** Funds can be acquired at short notice

Use the following information to answer questions 8 and 9.

Income Statement of GAL Chickens for the year ended 30 June 2020		
	$	$
Sales		?
Opening Stock	7 000	
Purchases	15 000	
Closing Stock	6 000	
Cost of Goods Sold		?
Gross Profit		175 000
Expenses		53 500
Net Profit		?

8. Calculate the Cost of Goods Sold for this period.
   - **A** – $2000
   - **B** $16 000
   - **C** $28 000
   - **D** $147 000

9. Calculate the net profit ratio (net profit + sales) for GAL Chickens.
   - **A.** 63.6%
   - **B.** 76.4%
   - **C.** 119.6%
   - **D.** 143.7%

10. The accounting equation is the basis of the accounting process and shows the relationship between assets, liabilities and owners' equity. Which of the following shows how the equation can be represented?
   - **A.** Owners' equity = Assets + Liabilities
   - **B.** Assets = Owners' equity – Liabilities
   - **C.** Liabilities = Assets –Owners' equity
   - **D.** Assets = Liabilities – Owner's equity

Exercise 2: Exam practice questions

Question 1 (4 marks)

Outline TWO processes of the planning and implementing cycle.

Question 2 (6 marks)

Use the following Balance Sheet to answer questions a to c.

The Balance Sheet as at 30/06/2016			
ASSETS		**LIABILITIES**	
Current Assets		**Current Liabilities**	
Cash	160 000		
Stock	210 000		
Accounts receivable	135 000	Accounts payable	140 000
Non-Current Assets		**Non-Current Liabilities**	
Vehicles	80 000	Bank loan	555 000
Equipment	800 000		
		Owner's Equity	
		Capital	210 000
		Re-invested Net Profit	480 000
TOTAL:	1 385 000	**TOTAL**:	1 385 000

Other information:

Sales: $2 100 000
Industry average liquidity ratio: 2:1

a. **Calculate** the current ratio (current assets ÷ current liabilities). Show all working. **(2 marks)**
b. **Outline** the liquidity position for this business. **(2 marks)**
c. **Calculate** the average number of days this business takes to collect their accounts receivable using the accounts receivable turnover ratio (sales ÷ accounts receivable). Show all working. **(2 marks)**

Question 3 (4 marks)

Explain ONE limitation of financial reports.

Question 4 (6 marks)

Analyse why it's important for business owners to calculate financial ratios.

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Teacher-led video Chapter 14 Exam practice solutions (tlvd-1877)

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15 Financial management strategies

15.1 Overview

LEARNING SEQUENCE

15.1 Overview
15.2 Cash flow management
15.3 Working capital management
15.4 Profitability management
15.5 Global financial management
15.6 Review

Financial management strategies are highly important in improving business performance and ensuring financial objectives are met. Every business, regardless of size, needs to implement a variety of financial management strategies to help them manage their finances and achieve their goals. There are a variety of strategies financial managers can implement to address issues of concern and to help the business achieve its objectives. The main strategies that will be addressed in this chapter relate to cash flow management, working capital management, profitability management and global financial management.

FIGURE 15.1 There are many different financial management strategies used by businesses.



SNAPSHOT

Case study: Effective financial management strategies at Guzman Y Gomez Mexican Kitchen franchise



Husband and wife team, Ruben and Natalie Henriques, opened their first Guzman Y Gomez Mexican Kitchen (GYG) franchise in 2013 at Rhodes Shopping Centre. They decided to start their own business after recognising their individual and complementary skill sets could provide the right mix for a new business venture. While Ruben had over 10 years' experience in corporate finance, Natalie's skills were based in hospitality and wedding venues.

From the outset, their main financial objectives have been profitability and growth. Their central aim was to run a profitable business, which they found quite difficult to achieve in the establishment phase. Not only were they learning how to run a business for the first time, GYG was still evolving as a brand. Over time, as the owners gained more experience and as the brand itself become more established, their profitability improved.

Ruben and Natalie used a combination of debt and equity to start their business; more specifically, they used capital as well as a bank loan. In the first six years, the pair did not take out any profits from the business; instead, they used the retained profits to pay off their debt and reinvest the funds back into the business. This enabled them to pursue their objective of growth. Since 2013, Ruben and Natalie have expanded their business from one restaurant employing 28 staff, to four restaurants with 140 staff.

While many small business owners focus on analysing sales and profitability, Ruben has a very strong focus on cash flow management. The main strategy Ruben has implemented is a cash flow forecast. This includes all the projected income and expenses for rolling twelve-month periods so that he knows the business's exact cash position monthly, weekly and even daily. Coming from a financial background, Ruben developed his own cash flow forecasting model in Excel, which helps him effectively control the inflow and outflow of cash. His model uses data from Xero, their point-of-sale software and their inventory management system to help forecast cash-flow movements.

The owners have also implemented strict cash management processes to ensure that their restaurants are not only profitable, but cash-flow positive as well. They require each of their store managers to bank their cash receipts daily and they set up their banking infrastructure so that all credit card transactions are received the following day (as opposed to many small businesses who only receive credit card deposits and do their banking every few days). Using this system, the owners essentially know the cash position of all four restaurants on a daily and even hourly basis. This forecast helps minimise uncertainty by predicting peaks and troughs in the cash balance. Ruben and Natalie also ensure they always have cash reserves set aside to act as a safety net for when they need money unexpectedly.

In relation to profitability management, Ruben and Natalie set specific targets for sales, cost of goods, food waste, labour, etc. which they try to achieve on a daily basis. Every few weeks, the owners analyse the targets and then implement different strategies to help them improve in those areas. They also use a variety of budgets for their expenditure in an attempt to minimise and control their expenses.

on Resources

Digital document Key terms glossary (doc-35652)

Exam question booklet Chapter 15 Exam question booklet (eqb-0037)

15.2 Cash flow management

SYLLABUS LINK In this subtopic you will learn about:
- cash flow management:
  - cash flow statements
  - distribution of payments, discounts for early payment, factoring.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Understanding business cash flow is the key to running a successful small business. Effective cash flow management helps business owners to anticipate and prepare for future highs and lows. **Cash flow** is the movement of cash in and out of a business over a period of time. If more money goes out than comes in, or if money must be paid out before cash payments have been received, there is a cash flow problem. Matching cash flow in with cash flow out is essential.

By keeping records of cash flow, you know how much cash you have in your wallet or in the bank at a given time. However, this record does not tell you what debts you have or what is owed to you by others. The issue is the same for a business, which is why budgets are an important tool for managing cash flows. Examples of cash inflows and outflows are given in table 15.1.

TABLE 15.1 Some examples of a business's inflows and outflows of cash

Inflows	Outflows
Sales	Payments to suppliers — raw materials/finished goods, etc.
Cash payment for accounts receivable	Interest on loans
Commissions received	Operating expenses — wages/salaries, raw materials/finished goods
Sales of assets	
Proceeds from issue of shares	Drawings
Interest received (investments/loans, etc.)	Purchase of assets
Dividends received	Loan repayments

15.2.1 Cash flow statements

Cash flow statements are examined in detail in chapter 14, section 14.5.1. Remember though, the statement of cash flow indicates the movement of cash receipts and cash payments resulting from transactions over a period of time. It can also identify trends and can be a useful predictor of change.

As was seen in the opening case study on Guzman Y Gomez (GYG), many businesses prepare a cash flow forecast. This is an estimate of the amount of money they expect to flow in and out of their business. It includes all their anticipated income and expenses and usually covers the next year, although it can also cover a shorter period such as a month or a week.

A cash flow forecast can make managing cash flow easier by helping owners to predict surpluses or shortages of cash. This enables them to make more informed decisions as the forecast will enable them to see the likely effect a potential decision could have on their cash flow.

cash flow the movement of cash in and out of a business over a period of time

15.2.2 Cash flow management strategies

A business may have temporary shortfalls of cash. Many businesses use overdrafts to cover these shortages. Banks allow the business to overdraw its account to a set limit with the payment of competitive interest rates. Shortfalls of cash over longer periods are of greater concern for a business as insolvency or bankruptcy may result.

The receipt of cash into a business does not necessarily coincide with payments of cash coming in. Management must implement strategies to ensure that cash is available to make payments when they are due — for example, to:

- the Australian Taxation Office
- suppliers for accounts payable
- employees for wages
- owners and shareholders for profits and dividends
- banks and financial institutions for interest on loans or overdrafts, and leasing payments.

FIGURE 15.2 The cash flow cycle describes how money flows through a business. Think of a business's cash balance like a bathtub. If you want the water in the tub to rise, you need to add more water and keep it from going down the drain. The more water that flows in and the less that flows out, the higher the level of water in the tub. Cash inflows and outflows work the same way.



Three common cash flow management strategies include distribution of payments, discounts for early payment and factoring.

BizFACT

The five most common reasons small and medium-sized enterprises (SMEs) experience cash flow problems are: slow paying debtors, rapid or unsustainable growth, failure to perform credit checks on debtors, tightened lending restrictions making it more difficult to get credit and seasonality (companies that make or sell seasonal goods often run out of funds during quieter times of the year).

Distribution of payments

An important strategy involves distributing payments throughout the month, year or other period so that large expenses do not occur at the same time and cash shortfalls do not occur. Distributing payments throughout the year means there is a more equal cash outflow each month rather than large outflows in particular months. A cash flow forecast can assist in identifying periods of potential shortfalls and surpluses.

Discounts for early payment

Another cash flow management strategy is to offer debtors a discount for early payment. An early payment discount occurs when a business offers customers a percentage reduction on the total invoice value when it's settled before the payment deadline; for example, a 2 per cent discount for invoices paid within 10 days.

This strategy is most effective when targeted at those debtors who owe the largest amounts over the financial year period. This is not only beneficial for the debtors, who are able to save money and therefore improve their cash flow, but it also positively affects the business's cash flow status. Table 15.2 summarises the main advantages and disadvantages of this strategy.

TABLE 15.2 Advantages and disadvantages of offering discounts for early payment

Advantages	Disadvantages
• Reduces risk of late payment and associated costs. Studies have found that globally 72.5 per cent of invoices are paid late. Late or unpaid invoices cost businesses in terms of debt interest, administrative costs, and wasted time chasing payment. • Can increase customer loyalty and improve customer relationships, as customers may see the discount as an incentive to choose your business over competitors. • Improves working capital and will provide extra liquidity • Reduces the risk of non-payment and bad debt	• Will decrease profit margins as any discount offered is paid directly from a business's profits • May impact ability of business to forecast cash flow • If a business implements this strategy, it will need to track its cash flows carefully, otherwise it could end up mistakenly giving discounts to customers who claim they are paying sooner, but aren't. Trying to recover the underpayment can cause problems and can affect the relationship with the customer. • There is no guarantee that customers will keep paying quickly.

Factoring

Factoring is the selling of accounts receivable for a discounted price to a finance or specialist factoring company. The business saves on the costs involved in following up on unpaid accounts and debt collection. Factoring is growing in popularity as a strategy to improve working capital. Factoring is examined in more detail in chapter 13, section 13.2.2.

Table 15.3 summarises some of the advantages and disadvantages of factoring as a cash flow management strategy.

TABLE 15.3 Advantages and disadvantages of factoring

Advantages	Disadvantages
• Immediate cash injection – funds can be in your account within 24 hours. This helps improve working capital. • Factoring isn't a loan, so businesses won't be taking on debt or paying interest. • It's quick and easy to arrange. There is usually no lengthy application process. • Businesses can avoid the hassle of collecting debts, freeing up the owner's time to concentrate on their business. • Customers may be more likely to pay on time if a factor is collecting the debt. • Availability depends more on customers' credit ratings than the business's, so even firms with bad credit may be able to access factoring.	• Factoring reduces a business's profit margin on each invoice they sell. • Factoring can be more expensive than other forms of short-term finance. • It can damage a business's relationship with their customers as they no longer deal exclusively with the business, especially if the factor uses aggressive collection methods. • It could indicate to customers that the business has cash flow problems, potentially making them wary about dealing with them.

BizFACT

Invoice discounting, which is very similar to factoring, is a growing strategy used by businesses to manage cash flow. The difference between them is that with factoring the finance company is responsible for collecting the debts owed, whereas with invoice discounting the business chases their own payments in the usual way so that customers won't be aware of the arrangement.

FIGURE 15.3 In January 2020, Rio Tinto scrapped its controversial reverse factoring program to speed up payments to small suppliers, in a quick response to rising pressure from media and small businesses. Telstra also made the same decision. The telecommunications company extended its payment terms to suppliers to 90 days, allowing Telstra to better manage its cash flow. Small businesses that needed the money earlier would receive their payment but with a discount applied so they received less cash. This was particularly detrimental to small businesses.



KEY IDEAS

- Cash flow is the movement of cash in and out of the business over a period of time. Management is required to make sure payments are made and received without creating a cash flow problem.
- A cash flow statement provides important information regarding a firm's ability to pay its debts on time.
- A cash flow forecast can assist in identifying periods of potential shortfalls and surpluses.
- Management strategies for cash flow include:
  - distributing payments throughout the year so that cash shortfalls don't occur
  - offering discounts for early payments
  - factoring.

15.2 Activities

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15.2 Quick quiz on | **15.2 Exercise** | **15.2 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 6, 9	4, 5, 7, 8, 10, 11	12, 13

15.2 Exercise

Revision

1. **Define** the term 'cash flow'.
2. Choose a business you are familiar with and **identify** three cash inflows and three cash outflows for that business.
3. **Clarify** what information can be obtained from a cash flow statement.
4. **Demonstrate** why a cash flow statement is so important for a business.
5. **How** do the strategies of (a) distribution of payments and (b) discounts for early payment help improve cash flow?
6. **Recall** the purpose of factoring and **outline** how it influences cash flow.
7. Patane Motorcycle Tours runs both short and long trips throughout the year, although the warmer months, from September to April, generate the most revenue. Cash flow problems often arise in July as repairs are carried out on the bikes, and registration and insurances fall due. **Propose** ways for Patane Motorcycle Tours to manage their cash flow.
8. Judith runs a landscape gardening business and has come to you for financial advice. You find that she is reluctant to offer discounts for cash. **Explain** the reasons for and against offering discounts for cash and **recommend** some financial advice for Judith's business.

Read the 'Effective financial management strategies at Guzman Y Gomez Mexican Kitchen franchise' case study in subtopic 15.2 Overview and answer questions 9 to 11.

9. **Outline** how Ruben and Natalie have worked towards achieving their financial management objectives.
10. **Explain** the cash flow management strategies Ruben and Natalie have implemented.
11. **How** has the economic outlook influenced this franchise?

Extension

12. 'Profit is not the same as cash in the bank.' **Analyse** this statement.
13. Examine cash flow statements from a number of businesses and **determine** the source of their cash flows. Comment on the management of cash flow for each business.

15.2 Exam questions

Question 1 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q13

Why would a business factor its accounts receivables?

A. To improve cash flow.
B. To increase owner's equity.
C. To increase the value of current assets.
D. To improve the value of the business.

Question 2 (4 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q24c

Discuss *factoring* as a strategy for cash flow management.

Question 3 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q19

What does a cash flow statement show?

A. Assets
B. Liquidity
C. Profitability
D. Receivables

Question 4 (1 mark)

Source: HSC 2008 Business Studies Exam, Section I, Q6

What is ONE use of a cash flow statement for management?

A. To negotiate finance
B. To identify new markets
C. To determine the value of intangibles
D. To calculate depreciation of non-current assets

Question 5 (1 mark)

Source: HSC 2007 Business Studies Exam, Section I, Q10

A business sells its accounts receivable to improve cash flow.

Which of the following best describes this strategy?

A. Factoring
B. Equity financing
C. Sale and lease back
D. Accounts receivable turnover

More exam questions are available in your learnON title.

15.3 Working capital management

SYLLABUS LINK In this subtopic you will learn about:

- working capital management
- control of current assets: cash, receivables, inventories
- control of current liabilities: payables, loans, overdrafts
- strategies: leasing, sale and lease back.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Short-term liquidity is important for businesses. It means a business can take advantage of profit opportunities when they arise, as well as meet short-term financial obligations, pay creditors on time to claim discounts, pay tax and meet payments on loans and overdrafts. A business must have sufficient liquidity so that cash is available or **current assets** can be converted to cash to pay debts. The lack of short-term liquidity could necessitate the sale of non-current assets, including long-term investments such as property and equipment, to raise cash. In the longer term, this can lead to reduced profitability for owners and shareholders.

Creditors place importance on a business's liquidity as they seek guarantees that their accounts will be paid. Failure to pay debts on time can alienate a business's creditors and suppliers who incur extra debt collection costs and lose confidence in the business.

Working capital is the term used in businesses to describe the funds available for the short-term financial commitments of a business. **Net working capital** is the difference between current assets and **current liabilities**. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity. The working capital cycle for businesses is illustrated in figure 15.4.

current assets assets that a business can expect to convert into cash within 12 months. They usually include cash and accounts receivable.

working capital the funds available for the short-term financial commitments of a business

net working capital the difference between current assets and current liabilities. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity

current liabilities liabilities that a business must repay within the short term. They usually include overdraft and accounts payable.

FIGURE 15.4 The working capital cycle. This refers to the length of time it takes a business to convert its net current assets and current liabilities into cash; that is, the time it takes from when a business purchases inventory to resell (or raw materials if they manufacture their products) to when they receive the cash once it's sold.

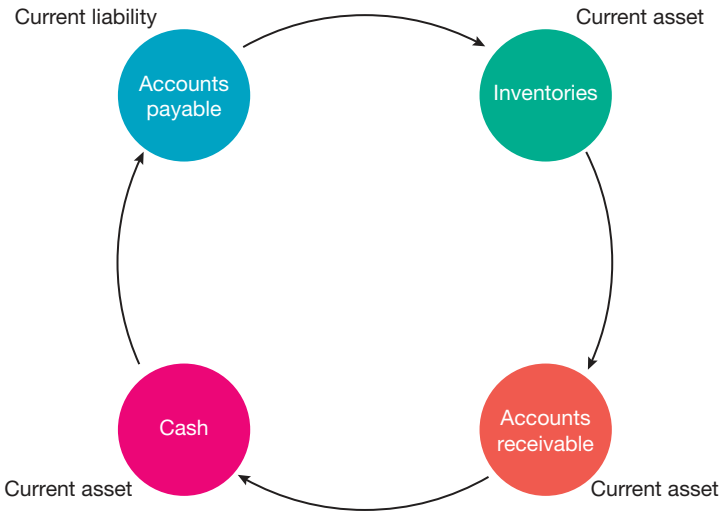
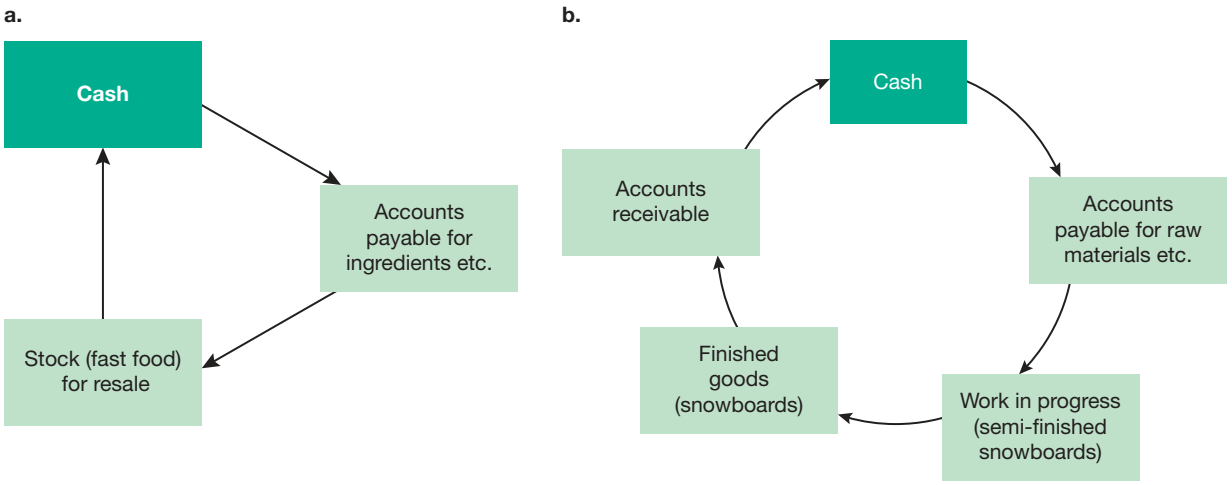


FIGURE 15.5 The requirements for working capital vary for each business. **a.** A food outlet requires a relatively low level of working capital as its cash flow cycle is short. **b.** A snowboard manufacturer requires a higher level of working capital as the cash flow cycle — between paying for raw materials and receiving payment for finished goods sold — is longer.



Business failure can result from poor management of working capital. Insufficient working capital means there are cash shortages or liquidity problems and the situation forces businesses to increase their debt, find new sources of finance or sell off non-current assets. On the other hand, an excess of working capital means that assets are earning less than the cost to finance them.

Working capital management involves determining the best mix of current assets and current liabilities needed to achieve the objectives of the business. Management must achieve a balance between using funds to create profits and holding sufficient funds to cover payments. The more efficient a business is in organising and using its working capital, the more effective and profitable it will be.

working capital management determining the best mix of current assets and current liabilities needed to achieve the objectives of the business

15.3.1 The current (working capital) ratio

As outlined in chapter 14, the current (working capital) ratio shows if current assets can cover current liabilities. That is, it helps to determine whether a business is managing cash flows so that it can pay its immediate debts. The ratio indicates the amount of risk taken by a business in relation to profitability and liquidity, and can help determine whether the business's financial structure is acceptable. For example:

BizFACT

Many businesses are profitable and yet they have a cash flow problem. Profit does not equal cash and cash does not equal profit. Many profitable businesses get into difficulty because they have a working capital problem.

$$\text{Current assets (working capital) ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$
$$= \frac{500\,000}{250\,000}$$
$$= 2:1 \text{ or } 200\%$$

In this example, the ratio indicates that, within the next 12 months, twice the amount of assets need to be sold to generate cash to meet the short-term debts of the business for the same period.

A high current ratio may indicate the business has invested too much in current assets that bring in a small return. Profitability may be reduced as the business has chosen to reduce its risk of not being able to pay its debts by having a higher current ratio. A low current ratio may mean that the business is more profitable if it is investing its resources in longer term assets and generating more profits. However, there is a risk that the business may not be able to pay its current liabilities.

A current ratio of 2:1, or 200 per cent, is generally acceptable, but ratios vary depending on the industry, the type of business, the efficiency of the business in being able to convert current assets into cash, and the relations with creditors and banks that are sources of cash. Each business determines an appropriate current ratio, but the careful monitoring of working capital is important for the survival of a business. Figure 15.6 shows the importance of working capital management.

FIGURE 15.6 An example of current (working capital) ratio

	2020	**2021**
Current Assets	$m	$m
Bank	3.4	0
Accounts receivable	30.6	34.8
Short-term investments	6.7	4.2
Inventory	21.6	25.1
	62.3	64.1
Current Liabilities		
Overdraft	0	4.6
Accounts payable	22.3	20.4
Short-term loans	17.8	19.2
	40.1	44.2
Working capital	22.2	19.9

$$\text{Working capital} = \text{Current assets} - \text{Current liabilities}$$

$$2020 = 62.3 - 40.1$$

$$= \$22.2\,\text{m}$$

$$2021 = 64.1 - 44.2$$

$$= \$19.9\text{m}$$

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

$$2020 = \frac{62.3}{40.1}$$

$$= 1.55 : 1\,(155\%)$$

$$2021 = \frac{64.1}{44.2}$$

$$= 1.45 : 1\,(145\%)$$

FIGURE 15.6 An example of current (working capital) ratio (*continued*)

- Current assets have increased in total over the two periods but at a slower rate than current liabilities. Working capital has fallen by $2.3m ($22.2m – $19.9m).
- There has been an increase in current liabilities ($17.8m to $19.2m).
- Current ratio has changed from 1.55:1 (155 per cent) to 1.45:1 (145 per cent). Management must decide whether this ratio and trend is acceptable.
- Bank has moved from a surplus to an overdraft ($0 to $4.6m). This would need to be evaluated in terms of the costs.
- Accounts receivable has increased ($34.8m – $30.6m = $4.2m) by over 10 per cent (S4.2m/30.6m = 13.7 per cent).
- Accounts payable has fallen ($22.3m to $20m).
- Short-term investments have fallen ($2.5m from $6.7m to $4.2m).
- Short-term loans have increased ($1.4m from $17.8m to $19.2m).

It would appear that short-term loans are balanced by accounts payable and short-term investments with accounts receivable. Management must examine this in the light of past experience and business policy.

Inventories have increased significantly ($3.5m from $21.6m to $25.1m). The reasons for this change should be investigated.

Although the current ratio has declined a little, there is sufficient liquidity (current assets) to fund current liabilities.

15.3.2 Control of current assets

Through the operating cycle of a business, current assets are constantly changing as inventories are sold, cash is paid out and payments are received. Current assets may make up approximately 40 per cent of a business's assets. Therefore, their use and management are important for managing working capital and require planning and constant monitoring. Excess inventories and lack of control over accounts receivable lead to an increased level of unused assets, leading in turn to increased costs and liquidity problems. Excess cash is a cost if left idle and unused. On the other hand, insufficient inventories and tight credit control policies may also lead to problems.

Control of current assets requires management to select the optimal amount of each current asset held, as well as raising the finance required to fund those assets. The costs and benefits of holding too much or too little of each asset must be assessed. Working capital must be sufficient to maintain liquidity and access to credit (overdraft) to meet unexpected and unforeseen circumstances.

Cash

Cash is critical for business success, and careful consideration must be given to the levels of cash that are held by a business. Cash ensures that the business can pay its debts, repay loans and pay accounts in the short term, and that the business survives in the long term. Reserves of cash also enable management to take advantage of investment opportunities, such as the short-term money market.

Planning for the timing of cash receipts, cash payments and asset purchases avoids the situation of cash shortages or excess cash. This can be done by using a cash flow forecast. Cash shortages can, however, occur due to unforeseen expenses and they are a cost to the business. Money may need to be borrowed, incurring interest and perhaps set-up costs.

Businesses try to keep their cash balances at a minimum and hold marketable securities as reserves of liquidity. Reserves of cash and marketable securities guard against sudden shortages or disruptions to cash flow.

Receivables (accounts receivable)

Accounts receivable refers to the outstanding invoices or payments that a business has — that is, the money that the business is owed by its customers. In many ways, accounts receivable represents cash waiting to come into the business.

When a business makes a sale — and has delivered the good or service to a customer — but the customer stills owes payment on the good or service, the amount will be recorded under accounts receivable. It is important to note here that the business has made a sale. However, the money is still owed. Collecting accounts receivable is vital in a business to ensure cash flow.

The collection of **receivables** is important in the management of working capital. Consequently, a business must monitor its accounts receivable and ensure that their timing allows the business to maintain adequate cash resources. The quicker the debtors pay, the better the firm's cash position. Procedures for managing accounts receivable include:

- stipulating a reasonable period for the payment of accounts and ensuring they set the right credit terms. A typical payment cycle ranges from 30 to 90 days. A longer payment term extends more credit to customers, while shorter terms should result in the business being paid faster.
- offering customers a variety of payment methods to make payment easier
- offering bonuses or rewards for early payment, such as discounts, free shipping, gifts, loyalty/points programs or future credits. This may encourage customers to pay on time.
- late payment fees, to encourage prompt payments
- checking the credit rating of prospective customers
- sending customers' statements monthly and at the same time each month so that debtors know when to expect accounts
- following up on accounts that are not paid by the due date
- putting policies in place for collecting bad debts, such as using a debt collection agency
- offering discounts to customers for early payment.

receivables sums of money due to a business from customers to whom it has supplied goods or services. Receivables are recorded as accounts receivable.

BizFACT

According to the annual overview of corporate insolvencies based on statutory reports lodged by external administrators, 852 business failed in the 2018–19 financial year as a result of poor management of accounts receivable. This represents over 4 per cent of failed businesses.

The disadvantage of operating a tight credit control policy is the possibility that customers might choose to buy from other firms. The costs and benefits must be weighed up carefully by management.

FIGURE 15.7 One way some businesses manage their receivables is to prepare an aged debtors report. This lists any customers (debtors) that owe the business money, how much they owe the business and how long the payment is overdue. This makes it easy for a business to identify slow payers so that they do not issue them with additional credit until they've paid their outstanding debts.

Aged debtors report

Name	Reference no.	Total	30 days	60 days	90 days	>90 days
Isabella Faro	4671	150.00	150.00	0.00	0.00	0.00
Michael Gray	4784	405.00	405.00	0.00	0.00	0.00
John Flemming	4379	225.00	1650.00	0.00	0.00	1875.00
Anthony Tran	4469	280.00	280.00	0.00	0.00	0.00
Cathy Otter	4832	49.00	49.00	0.00	0.00	0.00
Totals		**1109.00**	**2534.00**	**0.00**	**0.00**	**1875.00**

BizFACT

Afterpay is a fairly recent digital service that makes it possible for customers to buy something now and pay it off in fortnightly instalments. The money owed by customers will form part of a business's receivables. Unlike lay-by, customers will get the product straight away and, if they meet the regular repayments, they won't be charged interest. Missing an instalment, however, will result in a $10 fee. This checkout method is quickly gaining popularity in Australia.

SNAPSHOT

Case study: Small businesses losing up to $7b cashflow from late payments, study finds



Small and medium businesses are losing access to as much as $7 billion a year because bigger companies are not paying their bills on time, according to a study.

And late payments on outstanding invoices, worth $115 billion, create a 'domino effect' on the broader economy by tying up cashflow.

Those findings were based on a study of more than 150 000 businesses, conducted by the business software company Xero.

Based on its review of 10 million invoices, large businesses pay 53 per cent of invoices late by an average 23 days, making it harder for smaller businesses to take risks and employ new staff, Xero chief executive Trent Innes said.

'I think there is a bit of a cultural aspect that's been going for quite some time where big business has that power to set those terms,' Mr Innes told *The World Today*.

'If we could just get big business to pay small business on time, that would unlock about $7 billion in working capital for small business.

'That's taking it right down to the grass roots into businesses that are looking to employ that next person.'

The domino effect

The Xero report also found a link between long payment times and slower growth for small businesses, with 46 per cent failing in their first five years.

The report cites the case of Brisbane entrepreneur Deborah Peralta who created Dello Mano, which supplies packaged bite-sized brownies as corporate gifts and consumer purchases.

'When we started out, we were flexible with payments. We lived in fear of scaring off customers,' Ms Peralto told Xero's researchers.

But Ms Peralta said for large invoices she now asked for a deposit before baking — and in one case she requested 100 per cent payment upfront.

'Recently we stepped up and decided it's time to step up and quit being scared of asking for payment,' she said.

Carolyn Stebbing of Little Village Creative said that when substantial invoices were overdue it had a significant flow-on effect.

'What clients don't think about is when they pay late, it can affect dozens of other businesses — printers, film companies, contractors — who depend on small businesses like mine for their livelihood,' Ms Stebbing told the study.

Mr Innes said he believed late payments were 'the scourge of small business' and the 'staggering' $115 billion involved provided fresh urgency to solve the problem.

'We call on big business and government to prioritise this issue,' he said.

'In a period of soft economic growth, encouraging large businesses to pay on time should be a priority for the new Parliament.'

He urged small and medium businesses to tackle late payments by establishing shorter payment terms and to switch to online payments.

From July, the Federal Government will commit to shorter terms by paying small business invoices within 20 days.

Source: Peter Ryan, 'Small businesses losing up to $7b cashflow from late payments, study finds', www.abc.net.au, 26 July 2019.

Inventories

Inventories make up a significant amount of current assets, and their levels must be carefully monitored so that excess or insufficient levels of stock do not occur. Some businesses hold large inventories to ensure they do not run out of stock; however, this can become a huge cost for a business because the stock has to be stored. Stock that takes up storage space for a long time can also result in the business missing opportunities to invest money in other places. In addition, materials can become unusable after a certain period of time. This is especially so for perishable goods such as food, and high fashion items. It is very important to manage materials effectively so that costs can be kept down. On the other hand, insufficient inventory of quick-selling items may lead to loss of customers, and hence lost sales.

The rate of inventory or stock turnover differs depending on the type of business. For example, a fruit and vegetable merchant has a high turnover and pays for inventory close to the time of sale, whereas a motor vehicle dealer has a much slower stock turnover and usually pays for inventory well before a sale is made.

Inventory control is a system businesses use to ensure that the costs associated with maintaining an inventory of materials are kept to a minimum. Costs can be minimised by not allowing materials to remain idle and by making sure that they are available for production when needed. Control may occur through both physical control of inventory and through accounting control — for example, by using an inventory recording system.

Many businesses use bar coding and computerised stock records to control inventory. Computerisation can help to minimise loss or theft of stock and it provides precise, up-to-date information about stock levels. Signals can alert management when it is time to order new materials and how much to order. Businesses can also conduct stocktakes, physically count stock and then compare the count against what was expected to be available. Any differences would indicate problems with stock control.

Some businesses use an inventory system called Just In Time (JIT). This system ensures that the correct materials arrive just as they are needed for production, which can reduce storage costs and reduce the risk of waste occurring in storage, thereby improving the business's financial performance. Of course, the supply of those materials must be reliable for this system to work.

Businesses must ensure that inventory turnover is sufficient to generate cash to pay for purchases and pay suppliers on time so that they will be willing to give credit in the future.

15.3.3 Control of current liabilities

As previously explained, current liabilities are financial commitments that must be paid by a business in the short term. Minimising the costs related to a firm's current liabilities is an important part of the management of working capital. This involves being able to convert current assets into cash to ensure that the business's creditors (accounts payable, bank loans or overdrafts) are paid.

Payables (accounts payable)

A business must monitor its **payables** and ensure that their timing allows the business to maintain adequate cash resources. The holding back of accounts payable until their final due date can be a cheap means to improve a firm's liquidity position, as some suppliers allow a period of interest-free trade credit before requiring payment for goods purchased. It may also be possible to take advantage of discounts offered by some creditors. This reduces costs and assists with cash flow. Accounts must, however, be paid by their due dates to avoid any extra charges imposed for late payment and to ensure that trade credit will be extended to the business in the future.

Control of accounts payable involves periodic reviews of suppliers and the credit facilities they provide, for example:

- discounts
- interest-free credit periods
- extended terms for payments, sometimes offered by established suppliers without interest or other penalty.

payables sums of money owed by the business to other businesses from whom it has purchased goods and services. Payables are recorded as accounts payable.

BizFACT

Businesses view trade credit as cost-free finance. For example, if a business buys goods from a supplier and the account is due for payment in 30 days, the business has 30 days of cost-free finance.

Alternative financing plans should be investigated with suppliers, such as floor plan and consignment finance. Motor vehicle dealers have slow stock turnover and often use floor plan or floor stock finance. This means that suppliers agree to provide the motor vehicles for a period of time before payment is due. Consignment financing is a similar arrangement — goods are supplied for a particular period of time and payment is generally not required until goods are sold. Goods supplied may also be returned if they are not sold within the designated period.

As there are costs involved in providing and receiving credit, businesses may negotiate reduced prices if credit card facilities are used. Costs and benefits in using credit must be determined in the control of accounts payable.

FIGURE 15.8 According to ASIC poor financial control, including poor bookkeeping, was cited by 33 per cent of owners as the cause of business failure. Business owners need to set up an effective record system so they can accurately trace their accounts payable to ensure they know how much they owe each supplier and they make their payments on time. Failure to properly manage and track payables can lead to late payment penalties, damaged supplier relationships and even business failure.



Loans

Businesses may need to borrow funds in the short term for a number of purposes. Funds may be required to cover the sale and purchase of property, unforeseen circumstances, and import and export commitments. Short-term loans and bridging finance are important sources of short-term funding for businesses.

Management of loans is important, as costs for establishment, interest rates and ongoing charges must be investigated and monitored to minimise costs. Short-term loans are generally an expensive form of borrowing for a business and their use should be minimised. Control of loans involves investigating alternative sources of funds from different banks and financial institutions. Positive, ongoing relationships with financial institutions ensure that the most appropriate short-term loan is used to meet the short-term financial commitments of the business.

BizFACT

According to Money.com.au the top 10 reasons why Australian SMEs use a bank loan are: to increase working capital, buy inventory and stock, buy equipment and machinery, smooth out seasonal cash flow, pay staff or employ new staff, renovations, advertising and marketing, buy a competitor out, move premises, and pay BAS or tax payments.

Overdrafts

As previously explained, overdrafts are a convenient and relatively cheap form of short-term borrowing for a business. They enable a business to overcome temporary cash shortages. Features of overdrafts differ between banks, but generally involve an arrangement with the bank that the business's account can be overdrawn to a certain amount. Banks may demand the immediate repayment of the overdraft, although this is rare, especially if the business has a good record and a positive relationship with the bank.

Banks require that regular payments be made on overdrafts and may charge account-keeping fees, establishment fees and interest. Interest payable for an overdraft is usually less than that for a loan. Bank charges do, however, need to be carefully monitored, as charges vary depending on the type of overdraft established. Businesses should have a policy for using and managing overdrafts and monitor budgets on a daily or weekly basis so that cash supplies can be controlled.

BizFACT

An Australian Bureau of Statistics survey in May 2020 found that of the third of businesses not using JobKeeper, about 8 per cent of small businesses said they did not have the cashflow to take advantage of it. Under JobKeeper, businesses are required to cover staff wages, even if the firm is not operating. These upfront costs are reimbursed a month in arrears (a month later). Many businesses had to take out bank loans or extend their overdrafts to cover the upfront costs of paying staff.

FIGURE 15.9 In addition to overdrafts and loans, many SME owners use credit cards to assist with working capital. A survey of SMEs by Scottish Pacific in 2018 revealed that approximately 67 per cent of SME owners rely on personal finance options such as credit cards to ease cash flow problems. Additionally, respondents also said they would prefer to use credit cards over other forms of cash flow management, with 66 per cent saying they'd prefer to get a credit card over undertaking cash flow forecasts, or offering suppliers discounts for early payments.



15.3.4 Strategies for managing working capital

Businesses use a number of strategies to manage working capital, which is required to fund the day-to-day operations of a business. Strategies for working capital management include:

- leasing
- sale and lease-back.

Leasing

Leasing involves the payment of money for the use of equipment that is owned by another party. A lease is a contract between the lessor (owner of the asset) and the lessee (user of the asset) that lets the lessee rent an asset for a period of time in exchange for periodical payments. Leasing is discussed in more detail in section 13.2.2.

Some advantages of leasing include:

- The cash outflows (payments) related to leasing are spread over several years as opposed to the one-off large initial cash outflow that would occur if the business had to purchase the asset outright. This helps improve working capital.
- It allows the business to make use of good quality assets, which might have been unaffordable or expensive if they had to purchase them outright.
- Lease payments are considered operating expenses and are therefore tax deductible.
- It allows businesses the flexibility to upgrade to new and better assets as and when it is necessary without having to make a large cash outlay purchasing new equipment once an asset becomes outdated.
- It reduces the risk of technological obsolescence since the leased asset can be upgraded.
- Depending on the terms of the agreement, it reduces the risk of unpredictable costs associated with the repairs and maintenance of equipment.
- The lease payments help with cash flow forecasting and budgeting as the payments are fixed for a specified time. Businesses will know at the outset what the payments will be for the duration of the lease and the repayments won't fluctuate over time like other forms of borrowing.

Sale and lease-back

Sale and lease-back refers to the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time. The lessor retains ownership of the asset as part of the agreement. The biggest advantage of sale and lease-back is that it helps improve a business's liquidity since it enables the business to receive a large cash injection from the sale of the asset, which can then be used as working capital if the business is experiencing a cash shortfall. The business still continues to benefit from the use of the asset. This strategy shares many of the same advantages as leasing.

leasing the payment of money for the use of equipment that is owned by another party

sale and lease-back the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time

BizFACT

In 2020, Woolworths raised over $59 million from the sale and lease-back of two Woolworths supermarket-anchored shopping centres. By selling these supermarkets and leasing them back from the new owner, Woolworths received a large amount of cash that could be used as working capital.

SNAPSHOT

Case study: Village Roadshow pursues sale and lease-back strategy



In December 2017, Village Roadshow announced the sale and lease-back of 154 hectares of land on Australia's Gold Coast that currently holds well-known theme park facilities. Altis Property Partners, on behalf of LGIA super, paid $100 million in the deal. This agreement will allow Village to pay down debt and free up capital, which will enable the company to pursue investment and growth opportunities.

The site includes the land on which Warner Bros. Movie World, Wet'n'Wild Gold Coast, Paradise Country, Australian Outback Spectacular and Village Roadshow Studios are located, as well as the land on which Australia's first Topgolf venue is being built.

Warner Bros. Movie World and Wet'n'Wild are staying put for decades to come in the agreement. In exchange for the $100 million sale of the land, Village will lease the land back for a fixed 30-year term starting at $6.2 million from January 2018 and increasing by 3 per cent per annum. After 30 years, Village has an option to renew the lease for six further terms of 10 years each, meaning they have the site secured for as long as 90 years.

While Village will no longer own this land, they will still own the theme parks that are built on the land. The company will remain the main operator of the parks and will continue to manage and develop the theme parks as they always have.

This deal is a win-win for both parties. The buyer of the land benefits from this deal as they inherit a large chunk of real estate on the Gold Coast that will grow in value. Even though they cannot use this land for development themselves, they can leverage its increasing value for other investments. In addition, they get a guaranteed tenant for many decades that generates a reliable 6 per cent return. It's a low-risk, long-term investment.

On the other hand, Village also benefits from the deal as this increases their potential to generate better returns by freeing up debt and reducing interest, thereby enabling the company to invest in other opportunities. The $100 million invested by Village will yield them over $500 million dollars after 30 years as against a total rent cost in this period of $295 million.

on Resources

Weblink Commonwealth Bank

KEY IDEAS

- Working capital refers to the funds available for the short-term financial commitments of a business.
- Net working capital is the difference between current assets and current liabilities. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity.
- Control of current assets refers to the management process that determines the optimal amount of each current asset held. This includes:
  - *cash.* Careful consideration must be given to the levels of cash that are held by a business.
  - *receivables*. A business must monitor its accounts receivable and ensure their timing allows the business to maintain adequate cash resources.
  - *inventories*. The level of inventory must be carefully monitored so that excess or insufficient levels of stock do not occur.

- Control of current liabilities refers to the management process that determines the optimal amount of each current liability held. This includes:
  - *payables*. A business must monitor their accounts payable and ensure their timing allows the business to maintain adequate cash resources.
  - *loans*. Businesses may need to borrow funds in the short-term for a number of purposes. The management of these loans is important.
  - *overdrafts*. This is a relatively cheap and convenient form of short-term borrowing that can be used to cover a temporary cash shortage.
- Other strategies for managing working capital include:
  - *leasing* — a contract between the lessor (owner of the asset) and the lessee (user of the asset) that lets the lessee rent an asset for a period of time in exchange for periodical payments
  - *sale and lease-back* — the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time.

15.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

15.3 Quick quiz on | **15.3 Exercise** | **15.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
6, 7, 10, 13, 15, 16, 19	1, 2, 3, 4, 5, 8, 9, 11, 14, 17, 18, 22, 23, 24	12, 20, 21, 25, 26

15.3 Exercise

Revision

1. **Distinguish** between working capital and net working capital.
2. **Why** is working capital important to a business?
3. 'Too much working capital is as bad as not enough working capital.' **Interpret** this statement.
4. **Construct** a diagram to **demonstrate** the working capital cycle of a business that sells computers and computer software, and provides repair services for computer hardware. The business generates $3 million in sales, $1 million in repairs; it has inventory valued at $500 000, accounts receivable to the value of $230 000, accounts payable to the value of $44 000 and $58 000 in cash.
5. **Why** is the current (working capital) ratio important?
6. **Outline** working capital management strategies businesses can implement to control their current assets.
7. **Outline** working capital management strategies businesses can implement to control their current liabilities.
8. **Discuss** the working capital management strategy of leasing.
9. **Explain** how sale and lease-back can improve a business's working capital.
10. **a.** **Clarify** what a current ratio of 3.5:1 (350 per cent) represents.
    b. Explain whether this is a satisfactory or unsatisfactory ratio. (*Note:* Take care with this question.)
11. **Why** is the management of cash so important to a business?
12. KJ Carpet Cleaning operates on a cash-only basis.
    a. Describe the working capital cycle for KJ Carpet Cleaning.
    b. **Determine** what the advantages and disadvantages are of cash only for KJ.
13. Simon and Kim's Architectural Services has a wide client base and 90 per cent of their fees are on credit. Simon and Kim allow 90 days payment of their architectural services.
    a. **Identify** what potential problems in relation to their credit policy that Simon and Kim's Architechtural Services might experience.
    b. Recommend strategies to improve the business.

14. Using the information for a soft toys manufacturer below, answer the following questions.

Financial status of soft toy manufacturer	
Cash	5 900
Inventory	2 800
Accounts receivable	2 500
Plant and equipment	45 000
Accounts payable	4 200
Long-term loans	20 000

   a. **Calculate** the amount of working capital for the business.
   b. Outline the apparent success of managing accounts receivable (all sales are on credit).
   c. Identify the amount of inventory in relation to working capital.
   d. Identify the amount of cash retained in the business.
   e. **Propose** the recommendations you would make to management in relation to the management of current assets.
   f. **Calculate** the current ratio and comment on the level of the ratio.
   g. If the ratio for the previous two periods was, respectively, 220 per cent and 240 per cent, comment on the trend.
   h. **Calculate** the current liabilities of the business and **recommend** how to manage its liabilities in the future. (*Hint:* Consider that the business may choose to expand in size.)

15. Answer the following questions by referring to the aged debtors report in figure 15.7.
   a. **Identify** which debtor owes $49.
   b. **Identify** which debtor is taking the longest to repay their debt. How many days is their repayment overdue?
   c. How much money is 30 days overdue?

Read the 'Small businesses losing up to $7b cashflow from late payments' case study and answer questions 16 to 18.

16. **Identify** the percentage of invoices that are paid late, as well as the average number of days late that they are paid.
17. **Explain** the effect late payments are having on small businesses.
18. **Recommend** a strategy small businesses could implement to address this issue.

Read the 'Village Roadshow pursues sale and lease-back strategy' case study and answer questions 19 and 20.

19. **Outline** how both parties will benefit from this sale and lease-back deal.
20. **Assess** the impact sale and lease-back will have on this business.

Extension

21. 'Over-investment in working capital ties up cash flow.' 'Under-investment in working capital reduces profits.' **Analyse** these statements.
22. **How** do inflation and fluctuating business cycles affect working capital?
23. **Explain**, with examples, how cash flow relates to working capital management.
24. **How** might a business have a high current ratio but experience difficulties in finding cash to pay its suppliers?
25. **Create** a report to management with recommendations on controlling assets to manage working capital.
26. Find information online about the services of the Commonwealth Bank.
   a. **Create** a concept map that includes the main services provided by this institution to financially assist businesses. (*Hint:* This includes a lot more than just loans.)
   b. Use the calculator provided on the Commonwealth Bank website to compare the business credit card options. Recommend and justify one credit card option for a small business of 20 employees.

15.3 Exam questions

Question 1 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q6

Which of the following would immediately improve the working capital of a business?

A. Increasing credit sales
B. Using sale and lease back
C. Preparing a cash flow statement
D. Repaying debt to creditors more quickly

Question 2 (4 marks)

Source: HSC 2008 Business Studies Exam, Section II, Q25b

The balance sheet of OBOS Engineering is shown.

Balance Sheet of OBOS Engineering
As at 30 June 2008

	2007 ($)		2008 ($)	
Current assets				
Cash	2 000		–	
Inventory	10 000		20 000	
Accounts receivable	18 000	30 000	20 000	40 000
Non-current assets		240 000		260 000
Total assets		270 000		300 000
Current liabilities				
Bank overdraft	–		5 000	
Accounts payable	10 000	10 000	15 000	20 000
Non-current liabilities				
Loan		80 000		100 000
Total liabilities		90 000		120 000
Owner's equity				
Capital	150 000		160 000	
Net profit	30 000	180 000	20 000	180 000
		270 000		300 000

Additional information: *Industry standard liquidity ratio is 3:1 in 2008*

Recommend TWO strategies that OBOS Engineering could use to improve liquidity in 2009.

Question 3 (4 marks)

Source: HSC 2007 Business Studies Exam, Section II, Q23c

Recommend TWO strategies to manage working capital.

Question 4 (1 mark)

Source: HSC 2005 Business Studies Exam, Section I, Q15

The cashflow forecast for Nic's Cafe highlights that there may be a liquidity problem.

Which of the following strategies would be most appropriate to solve this liquidity problem at Nic's Cafe?

	October	November	December	January
	$	$	$	$
Opening balance	6 000	8 000	?	?
Cash inflow	7 000	7 000	7 000	10 000
Cash outflow	5 000	16 000	3 000	2 000

A. Issue debentures
B. Obtain a mortgage
C. Seek venture capital
D. Apply for an overdraft

Question 5 (1 mark)

Source: HSC 2001 Business Studies Exam, Section I, Q8

Which strategy could a business use to effectively manage receivables?
A. Offering discounts for early payment
B. Increasing the price of the product
C. Taking out a short-term loan
D. Increasing its overdraft

More exam questions are available in your learnON title.

15.4 Profitability management

SYLLABUS LINK In this subtopic you will learn about:
- profitability management
- cost controls
- fixed and variable, cost centres, expense minimisation
- revenue controls
- marketing objectives.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

15.4.1 Cost controls

Profitability management involves the control of both the business's costs and its revenue. Accurate and up-to-date financial data and reports are essential tools for effective profitability management.

profitability management involves the control of both the business's costs and its revenue

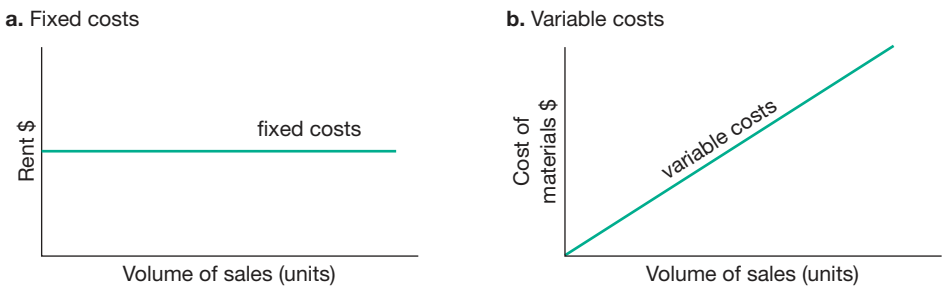
Most business decisions — for example, to open a new store or buy a new piece of machinery — are influenced by costs. The costs associated with a decision need to be carefully examined before it is implemented.

Fixed and variable costs

Before a business can control its costs, management must have a clear understanding of what those costs are. As outlined in chapter 3, businesses generally have fixed costs and variable costs.

Fixed costs are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business (see figure 15.10). Examples of fixed costs are salaries, depreciation, insurance and lease. (In reality, fixed costs can change — for example, if new premises are needed then leasing costs will increase — but, once the changes are made, the costs again become fixed.)

FIGURE 15.10 A simplified illustration of **a.** fixed costs and **b.** variable costs



Variable costs are those that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy (see figure 15.10). For example, materials and labour used in the production of a particular item are variable costs, because they are often readily identifiable in a business and can be directly attributable to a particular product.

Monitoring the levels of both fixed and variable costs is important in a business. Changes in the volume of activity need to be managed in terms of the associated changes in costs. Comparisons of costs with budgets, standards and previous periods ensure that costs are minimised and profits maximised.

Cost centres

A business's costs must be accounted for and management needs to be able to identify their source and amounts. A number of costs can be directly attributable to a particular department or section of a business, and these are termed **cost centres**. A cost centre is a department within a business that is responsible for a particular set of activities that benefits the organisation. By treating the cost centre as a separate unit, the business can measure how much they are spending on that function each year. It allows management to measure, budget and control costs for each specific function.

The use of cost centres helps management utilise resources more efficiently as it gives them a better understanding of how those resources are being used. The main function of a cost centre is to track expenses. Monitoring expenses through the use of cost centres allows for greater control of total costs. Examples of cost centres include the IT department, human resources department, accounting department and maintenance staff. Cost centres are not limited to departments, however, in some instances there may be several cost centres within one department. For instance, within the manufacturing department, each assembly line could be a cost centre.

fixed costs costs that are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business

variable costs costs that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy

cost centres particular areas, departments or sections of a business to which costs can be directly attributed

Expense minimisation

Every area in a business creates costs. A business will need to examine all of its activities and decide where costs in the production of its good or provision of its service can be cut. Balancing cost savings and quality can be difficult, so managers must determine which area or areas and which activities to focus on. Many businesses will aim to reduce costs and pass these savings on to customers without significantly impacting on the overall value of the product to customers.

Profits can be weakened if the expenses of a business are high, as they consume valuable resources within a business. Guidelines and policies should be established to encourage staff to minimise expenses where possible. Savings can be substantial if people take a critical look at costs and eliminate waste and unnecessary spending.

BizFACT

Aldi keeps its costs low by stocking a limited number of brands (most of which are its own). In addition, its products are usually purchased in bulk and stacked in store on pallets and cartons, delivery routes are kept short, store sizes are small, in store staff numbers are minimised (usually four or five per store), opening hours are limited (reducing staffing and utility costs), and the number of checkouts is minimised with customers packing their own bags away from the till (improving efficiency and reducing costs).

SNAPSHOT

Case study: IKEA cutting costs



While many retailers devote a lot of time trying to figure out how to charge more for their goods, IKEA's success has been based on the relatively simple idea of minimising costs. They pursue a cost leadership strategy and are constantly trying to do everything a little simpler, more efficiently and cost effectively.

IKEA minimises costs in the following areas:

- *design.* IKEA's designs are simple, functional and efficient to manufacture in large mass-produced batches. IKEA uses low-cost materials and their pieces are designed to include minimal parts in order to cut down on supplier and manufacturing costs.
- *supplier partnerships*. IKEA established long-term partnerships with their suppliers and order supplies in high volumes to take advantage of economies of scale and keep costs down.
- *packaging*. All their pieces are designed so that they can be packaged efficiently. IKEA pioneered the flat-pack model for their furniture. Their furniture is sold in pieces that are placed into convenient and efficient flat packages, which take up less room in trucks and maximise the number of products that can be shipped. Since their packages are flat, trucks are filled to maximum capacity, which saves on fuel and transportation costs. They also save on storage costs since each piece of furniture takes up less space in their warehouse.
- *location*. IKEA stores are generally located outside major city centres (although within driving distance) where huge spaces of land can be acquired cheaper.
- *production*. IKEA mass produces a limited number of products in order to achieve economies of scale.

15.4.2 Revenue controls

Revenue is the income earned from the main activity of a business. For most businesses, revenue comes from sales or, in the case of a service business, from fees for professional services or commission. One way to increase profits is to increase revenue, so in determining an acceptable level of revenue with a view to maximising profits, a business must have clear ideas and policies, particularly about its marketing objectives including the sales objectives, sales mix or pricing policy.

BizFACT

Budgets and cost-volume-profit analysis are the tools used in the control of revenue.

Marketing objectives

Marketing strategies and objectives should lead to an increase in sales and hence an increase in revenue. Sales objectives must be pitched at a level of sales that will cover costs, both fixed and variable, and result in a profit. A cost-volume-profit analysis can determine the level of revenue sufficient for a business to cover its fixed and variable costs to break even, and predict the effect on profit of changes in the level of activity, prices or costs.

FIGURE 15.11 When the first COVID-19 lockdowns occurred in Australia, Accent Group (the footwear giant that owns brands including The Athlete's Foot, Hype DC, Platypus Shoes and Sketchers) closed stores to the public and transitioned their entire physical network to 'dark stores' to support the delivery of online orders. The company experienced a 7.5 per cent increase in net profit in FY20. Key to this result was the group's quick pivot to e-commerce. Since then the company has modified their marketing objectives and are now targeting 30 per cent e-commerce penetration in future.



Changes to the sales mix can affect revenue. Businesses should control this by maintaining a clear focus on the important customer base on which most of the revenue depends before diversifying or extending product ranges or ceasing production on particular lines. Research should be carried out to identify the potential effects of sales-mix changes before decisions are made.

Pricing policy affects revenue and, therefore, affects working capital. Pricing decisions should be closely monitored and controlled. Overpricing could fail to attract buyers, while underpricing may bring higher sales but may still result in cash shortfalls and low profits. Factors that influence pricing include:

- the costs associated with producing the goods or services (materials, labour, overheads)
- prices charged by the competition
- short- and long-term goals — for example, if the business aims to improve market share over a five-year period,
  prices may be reduced
- the image or level of quality that people associate with the goods or services
- government policies.

SNAPSHOT

Case study: Why your grocery prices are going up but you're not getting any more in your trolley



Aussies might not like the impact on their grocery bill or the shrinking sizes in their trolleys, but food manufacturers don't like it either.

Experts say the reason we're getting smaller packets and products for the same prices is because manufacturers have no choice but to make changes to keep their companies afloat.

Not everyone will have noticed because the differences are subtle — Tiny Teddies and Shapes that used to come in a 10 pack were shrunk down to eight, and Freddo Frogs that were once 15g are now 12g.

If brands are not shrinking their products, they're putting prices up overall — not just because of the drought but because of higher manufacturing costs through rising electricity prices.

Thousands of Aussies working in the food industry have already lost their jobs and Australian Food and Grocery Council head Tanya Barden warned there could be more cuts.

She said companies could absorb mounting manufacturing costs for only so long, with the latest round of increasing costs now affecting the viability of some operations, ultimately impacting consumers.

'Food and grocery suppliers, big and small, are conscious of cost of living pressures on consumers, and have been absorbing rising manufacturing costs for some time,' she said.

'But the high pressure on Australia's largest manufacturing sector is only expected to intensify with costs on everything from commodities, particularly caused by the drought, to labour to energy continuing to increase.'

Ms Barden warned the situation had now reached the stage where something had to give.

'A number of companies either need to increase their prices, decrease their product sizes or reduce the product ranges they produce if they are to continue production in Australia,' she said.

Other shrinking packages include Red Rock Deli chips down from 185g to 165g, Doritos from 200g to 175g and Weet-Bix from 1.5kg to 1.2kg.

The larger box of Weet-Bix could be bought for $4 but the smaller package price now sits at $5.

[In 2018], amid the worsening drought crisis, experts warned shoppers would soon feel the pinch at the checkout.

They forecast vegetables, bread and even margarine to become particularly expensive.

In the drought between 2005 and 2007, food prices increased by 12 per cent, which was double inflation.

In August a report by Commonwealth Bank put the potential cost of the drought to the economy at $12 billion because of its 'significant' effect on food prices.

Ms Barden said people were losing their jobs and businesses were closing or going overseas because of growing pressures.

'Food and grocery manufacturers are under enormous pressure to be competitive, and are constantly looking for ways to keep a lid on their prices, especially given they are aware that value conscious consumers could switch to imported and private label alternatives,' she said.

'Companies have been cutting costs, automating, absorbing cost increases and innovating. But the cost increases are now impacting the viability of Australian operations, with 4750 jobs lost in the sector in recent times and the potential for further job losses, business closures or moving operations offshore.'

'In order to keep manufacturing here, companies are having to consider job cuts or changing or cutting back on the range of products they make, both of which impact Australians in the long run.'

Source: Stephanie Bedo, 'Why your grocery prices are going up but you're not getting any more in your trolley', www.news.com.au, 26 January 2019.

KEY IDEAS

- Profitability management involves the control of both the business's costs and its revenue.
- Cost controls involve:
  - understanding and monitoring the levels of both fixed and variable costs
  - accounting for and identifying the source and amount of costs through the use of cost centres
  - ensuring that expenses are minimised.
- Revenue controls are also part of profitability management and specifically address policies about a business's marketing objectives, including the sales objectives, sales mix or pricing policy.

15.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

15.4 Quick quiz on | **15.4 Exercise** | **15.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 4, 6, 8, 11, 12	2, 3, 5, 7, 9, 10	13

15.4 Exercise

Revision

1. **Define** the term 'profitability management'.
2. **Distinguish** between fixed and variable costs.
3. **Why** should a business monitor the levels of both fixed and variable costs?
4. **Outline** the advantage of attributing costs to specific cost centres.
5. **How** can expenses can be minimised?
6. **Recall** the importance of revenue controls in achieving profit maximisation.
7. **Explain** how (a) sales objectives, (b) sales mix and (c) pricing policy can affect the level of profit.

Read the 'IKEA cutting costs' case study and answer questions 8 and 9.

8. **Summarise** IKEA's expense minimisation strategies.
9. **Explain** the effect of these strategies on IKEA's profitability.

Read the 'Why your grocery prices are going up but you're not getting any more in your trolley' case study and answer questions 10 and 11.

10. **Why** are consumers getting smaller packets and products for the same prices?
11. **Outline** the external factors in the business environment that have led to these reduced sizes.

Extension

12. Research Aldi and **describe** the expense minimisation strategies they have implemented.
13. Walmart is an American multinational retailer that owns a chain of discount department stores. At the core of Walmart's success is their cost leadership. Research Walmart and **assess** the strategies the company has adopted that have enabled them to become the world's most famous cost leader.

15.4 Exam questions

Question 1 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q18

Which of the following would be the focus of a business aiming to reduce expenses?

A. Changing task design
B. Differentiating its product
C. Establishing cost leadership
D. Developing quality expectations

Question 2 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q8

What would be the best strategy for a business to increase its gross profit?

A. Use cost centres
B. Reduce fixed costs
C. Minimise expenses
D. Use sale and leaseback

Question 3 (6 marks)

Source: Adapted from HSC 2006 Business Studies Exam, Section II, Q25c

Evaluate TWO profitability management strategies the owners of Pizza and Pasta Restaurant could implement to improve profitability.

Pizza & Pasta Restaurant Revenue statement year ended 30 June 2006		Industry average	
	$		$
Sales	150 000		200 000
Cost of goods sold	105 000		100 000
Gross Profit	45 000		100 000
Operating expenses			
Administrative	5 000		12 000
Selling & distribution	7 000		15 000
Financial	3 000		3 000
Net profit	30 000		70 000

Question 4 (1 mark)

Jules Jeans has targeted gross profit and turnover of stock as ways to increase profits. Which of the following is the most likely strategy Jules Jeans would use to achieve these targets?

A. Cost centres
B. Expense minimisation
C. Fixed costs reduction
D. Marketing objectives

Question 5 (1 mark)

Source: HSC 2001 Business Studies Exam, Section I, Q10

Which of the following would be an effective management strategy to improve the long-term profitability of a business?

A. Altering the credit terms to ensure early payment of receivables
B. Improving the efficiency of cost centres
C. Selling of non-productive assets
D. Factoring of accounts receivable

More exam questions are available in your learnON title.

15.5 Global financial management

SYLLABUS LINK In this subtopic you will learn about:

- comparing the risks involved in domestic and global financial transactions
- global financial management
  - exchange rates
  - interest rates
  - methods of international payment
  - payment in advance, letter of credit, clean payment, bill of exchange
  - hedging
  - derivatives.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

15.5.1 Comparing the risks involved in domestic and global financial transactions

The growth of global business has resulted in economic expansion for many countries, as well as bringing extra concerns.

BizFACT

A number of larger financial institutions offer a range of services to facilitate the financial management of global business.

Financial risks are examined in section 14.2.4. Global businesses, however, bring extra concerns and risks for financial managers — in particular, currency fluctuations/exchange rates, interest rates, methods of international payment, hedging and derivatives.

Financial risks associated with global expansion are greater than those encountered domestically, but such risk taking is necessary for the business strategy to be implemented.

Largely 'uncontrollable' financial influences include currency fluctuations, interest rates and overseas borrowing. 'Uncontrollable' means that these influences are part of the external business environment and may not be significantly controlled by the business. However, a business can put in place appropriate financial management strategies to minimise their negative effects.

One of the most difficult financial influences to manage is currency (exchange rate) fluctuations.

FIGURE 15.12 Foreign exchange trading involves the buying of one currency and the selling of another currency in an attempt to make a profit. This is done by speculating on the value of one currency in comparison to another. Foreign currencies can be traded because exchange rates fluctuate all the time. Foreign exchange trading is very complex and risky since it is extremely difficult to predict movements in currencies.



15.5.2 Exchange rates

Countries have their own currency, which they use for domestic purposes. This means that when transactions are conducted on a global scale, one currency must be converted to another. For example, if an Australian business (importer) purchases machinery from Japan, the Japanese firm (exporter) will want to be paid in Japanese yen, not Australian dollars. Similarly, if a Japanese tourist visits Australia, he or she will pay for accommodation, restaurant meals and other products in Australian dollars, not yen. Therefore, in all global transactions it is necessary to convert one currency into another. This transaction is performed through the **foreign exchange market**, commonly abbreviated to **forex** or **fx**, which determines the price of one currency relative to another.

Foreign exchange dealers around the world are constantly buying and selling each other's currency. In this way, the price or value of each country's currency is established. This value or price is called the exchange rate.

The **foreign exchange rate** is the ratio of one currency to another; it tells how much a unit of one currency is worth in terms of another. For example, if A$1 = US$0.70, that means one Australian dollar is worth 70 US cents. Conversely, one US dollar would be worth A$1.43.

Effects of currency fluctuations

Exchange rates fluctuate over time due to variations in demand and supply.

Such fluctuations in the exchange rate create further risk for global business. For example, suppose that the value of the Australian dollar rises from US$0.70 to US$0.95. This upward movement of the Australian dollar (or another currency) against the US dollar is called an **appreciation**. (Of course, this means that the value of the US dollar has decreased against the Australian dollar, with one US dollar being worth A$1.05.)

The impact of this currency fluctuation is twofold:

1. A currency appreciation raises the value of the Australian dollar in terms of foreign currencies. This means that each unit of foreign currency buys fewer Australian dollars. However, one Australian dollar buys more foreign currency. Therefore, an appreciation makes our exports more expensive on international markets but prices for imports will fall. The result of the appreciation, therefore, reduces the international competitiveness of Australian exporting businesses.
2. A currency depreciation has the opposite impact. A depreciation lowers the price of Australian dollars in terms of foreign currencies. Therefore, each unit of foreign currency buys more Australian dollars. The result is that our exports become cheaper and the price of imports will rise.

foreign exchange market (forex or fx) a market that determines the price of one currency relative to another

foreign exchange rate the ratio of one currency to another; it tells how much a unit of one currency is worth in terms of another

appreciation an upward movement of the Australian dollar (or any other currency) against another currency

A depreciation, therefore, improves the international competitiveness of Australian exporting businesses.

Currency fluctuations, therefore, significantly impact on the profitability of global businesses. When revenues and expenses are transferred between nations, the exchange rate can either increase or decrease their value. Currency fluctuations will also affect the business's ability to meet their financial objectives.

15.5.3 Interest rates

A business that plans to either relocate offshore or expand domestic production facilities to increase direct exporting will normally need to raise finance to undertake these activities. A global business has the option of borrowing money from financial institutions in Australia, or they can borrow money from financial markets overseas. Traditionally, Australian interest rates tend to be above those of other countries, especially the United States and Japan. Thus, Australian businesses could be tempted to borrow the necessary finance from an overseas source to gain the advantage of lower interest rates.

However, the real risk here is exchange rate movements. Any adverse currency fluctuation could see the advantage of cheaper overseas interest rates quickly eliminated. In the long term, the 'cheap' interest rates may end up costing more. Changes in interest rates will therefore have a major impact on a business's profitability if they have borrowed money from finance markets overseas.

BizFACT

In Australia, interest rates decisions are taken by the Reserve Bank of Australia's (RBA) Board. In November 2020, the RBA cut the cash rate by 15 basis points taking it to a new record low of 0.10 per cent. Policymakers reiterated their commitment to do what they can to support jobs, incomes and businesses in Australia during the pandemic. Interest rates in Australia have averaged 4.16 per cent from 1990 until 2020, reaching an all-time high of 17.50 per cent in January of 1990 and a record low of 0.10 per cent in November 2020.

15.5.4 Methods of international payment

One of the most crucial aspects of global financial management is to select an appropriate method of payment. This is because not being paid is a very real risk for exporting businesses. Payment can be complicated by the fact that the business may be dealing with someone they have never seen, who speaks another language, uses a different monetary system, abides by a different legal system and/or who may prove difficult to deal with if problems occur later on. One major concern for the exporter is that if the products are shipped before payment is received, there may be no guarantee that the importer will pay.

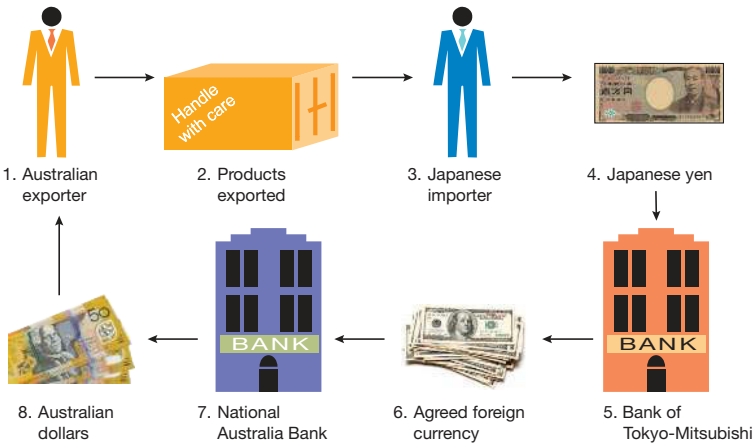
On the other hand, the buyer is faced with a similar situation. The importer may be concerned that if payment is sent before the products are received, there is similarly no guarantee that the exporter will send the products. This dilemma is as old as global business itself. Neither party completely trusts the other.

To solve this problem, a method of payment using a third party, who both parties trust, is required. This third party is normally a bank, which acts in an intermediary role. Figure 15.13 provides a simple explanation of the payment procedures when a product is exported from Australia to Japan. Note how both parties agree to the contract price being written in US dollars.

There are four basic methods of payment from which a business can select:

- payment in advance
- letter of credit
- clean payment
- bill of exchange.

FIGURE 15.13 Simple international payment system showing the intermediary role of banks



The option selected will largely depend on the business's assessment of the importer's ability to pay — that is, the importer's creditworthiness. Of course, as with all financial transactions, each method carries varying degrees of risk, especially when credit payments are involved (see figure 15.14).

FIGURE 15.14 Degree of credit risk for different methods of international payment



The following section discusses the different methods of payment in order of increasing risk to the exporter.

Payment in advance

The **payment in advance** method allows the exporter to receive payment and then arrange for the goods to be sent. This method exposes the exporter to virtually no risk and is often used if the other party is a subsidiary or when the credit worthiness of the buyer is uncertain. However, very few importers will agree to these terms because it exposes them to the most risk. Furthermore, they have no guarantee that they will receive what they ordered.

payment in advance a payment method that allows the exporter to receive payment and then arrange for the goods to be sent

Letter of credit

In order to ensure that payment will be received, sometimes exporters will require the importer to have a letter of credit confirmed by a secure bank. A **letter of credit** is a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met. In order for the payment to occur, the seller has to present the bank with the necessary documents proving shipment of the goods.

letter of credit a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met.

In all but exceptional circumstances, once the bank has made such a commitment it cannot be withdrawn. In the event that the buyer cannot make the payment, the bank will then be required to cover the purchase. Therefore, the bank will only issue a letter of credit if they know the buyer will pay. Some banks require buyers to deposit or have enough money to cover the payment or else they allow the buyers to use a line of credit.

Only payment in advance offers less risk and, for this reason, a letter of credit is very popular with exporters. This is because it relies on the overseas bank rather than the importer.

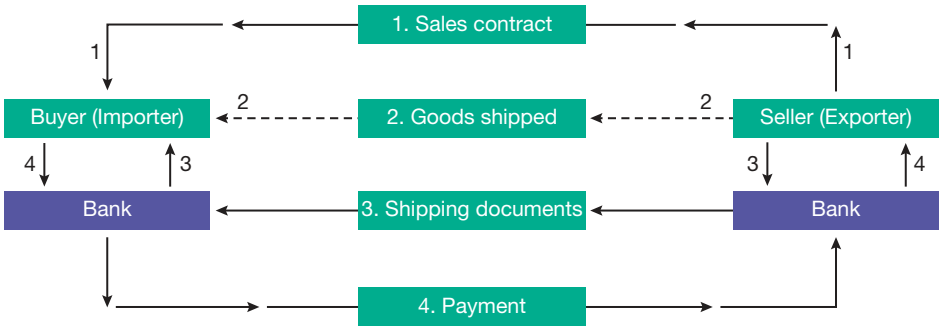
Bills of exchange

A bill of exchange is a document drawn up by the exporter demanding payment from the importer at a specified time. This method of payment is one of the most widely used and allows the exporter to maintain control over the goods until payment is either made or guaranteed.

There are two types of bill of exchange.

1. *Document (bill) against payment*. Using this method, the importer can collect the goods only *after* paying for them. The exporter draws up a bill of exchange with his or her Australian bank and sends it to the importer's bank along with a set of documents that will allow the importer to collect the goods. The importer's bank hands over the documents only after payment is made. The importer's bank then transfers the funds to the exporter's bank.
2. *Document (bill) against acceptance*. Using this method, the importer may collect the goods *before* paying for them. The same process applies as with documents against payment, except the importer must sign only acceptance of the goods and the terms of the bill of exchange to receive the documents that allow him or her to pay for the goods at a later date.

FIGURE 15.15 How bills of exchange work



1. Seller and buyer agree terms and enter into a sales/purchase contract.
2. Goods are shipped.
3. Seller presents shipping documents through the banking system. Generally buyers are unable to take delivery of the goods until they have these shipping documents (this does not normally apply to airfreights shipments).
4. Per contracted payment terms, the buyer pays immediately (a 'sight' payment, sometimes known as Docs against Payment — D/P) or formally agrees to pay at a future date (a 'term' payment, sometimes known as Docs against Acceptance — D/A). Upon payment or acceptance documents are released to the buyer to enable them to obtain the goods.

The risk of non-payment or payment delays when using a bill of exchange is always greater than for a letter of credit. However, documents against acceptance expose the exporter to much greater risk than documents against payment. The risk with documents against payment is that the importer may not collect the documents nor pay for the goods. With documents against acceptance there is the risk the importer may delay payment or not pay at all.

BizFACT

Countertrade is becoming more popular as a trading or payment system, similar to bartering.

Clean payment

A type of **clean payment** is an open account payment method. Under this method, the exporter ships the goods directly to the importer before payment is received. The importer therefore doesn't send the payment until after they receive the goods. The goods are usually shipped with an invoice requesting payment at a certain time after delivery. This is typically 30, 60 or 90 days. The time the exporter gives the buyer to pay for the goods is called the credit term. This method is usually only used when the exporter is confident that the importer will pay by the agreed time. This method of payment is obviously one of the most risky for exporters; however, it is one of the most advantageous options for an importer.

15.5.5 Hedging

When two parties agree to exchange currency and finalise a deal immediately, the transaction is referred to as a spot exchange. Exchange rates determining such 'on-the-spot' transactions are referred to as spot exchange rates. The **spot exchange rate** is the value of one currency in another currency on a particular day. Therefore, when an Australian tourist in Tokyo goes to a bank to convert her dollars into yen, the exchange rate is the spot rate for the day.

Although there are situations when it is necessary to use a spot rate, it may not be the most favourable rate. As explained previously in this section, exchange rates can change constantly. Such currency fluctuations can be a cause of real concern since they can increase costs for businesses and therefore lead to a reduction in profits. However, it is possible for businesses to minimise the risk of currency fluctuations. This process is referred to as **hedging**. Hedging refers to the process of minimising the risk of currency fluctuations to help reduce the level of uncertainty involved with international financial transactions.

Natural hedging

A business may adopt a number of strategies to eliminate or minimise the risk of foreign exchange exposure. In this way the business provides itself with a natural hedge. Some examples of natural hedging include:

- establishing offshore subsidiaries
- arranging for import payments and export receipts denominated in the same foreign currency; therefore, any losses from a movement in the exchange rate will be offset by gains from the other
- implementing marketing strategies that attempt to reduce the price sensitivity of the exported products
- insisting on both import and export contracts denominated in Australian dollars. This effectively transfers the risk to the buyer (importer).

clean payment occurs when the exporter ships the goods directly to the importer before payment is received

spot exchange rate the value of one currency in another currency on a particular day

hedging the process of minimising the risk of currency fluctuations

Financial instrument hedging

Apart from such natural hedges there are a growing number of financial products available, called derivatives, that can be used to minimise or spread the risk of exchange rate fluctuations.

15.5.6 Derivatives

To minimise the financial risks involved with exporting, financial institutions are continually developing new types of products, collectively referred to as derivatives. **Derivatives** are simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations.

derivatives simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations

To help understand how hedging and derivatives work, it is comparable to having a fixed interest rate on a loan. Since interest rate movements are hard to predict, a fixed rate allows people to lock in a rate on their loan to protect themselves against future interest rate rises. This also helps them plan their finances because they will know exactly how much they will be repaying. The disadvantage is that they won't be able to benefit from falling interest rates if they occur.

Derivatives, if used unwisely, can be as dangerous as the risks against which they are supposed to protect.

The three main derivatives available for exporters include:

- forward exchange contracts
- option contracts
- swap contracts.

FIGURE 15.16 In the early 2000s BMW became aware that despite increasing sales revenue, their profits were severely hampered by changes in exchange rates. The company calculated that the negative effect of exchange rates cost them €2.4 billion between 2005 and 2009. Since the company did not want to pass on this cost to consumers, they attempted to manage their foreign exchange exposure by hedging. They used a combination of natural hedging (by developing ways to spend money in the same currency as where sales were taking place) as well as derivatives.



Forward exchange contract

A **forward exchange contract** is a contract to exchange one currency for another currency at an agreed exchange rate on a future date, usually after a period of 30, 90 or 180 days. This means that the bank guarantees the exporter, within the set time, a fixed rate of exchange for the money generated from the sale of the exported goods.

For example, imagine a business sells $50 000 worth of their products to a Japanese customer, with the invoice payable in 30 days. Derivatives will allow them to lock in the value of that sale by selling Japanese yen and buying Australian dollars for a fixed rate, to be settled at the same time the invoice will be paid, thus locking in the value of the currency.

BizFACT

Market research shows that many small- to medium-sized exporters hesitate in taking on large deals because of exchange rate concerns. A large order can often put an exporter under great financial pressure, especially if they are unfamiliar with the process of hedging.

Options contract

Foreign currency options provide another strategy for risk management. An **option** gives the buyer (option holder) the right, but not the obligation, to buy or sell foreign currency at some time in the future.

Option holders are protected from unfavourable exchange rate fluctuations, yet maintain the opportunity for gain should exchange rate movements be favourable.

Swap contract

Since its introduction in the 1980s, swaps have become a very popular financial instrument for businesses wanting to hedge. A **currency swap** is an agreement to exchange currency in the spot market with an agreement to reverse the transaction in the future. It involves a spot sale of one currency together with a forward repurchase of the currency at a specified date in the future; for example, swapping $50 million Australian dollars for US dollars now and an agreement to reverse the swap within three months.

Businesses also use currency swaps when they need to raise finance in a currency issued by a country in which they are not well known and are, therefore, forced to pay a higher interest rate than would be available to a better-known borrower or a local business.

For example, a medium-sized Australian business may need Japanese yen, but even though it is a reputable business and has a good credit rating, it may not be well known in Japan. If it can find, or if a broker or bank can team it with, a Japanese business that wants Australian dollars, the swap would work as follows. The Australian business would borrow Australian dollars in Australia, where it is well known and can arrange a loan at cheaper interest rates; the Japanese business would borrow yen in Japan for the same reason. They would then agree to swap the currencies and repay each other's loan; that is, the Japanese business would repay the Australian dollar loan, while the Australian business would repay the Japanese yen loan.

The main advantage of a swap contract is that it allows the business to alter its exposure to exchange fluctuations without discarding the original transaction.

forward exchange contract a contract to exchange one currency for another currency at an agreed exchange rate on a future date, usually after a period of 30, 90 or 180 days

option something that gives the buyer (option holder) the right, but not the obligation, to buy or sell foreign currency at some time in the future

currency swap an agreement to exchange currency in the spot market with an agreement to reverse the transaction in the future

SNAPSHOT

Case study: How airlines hedge against fluctuating fuel prices



The largest operating cost centres for airlines, on average, are their fuel expenses and those expenses related to the procurement of oil. When oil prices are decreasing in the global economy, it's natural for the share prices of airlines to increase. When oil prices increase in the economy, it's equally natural that the share prices of airlines will go down. Fuel costs are such a large part of an airline's costs that the fluctuating price of oil greatly affects their profitability.

To mitigate the risks associated with unpredictable fuel prices, airlines commonly practice fuel hedging. Different airlines adopt different approaches to hedging and use a range of different financial instruments to protect themselves against rising prices. Some will hedge almost all of their fuel requirements, currency and interest rate exposures, some do not hedge at all.

Usually, airlines hedge the risk of a possible increase in oil prices by purchasing forward contracts. This is a customisable contract where two parties agree to buy or sell a certain quantity of oil (or other commodity) at a pre-determined price on a future date. For example, if an airline believes that oil prices will rise in the future, they could purchase large amounts of current oil contracts to mitigate these rising prices.

Essentially, by entering into forward exchange contracts, both parties decide to give up potential profits in return for certainty. Once the forward contract reaches maturity, there is always a 'winner' and a 'loser'. If the price of fuel at maturity is higher than the one agreed upon in the contract, the airline 'wins'. Thanks to the hedge, it has spent less on fuel than it would have done if it had purchased it on the market on that date. In the event that the fuel market price at maturity is lower, then the supplier 'wins', as it will make more money off the fuel due to the forward exchange contract.

on Resources

Weblink Westpac Bank

KEY IDEAS

- Global financial management refers to strategies that can be adopted to deal with the financial risks and influences on global businesses.
- Fluctuations in the exchange rate create risks for global business. Depreciation and appreciations will impact on both import and export levels and the payments made to overseas businesses or financial intermediaries.
- Domestic and international businesses will source funds internationally and will therefore need to consider the interest rates offered on borrowings. The repayment of this debt must also allow for fluctuations in currency.
- The main methods of international payment include:
  - payment in advance — allows the exporter to receive the payment and then arrange for the goods to be sent
  - letter of credit — a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met
  - clean payment — occurs when the exporter ships the goods directly to the importer before payment is received
  - bill of exchange — a document drawn up by the exporter demanding payment from the importer at a specified time.

- Hedging is the process of minimising the risk of currency fluctuations. Hedging helps reduce the level of uncertainty involved with international financial transactions.
- Derivatives are simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations.

15.5 Activities

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15.5 Quick quiz on	15.5 Exercise	15.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 4, 7, 8, 9	2, 6, 10, 11, 12, 13, 15, 16, 18	5, 14, 17

15.5 Exercise

Revision

1. **Identify** four factors that make operating globally more complex than operating in a domestic market.
2. **Why** are financial influences often classified as 'uncontrollable'?
3. **Outline** the role played by the foreign exchange market.
4. **Define** the term 'exchange rate'.
5. Using the following exchange rates, **determine** whether the rates (a) to (d), when taken sequentially, show the Australian dollar depreciating or appreciating.
   a. A$1 = US$0.85
   b. A$1 = US$0.70
   c. A$1 = US$0.63
   d. A$1 = US$0.52
6. **Explain** the effect of (a) depreciation and (b) appreciation on the prices of exports and imports.
7. **Outline** how a lack of mutual trust between the exporter and importer may be overcome.
8. Use the following table to **summarise** the four basic methods of payment for exports and how each method works. The first one has been completed for you.

Method of payment	How it works
1. Payment in advance	• Exporter receives payment and then sends goods • No risk for exporter • Few importers use this method
2. Letter of credit	
3. Bill of exchange: **a.** against payment **b.** against acceptance	
4. Clean payment	

9. **Define** the terms 'spot exchange rate' and 'hedging'.
10. **Propose** three natural hedge strategies a business could implement.
11. An Australian business manager would like to export Ugg boots. However, she is concerned about currency fluctuations. **Discuss** how this risk could be reduced.
12. **Compare** a forward exchange contract, an option contract and a swap contract.

Read the 'How airlines hedge against fluctuating fuel prices' case study and answer questions 13 and 14.

13. **How** do fluctuations in the price of oil and fuel affect airlines' profitability?
14. **Assess** the impact of hedging for airlines.

Extension

15. Your business enters into a contract to pay a certain amount of foreign currency to someone in six months. Who bears the risk of currency fluctuation? **Explain**.
16. Futures and options are two other types of derivatives. **Investigate** how these two financial instruments help reduce the risk of exporting.
17. Find information online about the services of Westpac Bank.
    a. **Create** a concept map of the services offered to a business in relation to foreign exchange and international business.
    b. Locate the currency converter and **determine** the following conversions of Australian dollars to other foreign currencies.
        1. A$2.4 million = _____ Fijian dollars
        2. A$22.6 million = _____ Swedish kronor
        3. A$13.1 million = _____Thai baht
18. **Discuss** some of the issues an Australian business may need to consider when dealing with international trade and currencies.

15.5 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q18

Australian businesses export to Canada.

What would happen if the value of the Australian dollar increased compared to the Canadian dollar?

A. There would be no effect on Canadian businesses.
B. Australian imports from Canada would become more expensive.
C. Canadian businesses would find Australian products more affordable.
D. Australian products would become more expensive for Canadian businesses.

Question 2 (20 marks)

Source: HSC 2018 Business Studies Exam, Section IV, Q26

Explain the influence of global markets on financial management of businesses.

Question 3 (5 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q24b

A business imports computers from China and sells them to customers in Australia.

Justify the method of payment that would be most effective in reducing the business's financial risk.

Question 4 (3 marks)

Source: HSC 2013 Business Studies Exam, Section II, Q24a

An Australian-owned business manufactures bicycles in China and sells them to wholesalers in France. These wholesalers do not pay in advance.

Describe ONE method of payment the business could use to ensure that it receives payment for the sales.

Question 5 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q20

Which of the following groups would suffer the worst financial impact as a result of an increase in the value of the Australian dollar?

A. Japanese shareholders of an Australian bank
B. Australian producers selling wine to New Zealand
C. Australian car makers purchasing inputs from Italy
D. American travel agents organising tours for Australians

More exam questions are available in your learnON title.

15.6 Review

15.6.1 Summary

Cash flow management

- Cash flow is the movement of cash in and out of the business over a period of time. Management is required to make sure payments are made and received without creating a cash flow problem.
- A cash flow statement provides important information regarding a firm's ability to pay its debts on time.
- A cash flow forecast can assist in identifying periods of potential shortfalls and surpluses.
- Management strategies for cash flow include:
  - distributing payments throughout the year so that cash shortfalls don't occur
  - offereing discounts for early payments
  - factoring.

Working capital management

- Working capital refers to the funds available for the short-term financialcommitments of a business.
- Net working capital is the difference between current assets and current liabilities. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity.
- Control of current assets refers to the management process that determines the optimal amount of each current asset held. This includes:
  - cash. Careful consideration must be given to the levels of cash that are held by a business.
  - receivables. A business must monitor its accounts receivable and ensure their timing allows the business to maintain adequate cash resources.
  - inventories. The level of inventory must be carefully monitored so that excess or insufficient levels of stock do not occur.
- Control of current liabilities refers to the management process that determines the optimal amount of each current liability held. This includes:
  - payables. A business must monitor their accounts payable and ensure their timing allows the business to maintain adequate cash resources.
  - loans. Businesses may need to borrow funds in the short-term for a number o purposes. The management of these loans is important.
  - overdrafts. This is a relatively cheap and convenient form of short-ter borrowing that can be used to cover a temporary cash shortage.
- Other strategies for managing working capital include:
  - leasing — a contract between the lessor (owner of the asset) and the lessee (user of the asset) that lets the lessee rent an asset for a period of time in exchange for periodical payments
  - sale and lease-back — the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time.

Profitability management

- Profitability management involves the control of both the business's costs and its revenue.
- Cost controls involve:
  - understanding and monitoring the levels of both fixed and variable costs
  - accounting for and identifying the source and amount of costs through the use of cost centres
  - ensuring that expenses are minimised.
- Revenue controls are also part of profitability management and specifically address policies about a business's marketing objectives, including the sales objectives, sales mix or pricing policy.

Global financial management

- Global financial management refers to strategies that can be adopted to deal with the financial risks and influences on global businesses.

- Fluctuations in the exchange rate create risks for global business. Depreciation and appreciations will impact on both import and export levels and the payments made to overseas businesses or financial intermediaries.
- Domestic and international businesses will source funds internationally and will therefore need to consider the interest rates offered on borrowings. The repayment of this debt must also allow for fluctuations in currency.
- The main methods of international payment include:
  - payment in advance — allows the exporter to receive the payment and then arrange for the goods to be sent
  - letter of credit — a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met
  - clean payment — occurs when the exporter ships the goods directly to the importer before payment is received
  - bill of exchange — a document drawn up by the exporter demanding payment from the importer at a specified time.
- Hedging is the process of minimising the risk of currency fluctuations. Hedging helps reduce the level of uncertainty involved with international financial transactions.
- Derivatives are simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations.

15.6.2 Key terms

appreciation an upward movement of the Australian dollar (or any other currency) against another currency
cash flow the movement of cash in and out of a business over a period of time
clean payment occurs when the exporter ships the goods directly to the importer before payment is received
cost centres particular areas, departments or sections of a business to which costs can be directly attributed
currency swap an agreement to exchange currency in the spot market with an agreement to reverse the transaction in the future
current assets assets that a business can expect to convert into cash within 12 months. They usually include cash and accounts receivable.
current liabilities liabilities that a business must repay within the short term. They usually include overdraft and accounts payable.
derivatives simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations
fixed costs costs that are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business
foreign exchange market (forex or **fx)** a market that determines the price of one currency relative to another
foreign exchange rate the ratio of one currency to another; it tells how much a unit of one currency is worth in terms of another
forward exchange contract a contract to exchange one currency for another currency at an agreed exchange rate on a future date, usually after a period of 30, 90 or 180 days
hedging the process of minimising the risk of currency fluctuations
leasing the payment of money for the use of equipment that is owned by another party
letter of credit a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met.
net working capital the difference between current assets and current liabilities. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity
option something that gives the buyer (option holder) the right, but not the obligation, to buy or sell foreign currency at some time in the future
payables sums of money owed by the business to other businesses from whom it has purchased goods and services. Payables are recorded as accounts payable.

payment in advance a payment method that allows the exporter to receive payment and then arrange for the goods to be sent
profitability management involves the control of both the business's costs and its revenue
receivables sums of money due to a business from customers to whom it has supplied goods or services. Receivables are recorded as accounts receivable.
sale and lease-back the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time
spot exchange rate the value of one currency in another currency on a particular day
variable costs costs that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy
working capital the funds available for the short-term financial commitments of a business
working capital management determining the best mix of current assets and current liabilities needed to achieve the objectives of the business

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Digital documents	Key terms glossary (doc-35652) Chapter crossword (doc-36221)
Interactivity	Chapter crossword (int-7171)
Exam question booklet	Chapter 15 Exam question booklet (eqb-0037)

15.6 Activities

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Exercise 1: Multiple choice questions

1. Firms depend on cash flow for survival. Which of the following is not a cash inflow?
   - **A.** Interest paid on loans
   - **B.** Sales of assets
   - **C.** Proceeds from sales
   - **D.** Proceeds from issue of shares
2. What is the working capital ratio?
   - **A.** Current assets ÷ current liabilities
   - **B.** Current liabilities – current assets
   - **C.** Total liabilities ÷ total equity
   - **D.** Assets + liabilities
3. Insurance, depreciation and facilities leases are which of the following?
   - **A.** Fixed costs, which are dependent on the level of activity in the business
   - **B.** Fixed costs, which are not dependent on the level of activity in the business
   - **C.** Variable costs, which are dependent on the level of activity in the business
   - **D.** Variable costs, which are not dependent on the level of activity in the business
4. Which of the following would be an effective cost control strategy?
   - **A.** Cost centres
   - **B.** Marketing objectives
   - **C.** Distribution of payments
   - **D.** Discounts for early payment
5. What is an advantage of hedging?
   - **A.** It makes it easier for a business to expand.
   - **B.** It will allow a business to export more easily.
   - **C.** It increases a business's access to foreign markets.
   - **D.** It decreases the financial risk associated with currency exchanges.

6. A potential cause of a decline in working capital could be which of the following?
   - **A.** Poor credit collection policies
   - **B.** Use of owners' equity
   - **C.** Use of long-term assets
   - **D.** A high level of inventory
7. Which of the following are key current assets that businesses need to manage?
   - **A.** Cash, payables, inventories
   - **B.** Cash, short-term loans, receivables
   - **C.** Cash, overdrafts, inventories
   - **D.** Cash, receivables, inventories
8. Which of the following best describes factoring?
   - **A.** Offering debtors a discount for early payments
   - **B.** Putting policies in place for collecting bad debts
   - **C.** Selling accounts receivable to a third party at a discount
   - **D.** Distributing accounts payable throughout the year to avoid cash shortfalls
9. Which of the following is an example of a working capital management strategy?
   - **A.** Leasing
   - **B.** Cost centres
   - **C.** Marketing objectives
   - **D.** Expense minimisation
10. Michael imports the majority of his raw materials from overseas.
    Which method of payment would expose his business to the most risk?
    - **A.** Letter of credit
    - **B.** Clean payment
    - **C.** Bill of exchange
    - **D.** Payment in advance

Exercise 2: Exam practice questions

Question 1 (2 marks)
Define sale and lease-back.

Question 2 (2 marks)
Outline a working capital management strategy businesses can use to control current their liabilities.

Question 3 (3 marks)
Discuss the use of factoring as a cash flow management strategy.

Question 4 (6 marks)
A business is experiencing cash flow problems. **Explain** TWO cash flow management strategies that could be of assistance.

Question 5 (5 marks)
Assess the impact of TWO global financial management strategies.

Question 6 (5 marks)
Analyse how leasing could change the working capital position of a business.

Resources

Teacher-led video Chapter 15 Exam practice solutions (tlvd-1878)

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Topic 3 Finance review

Finance: Practice examination

Section I — Multiple choice questions (10 marks)

1. Which of the following are examples of external sources of funds?
   - **A.** Private equity, overdraft and leasing
   - **B.** Overdraft, leasing and factoring
   - **C.** Leasing, factoring and new issues
   - **D.** Factoring, new issues and mortgage
2. A business has decided to source its finance externally. What would be the main advantage of this?
   - **A.** It would improve their gearing.
   - **B.** The interest payments would be tax deductible.
   - **C.** It would be cheaper than other sources of finance.
   - **D.** It would result in less risk for the owner and the business.
3. Which ratio can be used to measure a business's efficiency?
   - **A.** Current ratio
   - **B.** Expense ratio
   - **C.** Debt to equity ratio
   - **D.** Return on equity ratio
4. Which of the following strategies could be used to manage working capital?
   - **A.** Leasing and factoring
   - **B.** Factoring and selling
   - **C.** Leasing and marketing
   - **D.** Inventory control and selling
5. Which of the following are important aspects of financial planning and implementing?
   - **A.** Developing budgets and financial controls
   - **B.** Financial controls and account management
   - **C.** Account management and maintaining record systems
   - **D.** Maintaining record systems and staff management
6. What is an advantage of equity?
   - **A.** Dividends must be paid.
   - **B.** There is a lower level of gearing.
   - **C.** Regular repayments must be made.
   - **D.** Interest payments are tax deductible.
7. Which of the following indicates the effectiveness of a firm's credit policy?
   - **A.** Expense ratio
   - **B.** Current ratio
   - **C.** Net profit ratio
   - **D.** Accounts receivable turnover ratio

8. Refer to the following information.

Financial information for Bella Pty Ltd

	$ million
Sales	650
Cost of goods sold	45
Expenses	470

Calculate the net profit ratio.

A. 21%
B. 35%
C. 72%
D. 93%

9. Which method of international payment represents the least risk for an exporter?

A. Clean payment
B. Letter of credit
C. Bill of exchange
D. Payment in advance

10. Which of the following would be an advantage of hedging?

A. It allows businesses to export more easily.
B. It increases a business's access to foreign markets.
C. It allows businesses to increase the use of derivatives to expand.
D. It decreases the financial risk associated with currency exchanges.

Section II — Short answer questions (62 marks)

1. The debt to equity ratio of Pantry Plus is currently at 0.44:1.
   - **a.** **Outline** what is meant by debt to equity ratio. **2 marks**
   - **b.** **Recommend** strategies that could be implemented by Pantry Plus to address this situation. **8 marks**
2. Georgia has decided to open a fashion and makeup business that caters for girls/women with a specific focus on tweens, teens and early twenties. She is currently creating her business plan and must now make financial decisions about her business.
   - **a.** **Describe** the strategic role of financial management for this business. **3 marks**
   - **b.** **Explain** the role of the government in Georgia's financial management considerations. **5 marks**
   - **c.** **Recommend** TWO sources of finance relevant to her business. **6 marks**
3. Slickwheels Pty Ltd is a medium-sized Australian business that specialises in the production of skateboards. Slickwheels is experiencing difficulties in relation to working capital management.
   - **a.** **Define** the term 'working capital'. **2 marks**
   - **b.** **Explain** one strategy to control current assets and one strategy to control current liabilities that could be implemented. **6 marks**
   - **c.** **Recommend** one working capital strategy that may assist the business to manage this financial situation effectively. **4 marks**

4. Refer to the following balance sheet.

	$	$
Current Assets		
Cash	7 000	
Receivables	6 000	
inventories	2 000	15 000
Non-Current Assets		
Property, plant and equipment		18 000
Total Assets		33 000
Current Liabilities		
Creditors		14 000
Net Assets		19 000
Owners' Equity		
Capital	16 500	
Net Profit	2 500	19 000

a. **Calculate** the current ratio of this business. **2 marks**

b. **Recommend** two strategies that could be used to improve this business's current ratio. **6 marks**

c. **Assess** how an overdraft of $2000 would affect the current ratio. **4 marks**

5. 'The Australian dollar has risen to a yearly high of US$1.10. Only six months ago it was trading at 85.4 US cents.'

a. **Define** the term 'exchange rate'. **2 marks**

b. **Demonstrate** the main risks to an Australian exporting business of excessive fluctuations in exchange rates. **6 marks**

c. **Evaluate** a global financial management strategy businesses can implement to help minimise the risk of exchange rate fluctuations. **6 marks**

Section III — Extended response questions

1. A high debt to equity ratio financed by both short-term and long-term borrowing has led to a decision by a firm to downsize its operations. **Discuss** the effects of such a decision on stakeholders in the business.
2. The following have been identified by management:
   - difficulties in matching cash inflows with outflows
   - declining liquidity
   - declining accounts receivable turn over and expense ratios.

   Write a report to management **recommending** a range of strategies to improve the position of the business.
3. Wax and Wayne is an Australian (private) company that manufactures retro and custom-made surfboards. The company has always been focused on the domestic market but with the increasing worldwide profile of surfing and an expansion in the demographic of the sport they have decided to (slowly) expand into the South East Asian market. This first stage of expansion will require a substantial financial commitment. Explain the influences on financial management that need to be considered in making this decision.
4. A business decides to undervalue its inventories and debtors to indicate favourable liquidity and thus better short-term financial stability of the business. **Discuss** the impacts of this decision.
5. Verada Constructions Limited is an Australian public company specialising in commercial property development. Verada wants to expand its operations by diversifying into residential property development. It is estimated that, to achieve this goal, it will require $85 million of additional finance. Write a report to the management **outlining** the internal and external sources of finance available for such a project. **Determine** which source you consider to be the most appropriate. **Justify** your selection.

Finance: Practice business report — 20 marks

Your answer will be assessed on how well you:
- demonstrate knowledge and understanding relevant to the question
- apply the hypothetical business situation
- communicate using relevant business terminology and concepts
- present a sustained, logical and cohesive response in the form of a business report.

A business, Roo's Outback Eatery Pty Ltd, is opening an additional restaurant in NSW. This will require an extensive marketing campaign and a significant financial investment. The business has recently experienced a loss of market share and declining profits over the last two years.

You have been hired as a consultant to write a report for the owners. In your report:
- discuss TWO sources of finance to be considered by management to facilitate the planned expansion
- explain TWO profitability management strategies for this business.

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Digital document Sample HSC Business Report (doc-14150)

TOPIC

4 Human resources

FOCUS AREA

The focus area of this topic is the contribution of human resource management to business performance.

OUTCOMES CHECKLIST

Students should be able to:

- ☐ evaluate management strategies in response to changes in internal and external influences
- ☐ discuss the social and ethical responsibilities of management
- ☐ analyse business functions and processes in large and global businesses
- ☐ explain management strategies and their impact on businesses
- ☐ evaluate the effectiveness of management in the performance of businesses
- ☐ plan and conduct investigations into contemporary business issues
- ☐ organise and evaluate information for actual and hypothetical business situations
- ☐ communicate business information, issues and concepts in appropriate formats.

CHAPTER SEQUENCE





SNAPSHOT

Case study: Phoning it in — the new normal in business meetings

It is the weekly 9.00 am sales meeting at the Farah Group, an educational software business. Since the initial COVID-19 shutdown, team members have been working remotely.

Team leader Jamie and senior manager Louise are present to welcome everyone through the video conferencing platform.

'Morning everyone,' Jamie begins, 'Hope the weekend was as good as can be expected. Peter, I see you have been out on the water again?'



Peter's background is all trees and water as he sits on his paddleboard next to the river. 'Yeah, great way to start the day! I love the online meetings and working from home.'

Jamie goes on to say that the chances of them returning to the office in the near future are slim. People are being advised to work from home until further notice. 'When we do come back to work, we can only be here in two shifts — the red team and the green team.'

'That sounds like a good idea,' replies Peter, 'but we only need to come in if we have to?'

'When we return to work that is how it will happen,' Jamie replies, 'and people will need to sanitise, wear masks and avoid congregating in kitchens and at watercoolers. I think the government wants you to wear masks on public transport on the way in, too.'

'I hate COVID-19,' says Lara. 'I want to go back to work and have a rest!'

Just then, Lara's 4-year-old granddaughter Pina comes into view and pipes up 'Why are you talking to those people, Nan? Let's play in the cubbyhouse and watch *Bluey* again.'

'See? As much as I love the cubbyhouse, I just can't watch another episode of *Bluey*!'

'Let us know if you need to come in, Lara. I understand it's difficult,' says Jamie reassuringly. 'We have lots of resources here so let me know if you need anything. Remember you can chat with me privately if you are experiencing difficulties working from home.'

online only

16 Kathmandu case study: Human resources

This case study provides detailed information on human resource management at outdoor apparel and equipment retailer Kathmandu, including case study content and exercises.

on Resources

Digital documents	Kathmandu case study: Human resources (doc-35668) Answers for case study (doc-35669)
Weblink	Kathmandu

17 Role of human resource management

17.1 Overview

LEARNING SEQUENCE

17.1 Overview
17.2 The strategic role of human resource management
17.3 Interdependence with other key business functions
17.4 Outsourcing
17.5 Review

Human resource management refers to the management of the total relationship between an **employer** and **employee** in order to achieve the strategic goals of the business. A more contemporary view has brought about a shift in focus in the employee/employer relationship and the re-badging of the title of the traditional human resources department in many organisations. The 'new' human resources function places a higher value on the contribution of the employee to the business than ever before.

Moreover, the human resources department is more likely to be referred to as 'People and culture' or even more simply as 'People' and this is the new lens through which an organisation needs to view all aspects of the role of an employee as a key stakeholder in the effective functioning of the business.

Whatever title is used, human resource management includes functions such as recruitment, equal employment opportunity, training, development, separation and how each can be aligned to achieve business goals.

Effective human resource management sees an employee as an asset rather than a cost, and encourages open communication and goal orientation. It accepts that legitimate differences exist in workplaces but aims to reduce conflict through appropriate procedures and relationships.

human resource management the management of the total relationship between an employer and employee

employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees

employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.

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Digital document Key terms glossary (doc-35670)
Exam question booklet Chapter 17 Exam question booklet (eqb-0039)

17.2 The strategic role of human resource management

SYLLABUS LINK In this subtopic you will learn about the strategic role of human resources.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Businesses need to continually examine ways to improve competitiveness and profitability. Consequently an increasing number of businesses take a strategic (or big picture) approach to managing employees by:

- seeing an effective workforce as a way of adding value to all areas of their business performance, which will invariably involve working cooperatively with the other functional areas of operations, marketing and finance
- focusing on the use of specific human resource management strategies to retain, reward and motivate effective and skilled employees to achieve the business's objectives.

Businesses with effective practices manage change more effectively and this enhances their ability to gain a sustainable competitive advantage. In recent years, governments have also tried to assist businesses in becoming more competitive by creating a more flexible legal framework for human resource management.

FIGURE 17.1 Employees are a business's most valuable resource.



Over the next decade, the major strategic challenges for human resource management are:

- developing and retaining talented staff
- improving leadership development
- managing an ageing workforce
- analysing the increased role of technology
- communicating fully to all stakeholders the company's position on ethics and corporate and social responsibility
- discussing the advantages and disadvantages of outsourcing in a global market.

KEY IDEAS

- Human resource management (HRM) refers to the management of the total relationship between an employer and employee in order to achieve the strategic goals of the business.
- In recent years, governments have tried to assist businesses in becoming more competitive by creating a more flexible legal framework for human resource management.

17.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

17.2 Quick quiz on | **17.2 Exercise** | **17.2 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 4	2, 5	3, 6

17.2 Exercise

Revision

1. **Outline** the role of human resource management.
2. **Distinguish** between an employer and an employee.
3. **Analyse** the changing view of the role of employees in the workplace. Use examples to support your response.
4. **State** the importance of the human resource management role in business success.

Extension

5. **Investigate** the challenges facing human resource managers over the next decade.
6. Research and **analyse** the factors leading to the success of two of the companies currently considered the best human resource managers in the world.

17.2 Exam questions

Question 1 (6 marks)

Source: HSC 2018 Business Studies Exam, Section II, Q22a & b

The annual staff survey at a large retail store has revealed that employees are unmotivated and management does not listen to their suggestions and is unwilling to change. Management is concerned that many employees may leave the company and has brought in a consultant to manage change.

a. Outline the strategic role of human resources in this business. **(2 marks)**

b. Demonstrate how the leadership style of this business has affected employee performance. **(4 marks)**

Question 2 (1 mark)

The general manager of a business has set the goal of international expansion within a six-year period. She has asked the leader of human resources to have his team prepare a workforce for the future. Which statement best describes this situation?

A. Training and development
B. Recruitment
C. Outsourcing
D. Strategic human resource planning

Question 3 (2 marks)

Explain the strategic role of human resources to a successful business.

Question 4 (2 marks)

'We depend on our staff and we will reward them,' states the newly appointed CEO of a large bank.

Describe the importance of human resources to businesses such as this bank.

Question 5 (1 mark)

Outline a strategic role of human resources.

More exam questions are available in your learnON title.

17.3 Interdependence with other key business functions

SYLLABUS LINK In this subtopic you will learn about interdependence with other key business functions and learn to explain the interdependence between human resources and other key business functions.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Human resource managers themselves often understate the **interdependence** between human resources and the other key business functions. For some human resource managers, their role in achieving the business's strategic goals is not clearly apparent. Human resource managers are like the managers of any other functional area in that they have an integral role in whether the business is able to achieve these goals.

In respect to finance, an effective human resource policy within an organisation is linked to profitability gains, share price increases and higher incidence of long-term survival. The link between human resources and marketing is apparent in enduring relationships between the business and its customers. In operations, the managers of those businesses that invest strongly in the relationship between the business and its employees are more likely to see a more efficient and committed contribution to the production of goods and/or services.

BizFACT

The companies that are currently considered as the best in the world at managing employees are Apple, Google, Facebook, Coca-Cola, Deloitte, AT&T, Marriot International, LinkedIn., Goldman Sachs and Twitter. Each of these companies invests heavily in attracting and developing the best workforce. Managers within these businesses are committed to measuring, evaluating, reporting and acting on the results obtained through Key Performance Indicators (KPIs) that rank equally with financial performance indicators.

A concerted effort to improve opportunities for employee training and development and/or rewards has a positive correlation with employee productivity in the operations process. As the manager of a large Australian business recently noted, 'If we take care of our employees they take care of delivering our products, which leaves our customers satisfied which is reflected in our bottom line'.

Most specialist human resource managers are responsible for:

- human resource planning and job design
- acquisition: recruitment, selection and placement
- development: induction, training, career development and performance appraisal
- maintenance of staff: wellbeing, legal responsibilities and communication
- performance management and rewards
- separation
- managing diversity, including the implementation of gender equity and anti-discrimination legislation.

Specialist human resource managers are now more involved in negotiations with unions, establishing and negotiating agreements and preparing for tribunals than they were in the past.

Where the human resources manager is part of the senior executive, he or she collaborates in decisions about strategic issues, such as a change in what is produced or the organisation of work. This role increasingly involves awareness of global trends and labour market issues, industrial relations policies, risk management strategies, and high-level organisational and human resources auditing. Developing a strategic human resources plan, using this information, is a key function. It is then translated into operational plans for implementation.

interdependence the mutual dependence that the key business functions have on one another

SNAPSHOT

Case study: The interdependence between human resources and other key business functions

Google's human resources driving business growth and development

At Google, human resources is central to driving business growth and development. According to Google, it is people that:

> . . . keep Google going and growing. Our People Operations [POps] team (known elsewhere as HR) and administrative staff are the curious and creative colleagues that anchor us to our foundations and help us shoot for the moon. The POps team lives by the mantra 'find them, grow them, keep them,' and is dedicated to staffing, development, and a distinct and inclusive culture. Not just coworkers, we're proud Google colleagues who help our company thrive.



Google's people reflect the type of culture it has built from the outset and continues to develop. Its workplace promotes strong staff involvement and high levels of engagement through a common purpose that embraces the company's vision and goals. The workplace is designed to encourage interaction between staff that often manifests in new ideas for products. Its people-first culture has enabled Google to rank in the top 50 of the world's global companies and be recognised as one of the best employers.

As Google demonstrates, it is the link between human resources and the other functional areas of the business that needs to be managed to ensure a synergy and ultimately business success.
Source: Extracts from https://careers.google.com/fields-of-work/people

Bank of Queensland's human resources and operations

With respect to the human resources and operations functions, many companies acknowledge the importance of corporate social responsibility in the management of their staff. For example, the Bank of Queensland sees a harmonious work environment as integral to business success. It identifies the responsibility it has to its employees and the importance of the employee/management relationship in respect to the diversity of staff in its branches who reflect the multicultural character of the nation. It pursues the best employees in a recruitment and selection process that is both fair and equitable and provides employees with a formal program of support through confidential counselling. It has an ongoing commitment to professional learning and development, offering flexible work arrangements such as part-time, work from home and job share options and additional benefits such as health information, discounts on loans and travel.

Interdependence at Kathmandu (human resources and marketing)

Kathmandu (which is the major case study in this title) is an example of how the relationship between staff and marketing is linked to ongoing success. The managers at the business seek to employ those people that align their own environmentally sustainable approach to that of the business, recognise that its team of workers seek opportunities to develop skills through the initial induction process, regular training and development sessions, and provide generous financial incentives. In addition, employees are encouraged to see this approach to human resource management as an opportunity to seek customer-focused, long-term retail careers.

Kathmandu's marketing approach involves consolidating its reputation as an inspirational, iconic brand synonymous with adventure, innovation and passion. Its core purpose is to 'inspire and equip the adventurer in everyone'. The benefit of having its customer sales representatives endorsing this brand philosophy is that Kathmandu is able to deliver the best customer experience at all times with authentic experience-based service.

Human resources and finance: cutting costs

As staffing is a major cost associated with the operation of a business, there is a clear link between human resources and finance. Workers contribute to the production of the goods and services demanded by customers and this in turn generates income for the business. In a competitive environment that demands effective cost control and maintaining or even reducing labour costs, this is seen as essential to a business's financial wellbeing.

Changes in the manufacturing sector in the last 30 years have resulted in the closure of factories and in some cases their relocation overseas. For example, the decline in the automotive industry and subsequent impact on its staff had much to do with financial decisions. Businesses engaged in other sectors (such as telecommunications including Telstra, banking including NAB, Westpac and ANZ, and aviation including Qantas) have either moved operations offshore or are considering how best to facilitate this, primarily with a financial motivation.

The common theme to the changes outlined above is the desire to cut costs, especially those in relation to labour. Australia's higher wage rates mean that, for example, an administrative worker is six times more expensive to hire in Australia than in the Philippines and other employment expenses such as superannuation have an impact on the profitability of many businesses. Estimates are that operational costs can be reduced by up to 60 per cent by relocating production offshore, with wages accounting for 20 per cent of those savings, affecting financial results significantly.

KEY IDEAS

- In large businesses, a specialist human resources team or manager is responsible for the business's human resource management.
- Most specialist human resource managers are responsible for:
  - human resource planning and job design
  - acquisition — recruitment, selection and placement
  - development — induction, training, career development and performance appraisal
  - maintenance of staff — wellbeing, legal responsibilities and communication
  - performance management and rewards
  - separation
  - managing diversity, including the implementation of gender equity and anti-discrimination legislation.
- Where the human resource manager is part of the senior executive, he or she collaborates in executive decisions about strategic issues, such as a change in product, service or organisation of work.
- Many firms outsource specialist human resource management functions.

17.3 Activities

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17.3 Quick quiz on | **17.3 Exercise** | **17.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2	5, 6, 7	3, 4

17.3 Exercise

Revision

Read the 'Phoning it in — the new normal in business meetings' case study in the topic 4 opener and answer questions 1 to 5.

1. **Outline** the changes to the work structure at The Farah Group since the COVID-19 shutdown.
2. **Describe** how the 'new normal' being established at the business reflects key influences in human resource management including technology, ethics and corporate social responsibility.
3. **Analyse** the corporate culture at the Farah Group. Do you think it would be a good place to work?
4. **Evaluate** the effects of working from home on Peter and Lara. Are there potential issues that may arise should this situation continue indefinitely?

5. **Discuss** how the changes brought on by COVID-19 could benefit the future organisation of work at the business.

Extension

6. Read 'The interdependence between human resources and other key business functions' case study. **Explain** the interdependence between human resources and the other key business functions at each of the businesses in this case study.
7. **Investigate** the activities human resource managers may undertake at a strategic, tactical and operational level in a business.

17.3 Exam questions

Question 1 (1 mark)

The human resources team has designed a job and its staffing requirements based on task design information. This shows interdependence between human resources and which key function?

A. Marketing
B. Finance
C. Operations
D. Production

Question 2 (1 mark)

The human resources team is using performance-based rewards. This needs to stay within budget. This shows interdependence between human resources and which key function?

A. Marketing
B. Finance
C. Operations
D. Production

Question 3 (3 marks)

Project into the role as an employee in the People and culture section of a medium-sized business. You have been asked to prepare a summary to justify the creation of a management position for your section.

Question 4 (6 marks)

The senior management of a business wants the key functions to work more closely together to make the business more team-oriented. Explain how human resources can work with other key functions to achieve better business outcomes.

More exam questions are available in your learnON title.

17.4 Outsourcing

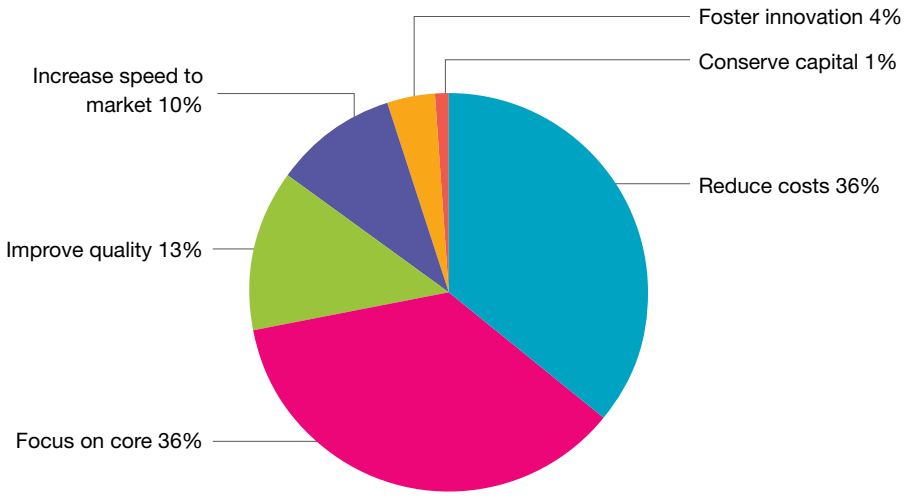
SYLLABUS LINK In this subtopic you will learn about outsourcing the human resource functions as well as how a business uses contractors both domestically and globally and learn to discuss the advantages and disadvantages of outsourcing in the global market.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Many changes in work patterns today are driven by a business's need to reduce costs and improve productivity. Globalisation and rapid technological change have led to increased pressure to be competitive. These factors have fostered the development of new organisational structures, with the growth of contracting out or outsourcing business functions. Outsourcing or contracting out business functions involves the use of third-party businesses such as recruitment firms. It aims to take advantage of the skills provided by the specialist and to achieve a reduction in labour costs.

Outsourcing is often used to obtain a superior service, better functional quality and a lower cost service than would be provided internally (see figure 17.2). Outsourcing, particularly offshore (global subcontracting), may significantly reduce costs for some businesses. Major areas being outsourced in Australia (domestic outsourcing) are property and facilities management, financial processes such as payroll, administration support services, internal auditing, call centres, maintenance and, most commonly, human resources functions.

FIGURE 17.2 Top reasons for outsourcing



17.4.1 Outsourcing human resource functions

Outsourcing allows firms to focus more on their core business as they grow, while experts in human resources assist by planning for growth, development and management of staff during this phase.

Outsourcing may also be used to review business practices and implement strategies to transform the business using 'independent' consultants with no perceived internal 'agenda'.

outsourcing contracting out business functions involving the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

TABLE 17.1 Most commonly outsourced human resource functions and areas

Human resource functions commonly outsourced	Human resource areas commonly outsourced for review or development
Recruitment	Human resources information systems (HRIS)
Induction	Change management
Leadership training	Payroll
Mediation	Training needs evaluation
Outplacement	Compensation (wages and salaries) systems
Payroll	Performance management systems
	Succession planning
	High performance coaching
	Employee surveys
	Written policies and programs
	Training and development
	Benchmarking

17.4.2 Using contractors

Today, **contractors** are primarily used by most businesses to create costs savings or to access greater expertise and capabilities to improve competitiveness. Contractors can be obtained for most business functions, but they are particularly used for processing functions. These are the functions that are repetitive and easily measured, which makes it easy for businesses to determine the cost savings and productivity gains.

Contracting is generally recommended for non-core functions, allowing staff to focus on the broader aspects of managing a firm.

Although there are many successful examples of outsourcing, there are risks, which increase as the proportion of a firm's activities are outsourced. The major risks include cost overruns (or cost increase), loss of quality, difficulty coordinating activities, and difficulty monitoring quality and performance in outsourced activities. In one major Australian firm, outsourcing maintenance to avoid industrial problems led to a loss of its competitive advantage. Where it had previously been proactive in managing maintenance, it became more reactive in the hands of its contractors and breakdowns in production proved to be costly.

Experience shows that businesses should set clear and legally binding terms, timeframes and conditions in a contractor agreement to avoid conflict and expensive litigation further down the track. This includes confirming responsibility for superannuation, insurance and workers' compensation.

Domestic subcontracting

Domestic subcontracting is very common today and avoids the need to employ additional 'in-house' staff, along with all the overhead expenses involved. It allows firms to focus their resources on essential business activities, leaving some of the detailed support- or compliance-related activities to experts, such as payroll management or order fulfilment. Others seek the benefits of fresh ideas and perspectives such as leadership development. This makes it particularly attractive to small to medium-sized businesses lacking the capacity to undertake internal auditing, compliance updates, research or manage some functions at the professional 'best practice' level of larger firms. Using this expertise, therefore, has the potential to improve the quality and productivity of a business's service without the resource scale normally required to achieve this level.

contractor an external provider of services to a business. It may be an individual or a business.

TABLE 17.2 Features of the most common forms of outsourcing

Form of outsourcing	Features
Labour hire/employment agency	• Workers are employees provided to the host company. • Superannuation, insurance and workers' compensation are managed by the labour hire company.
Labour hire/employment agencies/dependent contractors	• Workers are dependent contractors. Labour hire company may act as a broker. • They do not have control over their working procedures. They are prevented from subcontracting their work and from working for multiple clients.
Independent contractors	• They operate their own business and set the terms and conditions of employment. • They are engaged by a client under a commercial contract to perform the services without having the legal status of an employee. • Most independent contractors make their own superannuation, insurance and workers' compensation arrangements.
Outsourced suppliers	• They supply goods and services to a range of businesses. • They are owner managers who supervise their own employees. • They control their own work procedures and can work for multiple clients. • They manage superannuation, insurance and workers' compensation arrangements for their employees.

BizFACT

There are 1.1 million independent contractors in Australia.

SNAPSHOT

Case study: Australian Business Solutions Group



Australian Business Solutions Group (ABSG) seeks to assist businesses through the provision of expert specialist services across a number of functional areas including human resources. The aspects of human resources that it offers support for include performance management, workplace agreements and mediation as well as the processes of recruitment, selection, maintenance and separation.

One particular area of expertise offered by ABSG is its OnePeople HR program. This initiative assists businesses in the recruitment of top Aboriginal and Torres Strait Islander (ATSI) talent by providing businesses with expert strategies in locating suitable candidates whether they are seeking them on a permanent or temporary basis.

OnePeople HR has had particular success with its Aboriginal and Torres Strait Islander mentoring program. It provides specialist training to existing management to promote higher engagement of ATSI employees through:

- developing strategies to improve staff retention
- increasing the number of Indigeneous managers
- strengthening existing staff relationships
- promoting diversity in the workplace.



Source: © Business Australia www.businessaustralia.com

Global subcontracting

During the last decade, many firms under pressure from global competition turned to offshore contractors in countries such as India and the Philippines to reduce costs. Others used outsourcing as a first step toward operating in a new market overseas, to get more acquainted with market needs before expanding with a greater physical presence in the market.

BizFACT

Deloitte's most recent *Global Outsourcing Survey 2018* has identified the drift away from traditional outsourcing to disruptive outsourcing. Disruptive outsourcing involves the use of improved technological development in robotics, automation and cloud computing and is beginning to compete with traditional outsourcing solutions. Its emergence is largely due to cost benefits as well the identification of a clear competitive advantage by changing the way that businesses operate through agility, efficiency and increased effectiveness. This in turn increases revenue and can lead to business growth.

Outsourcing may take two forms.

1. *Process outsourcing* is the dominant form of outsourcing of repetitive, easily measured and documented work — for example, recruitment, multi-country payroll management, customer complaints, food preparation for an airline or garment manufacture for an Australian fashion company.
2. *Project outsourcing* is most commonly found in areas such as human resources, marketing, design, information technology (IT) and research. Project outsourcing involves much greater use of intellectual property and strategic business knowledge; it tends to operate in a longer time frame, is more difficult to measure and the quality cannot be fully anticipated, thus carrying more risk.

Global outsourcing carries some risks, including:

- difficulty controlling the quality and reliability of the service
- cultural differences such as language or accent issues, which may impact on customer service
- security issues such as opportunities for sharing of confidential company information and client poaching
- the lack of remedies for breach of contract or other legal matters under foreign legal systems
- the often high labour turnover particularly experienced in call centres
- well-qualified employees may be replaced by less qualified staff, causing the quality of the service to decline.

These disadvantages need to be weighed up against the benefits of major cost savings and potential productivity benefits.

Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

The advantages and disadvantages of outsourcing in a global market

FIGURE 17.3 Advantages and disadvantages of global outsourcing of human resources



A different view to global outsourcing has emerged since the COVID-19 pandemic of 2020. In many cases the managers of some of Australia's largest companies in the telecommunications, finance, government and other service industries found that many of the businesses contracted to carry out various functions were unavailable with little notice. Call centres, IT support and other process outsourced activities were severely disrupted.

Traditional outsourcing countries such as India and the Philippines operated with minimal staff or shut down completely. Unlike companies in Australia, working remotely was not a viable option for staff due to inadequate technology, ill-equipped telecommunications infrastructure and a lack of suitable work-from-home options.

While some Australian-based businesses did have some contingencies in place if an overseas partner was unable to continue with existing services, the scale of the pandemic was unprecedented and an immediate response for many was to bring many services back in-house.

SNAPSHOT

Case study: Telstra's outsourcing in a post-COVID-19 global business environment

India and the Philippines have for some time been the favoured location of the global call centre industry.



The emphasis on higher levels of customer service and the widespread use of English have consolidated these two countries as a trusted place to outsource customer service for a range of businesses including Australia's telecommunications market leader Telstra.

Telstra has sought to shore up its market domination through its strategic management of its resources.

The 'T22 strategy' was created to assist in Telstra's attempt to lead the Australian market by simplifying its operations and products, improving customer experience and reducing its cost base.

One of the details contained within the 'T22 strategy' was the decision to outsource 1500 call-centre jobs to Bangalore, India. The impact of the global pandemic in India (and in its other call centre location in the Philippines) meant that Telstra's overseas call centres were immediately shut down. Telstra's management responded by employing 3500 local staff members to replace the overseas call centre customer service operators and has indicated that the loss of the overseas call centres had led to a review on how to better deal with customer complaints.

Management has determined that future demands will require a higher level of customer service if it is to maintain its market dominance.

Telstra management has decided that its offshore call centre partners will be scaled down and the temporary use of local operators in response to the global pandemic will be maintained.

KEY IDEAS

- New business structures are developing in response to global competition.
- Outsourcing business functions to reduce costs, obtain specialist support and improve productivity is increasing.
- Many firms outsource specialist human resource functions such as recruitment and payroll.
- There has been a rapid growth in independent contractors, such as labour hire companies.
- Businesses generally find that outsourcing is most effective internationally when the business functions being outsourced are suitable for teleworking.
- There are benefits and risks in contracting, from lower costs, to the problem of loss of direct customer contact, and consistent quality and performance in outsourced activities.
- Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

17.4 Activities

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17.4 Quick quiz on | **17.4 Exercise** | **17.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5, 6, 7, 9	3, 10, 11, 12, 13, 14, 15, 16, 19, 21	8, 17, 20

17.4 Exercise

Revision

1. **What** is 'outsourcing'?
2. **Identify** the most appropriate term from the list to complete the following sentences.

quality	internally	costs	lower	offshore	superior

Outsourcing is often used to obtain a _____ service, better functional _____ and a _____ cost service than that would be provided _____. Outsourcing, particularly global subcontracting, may significantly reduce _____ for some businesses.

3. **Examine** figure 17.2 and list the four most common reasons for outsourcing.
4. **Identify** six human resource functions that are often outsourced.

Read the 'Australian Business Solutions Group' case study and answer questions 5 to 7.

5. **List** the human resource services that ABSG offers.
6. **What** is OnePeople HR?
7. **Outline** the advantages to a business of programs such as the Aboriginal and Torres Strait Islander mentoring program.
8. You are a human resource manager for a construction business that has 568 employees. The general manager has asked you to consider using contractors for a number of business functions including machine maintenance and accounts preparation. Prepare a report.
   a. Outline the costs and benefits of using contractors. Present your information in a 'T' table format as shown below. The 'T' table has been started for you.

Using contractors	
Costs	Benefits • Creates savings

   b. **Assess** the value of using contractors.
9. **Outline** the key features needed in agreements for successful outsourcing.
10. **Distinguish** between domestic and global subcontracting.
11. **Examine** figure 17.3. **Justify** which you consider to be the more persuasive: the potential advantages or potential disadvantages of global outsourcing of human resources.
12. **Why** is outsourcing important to the evolution of human resource management?

Read the 'Telstra's outsourcing in a post-COVID-19 global business environment' case study and answer questions 13 to 15.

13. **Why** are countries such as India and the Philippines seen as favourable locations for outsourcing by companies based in Australia?
14. **How** did the global pandemic impact companies such as Telstra?
15. **Discuss** the effect of the decision to outsource important activities such as call centres on Australia's economy.

Extension

16. Research the human resources processes and practices of two of the companies listed in the BizFACT at the start of subtopic 17.3. **Compare** and **contrast** these in a tabular form.
17. 'The role of human resources has been evolving for many years now. What was once the "personnel" department has been replaced by a sophisticated key business function with management keen to have a say in the strategic planning process.' **Human resources specialist at TA Industries**
    Analyse the ways in which the role of human resource management is changing.
18. 'I am sick and tired of ringing a call centre only to have to wait for half an hour, finally getting someone to talk to only to be transferred to another operator, getting cut off and having to start all over again.' Write a report on the advantages and disadvantages of outsourcing call centres.
19. **Propose** a range of business activities that would be suited for outsourcing to either domestic or global contractors.
20. **Predict** the future of both domestic and global outsourcing.
21. **Discuss** the ways in which human resource managers can ensure that high standards in quality and customer service are maintained as business structures evolve on a global scale.

17.4 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q3

A firm has been hiring its own staff but due to growth no longer has time to satisfactorily manage this process. What could the firm's human resource manager use to resolve this issue?

A. Acquisition
B. Outsourcing
C. Recruitment
D. Selection

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q15

What is a benefit to an Australian clothing company of outsourcing its manufacturing overseas?

A. It can control the production costs.
B. It can lower human resource compliance costs.
C. It can decide which particular employees manufacture its products.
D. It can consider the foreign manufacturer's workers as its own employees.

Question 3 (6 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q23

Heather owns a financial planning business with offices in four countries, including Australia. Heather outsources the cleaning of her Sydney office.

a. Explain ONE advantage of this strategy. **(2 marks)**
b. Heather also outsources all her financial record keeping. Explain TWO disadvantages of this strategy. **(4 marks)**

Question 4 (1 mark)

Source: Adapted from HSC 2008 Business Studies Exam, Section I, Q4

To reduce costs, a business employs external contractors to provide payroll services.

Which term describes this strategy?

A. Acquisition
B. Outsourcing
C. Recruitment
D. Performance management

Question 5 (6 marks)

Source: HSC 2008 Business Studies Exam, Section II, Q23b

Edpro designs software and employs its own software programming team. It plans to outsource programming in 2009.

Analyse the possible impact on management AND employees of outsourcing programming.

More exam questions are available in your learnON title.

17.5 Review

17.5.1 Summary

The strategic role of human resource management

- Human resource management (HRM) refers to the management of the total relationship between an employer and employee in order to achieve the strategic goals of the business.
- In recent years, governments have tried to assist businesses in becoming more competitive by creating a more flexible legal framework for human resource management.

Interdependence with other key business functions

- In large businesses, a specialist human resources team or manager is responsible for the business's human resource management.
- Most specialist human resource managers are responsible for:
  - human resource planning and job design
  - acquisition — recruitment, selection and placement
  - development — induction, training, career development and performance appraisal
  - maintenance of staff — wellbeing, legal responsibilities and communication
  - performance management and rewards
  - separation
  - managing diversity, including the implementation of gender equity and anti-discrimination legislation.
- Where the human resource manager is part of the senior executive, he or she collaborates in executive decisions about strategic issues, such as a change in product, service or organisation of work.
- Many firms outsource specialist human resource management functions.

Outsourcing

- New business structures are developing in response to global competition.
- Outsourcing business functions to reduce costs, obtain specialist support and improve productivity is increasing.
- Many firms outsource specialist human resource functions such as recruitment and payroll.
- There has been a rapid growth in independent contractors, such as labour hire companies.
- Businesses generally find that outsourcing is most effective internationally when the business functions being outsourced are suitable for teleworking.
- There are benefits and risks in contracting, from lower costs, to the problem of loss of direct customer contact, and consistent quality and performance in outsourced activities.
- Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

17.5.2 Key terms

contractor an external provider of services to a business. It may be an individual or a business.
employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.
employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees
human resource management the management of the total relationship between an employer and employee
interdependence the mutual dependence that the key business functions have on one another
outsourcing contracting out business functions involving the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

Resources

Digital documents	Key terms glossary (doc-35670) Chapter crossword (doc-36222)
Interactivity	Chapter crossword (int-7173)
Exam question booklet	Chapter 17 Exam question booklet (eqb-0039)

17.5 Activities

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Exercise 1: Multiple choice questions

1. Management of HRM is very important as
   - **A.** over the next decade there are major pressures from an ageing workforce.
   - **B.** outsourcing is increasing.
   - **C.** labour is generally around 60 per cent of operational costs.
   - **D.** governments are increasing the compliance requirements for human resource management.

2. Strategic HRM focuses on which of the following?
   - **A.** Negotiation with unions, establishing and negotiating agreements, awareness of global labour market issues
   - **B.** Collaboration with executive on organisational changes, induction, training, career development and performance appraisal
   - **C.** Recruitment, selection and placement, HR auditing
   - **D.** Collaboration with executive on a change in product or other issues, global trend analysis and risk management

3. A training and development officer has been appointed in a business. In which function will their work be carried out?
   - **A.** Human resources
   - **B.** Operations
   - **C.** Marketing
   - **D.** Finance

4. What are the most commonly outsourced HR functions?
   - **A.** Change management and training
   - **B.** High performance coaching and succession planning
   - **C.** Compensation and performance management systems
   - **D.** Outplacement, mediation and payroll

5. Best practice strategies for reducing risks of outsourcing do not include
   - **A.** setting clear and legally binding terms.
   - **B.** management of the recruitment of appropriate staff.
   - **C.** confirming responsibility for superannuation, insurance and workers compensation.
   - **D.** setting clear timeframes and conditions for contacts.

6. Domestic subcontracting would be most useful for
   - **A.** a major bank wishing to obtain financial expertise.
   - **B.** a major brick company wishing to have a new brick manufactured.
   - **C.** a small baker seeking a loan.
   - **D.** a pet boarding agency seeking expert veterinary knowledge.

7. Specialist HR companies like Seek.com assist other companies with outsourced function such as
   - **A.** providing advice on the construction of company profiles for job seekers.
   - **B.** providing advice on financial options for customers.
   - **C.** providing design ideas for new products.
   - **D.** providing advice on outplacement services.

8. Functions which are more suited to outsourcing
   - **A.** are those which can be clearly identified, repeated, staffed and supported by a legally binding framework.
   - **B.** are those which can be clearly identified, measured, managed and supported by a legally binding framework.
   - **C.** need to be weighed up against the benefits of major cost savings.
   - **D.** involve more repetitive, easily measured and simple work.

9. Two potential disadvantages of outsourcing include which of the following?
   - **A.** Consultants may not understand your culture, training costs may fall
   - **B.** Legal compliance increases, hidden costs emerge
   - **C.** Security risk, increased business learning through reliance on experts
   - **D.** Culture may be transformed, capital may be lost

10. In Australia, the main reason for outsourcing is
    - **A.** increase speed to market.
    - **B.** improve quality.
    - **C.** focus on core.
    - **D.** conserve capital.

Exercise 2: Exam practice questions

Question 1 (2 marks)
Outline the strategic role of human resources.

Question 2 (3 marks)
Explain the role of interdependence between human resources and one other key business function.

Question 3 (6 marks)
a. **What** is outsourcing? **(2 marks)**
b. **Discuss** the decision to outsource human resources functions. **(4 marks)**

Question 4 (4 marks)
Distinguish between domestic and global contractors.

Question 5 (5 marks)
Analyse the role of human resource management in business.

Question 6 (4 marks)
Assess the role of outsourcing in a global market.

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SNAPSHOT

Case study: The interdependence between human resources and other key business functions

Google's human resources driving business growth and development

At Google, human resources is central to driving business growth and development. According to Google, it is people that:

> . . . keep Google going and growing. Our People Operations [POps] team (known elsewhere as HR) and administrative staff are the curious and creative colleagues that anchor us to our foundations and help us shoot for the moon. The POps team lives by the mantra 'find them, grow them, keep them,' and is dedicated to staffing, development, and a distinct and inclusive culture. Not just coworkers, we're proud Google colleagues who help our company thrive.



Google's people reflect the type of culture it has built from the outset and continues to develop. Its workplace promotes strong staff involvement and high levels of engagement through a common purpose that embraces the company's vision and goals. The workplace is designed to encourage interaction between staff that often manifests in new ideas for products. Its people-first culture has enabled Google to rank in the top 50 of the world's global companies and be recognised as one of the best employers.

As Google demonstrates, it is the link between human resources and the other functional areas of the business that needs to be managed to ensure a synergy and ultimately business success.
Source: Extracts from https://careers.google.com/fields-of-work/people

Bank of Queensland's human resources and operations

With respect to the human resources and operations functions, many companies acknowledge the importance of corporate social responsibility in the management of their staff. For example, the Bank of Queensland sees a harmonious work environment as integral to business success. It identifies the responsibility it has to its employees and the importance of the employee/management relationship in respect to the diversity of staff in its branches who reflect the multicultural character of the nation. It pursues the best employees in a recruitment and selection process that is both fair and equitable and provides employees with a formal program of support through confidential counselling. It has an ongoing commitment to professional learning and development, offering flexible work arrangements such as part-time, work from home and job share options and additional benefits such as health information, discounts on loans and travel.

Interdependence at Kathmandu (human resources and marketing)

Kathmandu (which is the major case study in this title) is an example of how the relationship between staff and marketing is linked to ongoing success. The managers at the business seek to employ those people that align their own environmentally sustainable approach to that of the business, recognise that its team of workers seek opportunities to develop skills through the initial induction process, regular training and development sessions, and provide generous financial incentives. In addition, employees are encouraged to see this approach to human resource management as an opportunity to seek customer-focused, long-term retail careers.

Kathmandu's marketing approach involves consolidating its reputation as an inspirational, iconic brand synonymous with adventure, innovation and passion. Its core purpose is to 'inspire and equip the adventurer in everyone'. The benefit of having its customer sales representatives endorsing this brand philosophy is that Kathmandu is able to deliver the best customer experience at all times with authentic experience-based service.

Human resources and finance: cutting costs

As staffing is a major cost associated with the operation of a business, there is a clear link between human resources and finance. Workers contribute to the production of the goods and services demanded by customers and this in turn generates income for the business. In a competitive environment that demands effective cost control and maintaining or even reducing labour costs, this is seen as essential to a business's financial wellbeing.

Changes in the manufacturing sector in the last 30 years have resulted in the closure of factories and in some cases their relocation overseas. For example, the decline in the automotive industry and subsequent impact on its staff had much to do with financial decisions. Businesses engaged in other sectors (such as telecommunications including Telstra, banking including NAB, Westpac and ANZ, and aviation including Qantas) have either moved operations offshore or are considering how best to facilitate this, primarily with a financial motivation.

The common theme to the changes outlined above is the desire to cut costs, especially those in relation to labour. Australia's higher wage rates mean that, for example, an administrative worker is six times more expensive to hire in Australia than in the Philippines and other employment expenses such as superannuation have an impact on the profitability of many businesses. Estimates are that operational costs can be reduced by up to 60 per cent by relocating production offshore, with wages accounting for 20 per cent of those savings, affecting financial results significantly.

KEY IDEAS

- In large businesses, a specialist human resources team or manager is responsible for the business's human resource management.
- Most specialist human resource managers are responsible for:
  - human resource planning and job design
  - acquisition — recruitment, selection and placement
  - development — induction, training, career development and performance appraisal
  - maintenance of staff — wellbeing, legal responsibilities and communication
  - performance management and rewards
  - separation
  - managing diversity, including the implementation of gender equity and anti-discrimination legislation.
- Where the human resource manager is part of the senior executive, he or she collaborates in executive decisions about strategic issues, such as a change in product, service or organisation of work.
- Many firms outsource specialist human resource management functions.

17.3 Activities

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17.3 Quick quiz on | **17.3 Exercise** | **17.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2	5, 6, 7	3, 4

17.3 Exercise

Revision

Read the 'Phoning it in — the new normal in business meetings' case study in the topic 4 opener and answer questions 1 to 5.

1. **Outline** the changes to the work structure at The Farah Group since the COVID-19 shutdown.
2. **Describe** how the 'new normal' being established at the business reflects key influences in human resource management including technology, ethics and corporate social responsibility.
3. **Analyse** the corporate culture at the Farah Group. Do you think it would be a good place to work?
4. **Evaluate** the effects of working from home on Peter and Lara. Are there potential issues that may arise should this situation continue indefinitely?

5. **Discuss** how the changes brought on by COVID-19 could benefit the future organisation of work at the business.

Extension

6. Read 'The interdependence between human resources and other key business functions' case study. **Explain** the interdependence between human resources and the other key business functions at each of the businesses in this case study.
7. **Investigate** the activities human resource managers may undertake at a strategic, tactical and operational level in a business.

17.3 Exam questions

Question 1 (1 mark)

The human resources team has designed a job and its staffing requirements based on task design information. This shows interdependence between human resources and which key function?

A. Marketing
B. Finance
C. Operations
D. Production

Question 2 (1 mark)

The human resources team is using performance-based rewards. This needs to stay within budget. This shows interdependence between human resources and which key function?

A. Marketing
B. Finance
C. Operations
D. Production

Question 3 (3 marks)

Project into the role as an employee in the People and culture section of a medium-sized business. You have been asked to prepare a summary to justify the creation of a management position for your section.

Question 4 (6 marks)

The senior management of a business wants the key functions to work more closely together to make the business more team-oriented. Explain how human resources can work with other key functions to achieve better business outcomes.

More exam questions are available in your learnON title.

17.4 Outsourcing

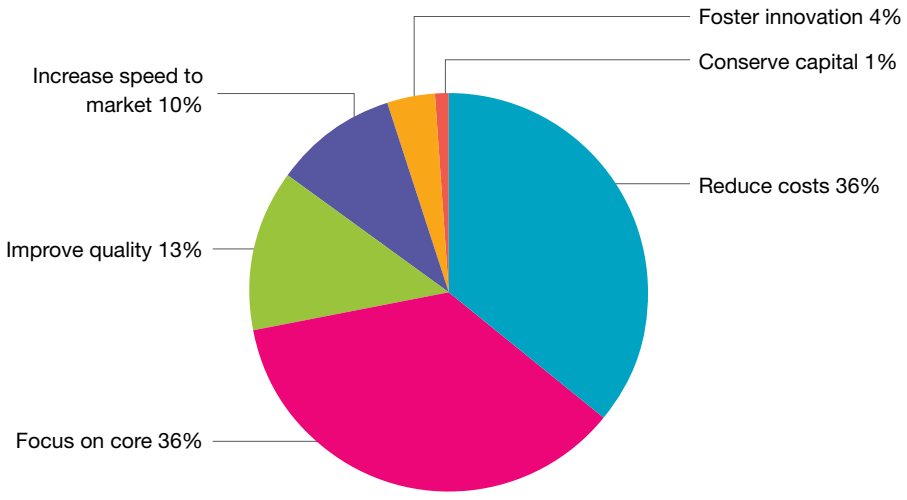
SYLLABUS LINK In this subtopic you will learn about outsourcing the human resource functions as well as how a business uses contractors both domestically and globally and learn to discuss the advantages and disadvantages of outsourcing in the global market.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Many changes in work patterns today are driven by a business's need to reduce costs and improve productivity. Globalisation and rapid technological change have led to increased pressure to be competitive. These factors have fostered the development of new organisational structures, with the growth of contracting out or outsourcing business functions. Outsourcing or contracting out business functions involves the use of third-party businesses such as recruitment firms. It aims to take advantage of the skills provided by the specialist and to achieve a reduction in labour costs.

Outsourcing is often used to obtain a superior service, better functional quality and a lower cost service than would be provided internally (see figure 17.2). Outsourcing, particularly offshore (global subcontracting), may significantly reduce costs for some businesses. Major areas being outsourced in Australia (domestic outsourcing) are property and facilities management, financial processes such as payroll, administration support services, internal auditing, call centres, maintenance and, most commonly, human resources functions.

FIGURE 17.2 Top reasons for outsourcing



17.4.1 Outsourcing human resource functions

Outsourcing allows firms to focus more on their core business as they grow, while experts in human resources assist by planning for growth, development and management of staff during this phase.

Outsourcing may also be used to review business practices and implement strategies to transform the business using 'independent' consultants with no perceived internal 'agenda'.

outsourcing contracting out business functions involving the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

TABLE 17.1 Most commonly outsourced human resource functions and areas

Human resource functions commonly outsourced	Human resource areas commonly outsourced for review or development
Recruitment	Human resources information systems (HRIS)
Induction	Change management
Leadership training	Payroll
Mediation	Training needs evaluation
Outplacement	Compensation (wages and salaries) systems
Payroll	Performance management systems
	Succession planning
	High performance coaching
	Employee surveys
	Written policies and programs
	Training and development
	Benchmarking

17.4.2 Using contractors

Today, **contractors** are primarily used by most businesses to create costs savings or to access greater expertise and capabilities to improve competitiveness. Contractors can be obtained for most business functions, but they are particularly used for processing functions. These are the functions that are repetitive and easily measured, which makes it easy for businesses to determine the cost savings and productivity gains.

Contracting is generally recommended for non-core functions, allowing staff to focus on the broader aspects of managing a firm.

Although there are many successful examples of outsourcing, there are risks, which increase as the proportion of a firm's activities are outsourced. The major risks include cost overruns (or cost increase), loss of quality, difficulty coordinating activities, and difficulty monitoring quality and performance in outsourced activities. In one major Australian firm, outsourcing maintenance to avoid industrial problems led to a loss of its competitive advantage. Where it had previously been proactive in managing maintenance, it became more reactive in the hands of its contractors and breakdowns in production proved to be costly.

Experience shows that businesses should set clear and legally binding terms, timeframes and conditions in a contractor agreement to avoid conflict and expensive litigation further down the track. This includes confirming responsibility for superannuation, insurance and workers' compensation.

Domestic subcontracting

Domestic subcontracting is very common today and avoids the need to employ additional 'in-house' staff, along with all the overhead expenses involved. It allows firms to focus their resources on essential business activities, leaving some of the detailed support- or compliance-related activities to experts, such as payroll management or order fulfilment. Others seek the benefits of fresh ideas and perspectives such as leadership development. This makes it particularly attractive to small to medium-sized businesses lacking the capacity to undertake internal auditing, compliance updates, research or manage some functions at the professional 'best practice' level of larger firms. Using this expertise, therefore, has the potential to improve the quality and productivity of a business's service without the resource scale normally required to achieve this level.

contractor an external provider of services to a business. It may be an individual or a business.

TABLE 17.2 Features of the most common forms of outsourcing

Form of outsourcing	Features
Labour hire/employment agency	• Workers are employees provided to the host company. • Superannuation, insurance and workers' compensation are managed by the labour hire company.
Labour hire/employment agencies/dependent contractors	• Workers are dependent contractors. Labour hire company may act as a broker. • They do not have control over their working procedures. They are prevented from subcontracting their work and from working for multiple clients.
Independent contractors	• They operate their own business and set the terms and conditions of employment. • They are engaged by a client under a commercial contract to perform the services without having the legal status of an employee. • Most independent contractors make their own superannuation, insurance and workers' compensation arrangements.
Outsourced suppliers	• They supply goods and services to a range of businesses. • They are owner managers who supervise their own employees. • They control their own work procedures and can work for multiple clients. • They manage superannuation, insurance and workers' compensation arrangements for their employees.

BizFACT

There are 1.1 million independent contractors in Australia.

SNAPSHOT

Case study: Australian Business Solutions Group



Australian Business Solutions Group (ABSG) seeks to assist businesses through the provision of expert specialist services across a number of functional areas including human resources. The aspects of human resources that it offers support for include performance management, workplace agreements and mediation as well as the processes of recruitment, selection, maintenance and separation.

One particular area of expertise offered by ABSG is its OnePeople HR program. This initiative assists businesses in the recruitment of top Aboriginal and Torres Strait Islander (ATSI) talent by providing businesses with expert strategies in locating suitable candidates whether they are seeking them on a permanent or temporary basis.

OnePeople HR has had particular success with its Aboriginal and Torres Strait Islander mentoring program. It provides specialist training to existing management to promote higher engagement of ATSI employees through:

- developing strategies to improve staff retention
- increasing the number of Indigeneous managers
- strengthening existing staff relationships
- promoting diversity in the workplace.



Source: © Business Australia www.businessaustralia.com

Global subcontracting

During the last decade, many firms under pressure from global competition turned to offshore contractors in countries such as India and the Philippines to reduce costs. Others used outsourcing as a first step toward operating in a new market overseas, to get more acquainted with market needs before expanding with a greater physical presence in the market.

BizFACT

Deloitte's most recent *Global Outsourcing Survey 2018* has identified the drift away from traditional outsourcing to disruptive outsourcing. Disruptive outsourcing involves the use of improved technological development in robotics, automation and cloud computing and is beginning to compete with traditional outsourcing solutions. Its emergence is largely due to cost benefits as well the identification of a clear competitive advantage by changing the way that businesses operate through agility, efficiency and increased effectiveness. This in turn increases revenue and can lead to business growth.

Outsourcing may take two forms.

1. *Process outsourcing* is the dominant form of outsourcing of repetitive, easily measured and documented work — for example, recruitment, multi-country payroll management, customer complaints, food preparation for an airline or garment manufacture for an Australian fashion company.
2. *Project outsourcing* is most commonly found in areas such as human resources, marketing, design, information technology (IT) and research. Project outsourcing involves much greater use of intellectual property and strategic business knowledge; it tends to operate in a longer time frame, is more difficult to measure and the quality cannot be fully anticipated, thus carrying more risk.

Global outsourcing carries some risks, including:

- difficulty controlling the quality and reliability of the service
- cultural differences such as language or accent issues, which may impact on customer service
- security issues such as opportunities for sharing of confidential company information and client poaching
- the lack of remedies for breach of contract or other legal matters under foreign legal systems
- the often high labour turnover particularly experienced in call centres
- well-qualified employees may be replaced by less qualified staff, causing the quality of the service to decline.

These disadvantages need to be weighed up against the benefits of major cost savings and potential productivity benefits.

Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

The advantages and disadvantages of outsourcing in a global market

FIGURE 17.3 Advantages and disadvantages of global outsourcing of human resources



A different view to global outsourcing has emerged since the COVID-19 pandemic of 2020. In many cases the managers of some of Australia's largest companies in the telecommunications, finance, government and other service industries found that many of the businesses contracted to carry out various functions were unavailable with little notice. Call centres, IT support and other process outsourced activities were severely disrupted.

Traditional outsourcing countries such as India and the Philippines operated with minimal staff or shut down completely. Unlike companies in Australia, working remotely was not a viable option for staff due to inadequate technology, ill-equipped telecommunications infrastructure and a lack of suitable work-from-home options.

While some Australian-based businesses did have some contingencies in place if an overseas partner was unable to continue with existing services, the scale of the pandemic was unprecedented and an immediate response for many was to bring many services back in-house.

SNAPSHOT

Case study: Telstra's outsourcing in a post-COVID-19 global business environment

India and the Philippines have for some time been the favoured location of the global call centre industry.



The emphasis on higher levels of customer service and the widespread use of English have consolidated these two countries as a trusted place to outsource customer service for a range of businesses including Australia's telecommunications market leader Telstra.

Telstra has sought to shore up its market domination through its strategic management of its resources.

The 'T22 strategy' was created to assist in Telstra's attempt to lead the Australian market by simplifying its operations and products, improving customer experience and reducing its cost base.

One of the details contained within the 'T22 strategy' was the decision to outsource 1500 call-centre jobs to Bangalore, India. The impact of the global pandemic in India (and in its other call centre location in the Philippines) meant that Telstra's overseas call centres were immediately shut down. Telstra's management responded by employing 3500 local staff members to replace the overseas call centre customer service operators and has indicated that the loss of the overseas call centres had led to a review on how to better deal with customer complaints.

Management has determined that future demands will require a higher level of customer service if it is to maintain its market dominance.

Telstra management has decided that its offshore call centre partners will be scaled down and the temporary use of local operators in response to the global pandemic will be maintained.

KEY IDEAS

- New business structures are developing in response to global competition.
- Outsourcing business functions to reduce costs, obtain specialist support and improve productivity is increasing.
- Many firms outsource specialist human resource functions such as recruitment and payroll.
- There has been a rapid growth in independent contractors, such as labour hire companies.
- Businesses generally find that outsourcing is most effective internationally when the business functions being outsourced are suitable for teleworking.
- There are benefits and risks in contracting, from lower costs, to the problem of loss of direct customer contact, and consistent quality and performance in outsourced activities.
- Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

17.4 Activities

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17.4 Quick quiz on | **17.4 Exercise** | **17.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 5, 6, 7, 9	3, 10, 11, 12, 13, 14, 15, 16, 19, 21	8, 17, 20

17.4 Exercise

Revision

1. **What** is 'outsourcing'?
2. **Identify** the most appropriate term from the list to complete the following sentences.

quality	internally	costs	lower	offshore	superior

Outsourcing is often used to obtain a _____ service, better functional _____ and a _____ cost service than that would be provided _____. Outsourcing, particularly global subcontracting, may significantly reduce _____ for some businesses.

3. **Examine** figure 17.2 and list the four most common reasons for outsourcing.
4. **Identify** six human resource functions that are often outsourced.

Read the 'Australian Business Solutions Group' case study and answer questions 5 to 7.

5. **List** the human resource services that ABSG offers.
6. **What** is OnePeople HR?
7. **Outline** the advantages to a business of programs such as the Aboriginal and Torres Strait Islander mentoring program.
8. You are a human resource manager for a construction business that has 568 employees. The general manager has asked you to consider using contractors for a number of business functions including machine maintenance and accounts preparation. Prepare a report.
   a. Outline the costs and benefits of using contractors. Present your information in a 'T' table format as shown below. The 'T' table has been started for you.

Using contractors	
Costs	Benefits • Creates savings

   b. **Assess** the value of using contractors.
9. **Outline** the key features needed in agreements for successful outsourcing.
10. **Distinguish** between domestic and global subcontracting.
11. **Examine** figure 17.3. **Justify** which you consider to be the more persuasive: the potential advantages or potential disadvantages of global outsourcing of human resources.
12. **Why** is outsourcing important to the evolution of human resource management?

Read the 'Telstra's outsourcing in a post-COVID-19 global business environment' case study and answer questions 13 to 15.

13. **Why** are countries such as India and the Philippines seen as favourable locations for outsourcing by companies based in Australia?
14. **How** did the global pandemic impact companies such as Telstra?
15. **Discuss** the effect of the decision to outsource important activities such as call centres on Australia's economy.

Extension

16. Research the human resources processes and practices of one of the companies listed in the BizFACT at the start of subtopic 17.3. **Compare** and **contrast** these in a tabular form.
17. 'The role of human resources has been evolving for many years now. What was once the "personnel" department has been replaced by a sophisticated key business function with management keen to have a say in the strategic planning process.' **Human resources specialist at TA Industries**
    Analyse the ways in which the role of human resource management is changing.
18. 'I am sick and tired of ringing a call centre only to have to wait for half an hour, finally getting someone to talk to only to be transferred to another operator, getting cut off and having to start all over again.' Write a report on the advantages and disadvantages of outsourcing call centres.
19. **Propose** a range of business activities that would be suited for outsourcing to either domestic or global contractors.
20. **Predict** the future of both domestic and global outsourcing.
21. **Discuss** the ways in which human resource managers can ensure that high standards in quality and customer service are maintained as business structures evolve on a global scale.

17.4 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q3

A firm has been hiring its own staff but due to growth no longer has time to satisfactorily manage this process. What could the firm's human resource manager use to resolve this issue?

A. Acquisition
B. Outsourcing
C. Recruitment
D. Selection

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q15

What is a benefit to an Australian clothing company of outsourcing its manufacturing overseas?

A. It can control the production costs.
B. It can lower human resource compliance costs.
C. It can decide which particular employees manufacture its products.
D. It can consider the foreign manufacturer's workers as its own employees.

Question 3 (6 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q23

Heather owns a financial planning business with offices in four countries, including Australia. Heather outsources the cleaning of her Sydney office.

a. Explain ONE advantage of this strategy. **(2 marks)**
b. Explain TWO disadvantages of this strategy. **(4 marks)**

Question 4 (1 mark)

Source: Adapted from HSC 2008 Business Studies Exam, Section I, Q4

To reduce costs, a business employs external contractors to provide payroll services.

Which term describes this strategy?

A. Acquisition
B. Outsourcing
C. Recruitment
D. Performance management

Question 5 (6 marks)

Source: HSC 2008 Business Studies Exam, Section II, Q23b

Edpro designs software and employs its own software programming team. It plans to outsource programming in 2009.

Analyse the possible impact on management AND employees of outsourcing programming.

More exam questions are available in your learnON title.

17.5 Review

17.5.1 Summary

The strategic role of human resource management

- Human resource management (HRM) refers to the management of the total relationship between an employer and employee in order to achieve the strategic goals of the business.
- In recent years, governments have tried to assist businesses in becoming more competitive by creating a more flexible legal framework for human resource management.

Interdependence with other key business functions

- In large businesses, a specialist human resources team or manager is responsible for the business's human resource management.
- Most specialist human resource managers are responsible for:
  - human resource planning and job design
  - acquisition — recruitment, selection and placement
  - development — induction, training, career development and performance appraisal
  - maintenance of staff — wellbeing, legal responsibilities and communication
  - performance management and rewards
  - separation
  - managing diversity, including the implementation of gender equity and anti-discrimination legislation.
- Where the human resource manager is part of the senior executive, he or she collaborates in executive decisions about strategic issues, such as a change in product, service or organisation of work.
- Many firms outsource specialist human resource management functions.

Outsourcing

- New business structures are developing in response to global competition.
- Outsourcing business functions to reduce costs, obtain specialist support and improve productivity is increasing.
- Many firms outsource specialist human resource functions such as recruitment and payroll.
- There has been a rapid growth in independent contractors, such as labour hire companies.
- Businesses generally find that outsourcing is most effective internationally when the business functions being outsourced are suitable for teleworking.
- There are benefits and risks in contracting, from lower costs, to the problem of loss of direct customer contact, and consistent quality and performance in outsourced activities.
- Many in the field believe that if the function to be outsourced can be clearly identified, measured, managed and supported by a binding legal framework then it may be more suited to outsourcing.

17.5.2 Key terms

contractor an external provider of services to a business. It may be an individual or a business.
employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.
employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees
human resource management the management of the total relationship between an employer and employee
interdependence the mutual dependence that the key business functions have on one another
outsourcing contracting out business functions involving the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

Resources

Digital documents	Key terms glossary (doc-35670) Chapter crossword (doc-36222)
Interactivity	Chapter crossword (int-7173)
Exam question booklet	Chapter 17 Exam question booklet (eqb-0039)

17.5 Activities

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Exercise 1: Multiple choice questions

1. Management of HRM is very important as
   - **A.** over the next decade there are major pressures from an ageing workforce.
   - **B.** outsourcing is increasing.
   - **C.** labour is generally around 60 per cent of operational costs.
   - **D.** governments are increasing the compliance requirements for human resource management.

2. Strategic HRM focuses on which of the following?
   - **A.** Negotiation with unions, establishing and negotiating agreements, awareness of global labour market issues
   - **B.** Collaboration with executive on organisational changes, induction, training, career development and performance appraisal
   - **C.** Recruitment, selection and placement, HR auditing
   - **D.** Collaboration with executive on a change in product or other issues, global trend analysis and risk management

3. A training and development officer has been appointed in a business. In which function will their work be carried out?
   - **A.** Human resources
   - **B.** Operations
   - **C.** Marketing
   - **D.** Finance

4. What are the most commonly outsourced HR functions?
   - **A.** Change management and training
   - **B.** High performance coaching and succession planning
   - **C.** Compensation and performance management systems
   - **D.** Outplacement, mediation and payroll

5. Best practice strategies for reducing risks of outsourcing do not include
   - **A.** setting clear and legally binding terms.
   - **B.** management of the recruitment of appropriate staff.
   - **C.** confirming responsibility for superannuation, insurance and workers compensation.
   - **D.** setting clear timeframes and conditions for contacts.

6. Domestic subcontracting would be most useful for
   - **A.** a major bank wishing to obtain financial expertise.
   - **B.** a major brick company wishing to have a new brick manufactured.
   - **C.** a small baker seeking a loan.
   - **D.** a pet boarding agency seeking expert veterinary knowledge.

7. Specialist HR companies like Seek.com assist other companies with outsourced function such as
   - **A.** providing advice on the construction of company profiles for job seekers.
   - **B.** providing advice on financial options for customers.
   - **C.** providing design ideas for new products.
   - **D.** providing advice on outplacement services.

8. Functions which are more suited to outsourcing
   - **A.** are those which can be clearly identified, repeated, staffed and supported by a legally binding framework.
   - **B.** are those which can be clearly identified, measured, managed and supported by a legally binding framework.
   - **C.** need to be weighed up against the benefits of major cost savings.
   - **D.** involve more repetitive, easily measured and simple work.

9. Two potential disadvantages of outsourcing include which of the following?
   - **A.** Consultants may not understand your culture, training costs may fall
   - **B.** Legal compliance increases, hidden costs emerge
   - **C.** Security risk, increased business learning through reliance on experts
   - **D.** Culture may be transformed, capital may be lost

10. In Australia, the main reason for outsourcing is
    - **A.** increase speed to market.
    - **B.** improve quality.
    - **C.** focus on core.
    - **D.** conserve capital.

Exercise 2: Exam practice questions

Question 1 (2 marks)
Outline the strategic role of human resources.

Question 2 (3 marks)
Explain the role of interdependence between human resources and one other key business function.

Question 3 (6 marks)
a. **What** is outsourcing? **(2 marks)**
b. **Discuss** the decision to outsource human resources functions. **(4 marks)**

Question 4 (4 marks)
Distinguish between domestic and global contractors.

Question 5 (5 marks)
Analyse the role of human resource management in business.

Question 6 (4 marks)
Assess the role of outsourcing in a global market.

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18 Key influences on human resource management

18.1 Overview

LEARNING SEQUENCE

18.1 Overview
18.2 Stakeholders in the human resource management process
18.3 Legal influences: The employment contract
18.4 Legal influences: Work health and safety and anti-discrimination
18.5 Economic, social, technological and ethical influences
18.6 Review

18.1.1 Introduction

The key influences on human resource management include the range of stakeholders. These stakeholders are integral to the management of people in a business as they engage with it in a variety of ways.

The legal framework underpins the relationship between the employer and employee. This includes the role of the government in supporting institutions such as the Fair Work Commission in articulating requirements for employment contracts, and facilitating an effective process for negotiating enterprise agreements, or where applicable individual contracts. Moreover, economic, social and technological influences from the internal and/or external environment will affect management decisions. Increasingly ethics and corporate and social responsibility play a significant role in human resources and are reflected in how modern workplaces, especially those operating in a global context, examine how to better manage diverse, culturally competent workforces.

FIGURE 18.1 Key influences on human resource management include stakeholders such as employers, employees, employer associations, trade unions, government organisations and society.



Key influences on human resource management will involve a strategic approach where the various influences determine the longer term direction of a business, how the human resources function relates to the other functional areas and the need to evaluate the effects of a decision to outsource some or all of its functions.

on Resources

Digital document	Key terms glossary (doc-35672)
Exam question booklet	Chapter 18 Exam question booklet (eqb-0040)

18.2 Stakeholders in the human resource management process

SYLLABUS LINK In this subtopic you will learn about the various stakeholders that influence human resource management including employers, employees, employer associations, unions, government organisations and society.

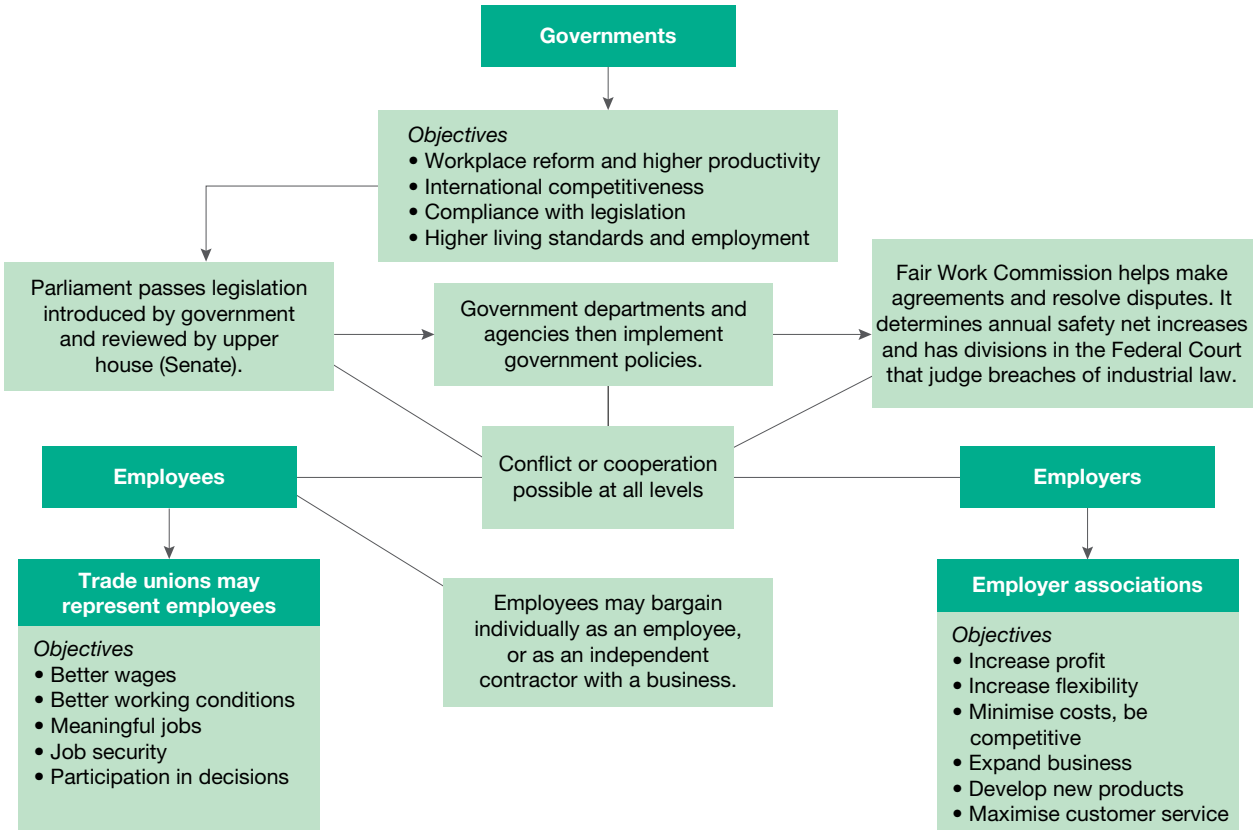
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Stakeholders are any individual or group that has a common interest in or is affected by the actions of an organisation.

stakeholder any individual or group that has a common interest in or is affected by the actions of an organisation

Stakeholders have a common interest in the survival and success of the business. However, not all their interests are shared — conflict can arise due to differences and competing interests (see figure 18.2).

FIGURE 18.2 Stakeholders in the human resource process and their interests



18.2.1 Employers

Employers, for legal purposes, are those who exercise control over employees, have responsibility for the payment of wages and/or salaries and have the power to dismiss employees. They handle human resource management issues on a daily basis. Some spend over half their work day on matters related to this area, including involvement in developing programs that focus on improving business performance. Employers' responsibilities are increasing, as recent legislation today encourages them to negotiate agreements and resolve disputes at the individual workplace. However, employers have been widely criticised in many management surveys for failing to tackle issues in managing employees effectively. A recent survey of more than 7600 people found 'people management' to be the most serious failing of business leaders in Australia, and was cited 2.5 times more frequently than any other management failing. Improving management training in Australia is therefore important in improving human resource management.

18.2.2 Employees

Employees are workers under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised. Employees today are, on average, more highly educated than in the past. They become bored very quickly and demand more challenging, interesting work, involvement in decision-making processes and autonomy at their workplace. Many feel driven to build their career through a succession of jobs in a range of different organisations.

Following periods of extensive downsizing in recent years, employees no longer trust one business to look after their needs. As a result, the practice of 'churning' — moving frequently from one job to another in different organisations — is increasing, particularly in service industries. Businesses hoping to retain and motivate skilled staff need to put extra effort into developing their career and training plans, rewards and opportunities for greater employee involvement. Around one-third of employees are also keen to get more work–life balance, including to spend more time with their families.

The structure of work has changed over the last decade and affects employees' access to work. For example, many older workers, women and younger inexperienced people struggle to obtain full-time jobs, particularly in the knowledge-based service sector. These people have become our 'flexible', casual workforce. Australia has experienced close to full employment for a long time, despite a global economic downturn.

The number of Australians aged 65 years and over is projected to double by 2055 and their participation rates will increase from 5 per cent to 17 per cent. Women will also have a more substantial role to play in the workforce and it is expected that their participation rates will grow by 4 per cent in the next 20 years.

Many trade unions have responded to worker fears and have made some employment issues — such as job security and limitations on the use of casuals — a priority in negotiating agreements. A significant number of employees do, nevertheless, enjoy the flexibility of job sharing, and part-time and casual work to manage family commitments.

employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees

employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.

BizFACT

In the May 2009 Federal Budget, the Australian Labor government announced the Age Pension age would increase to 67 years from 2023, remaining at 65 for anyone born before July 1952. In the May 2014 Federal Budget, the Australian Coalition government announced that from 1 July 2025, the Age Pension age would continue to rise by six months every two years to gradually reach a qualifying age of 70 years by 1 July 2035.

18.2.3 Employer associations

Employer associations were originally created by employers as a counter-party to unions, to represent employers in the making of awards through the conciliation and arbitration system established in 1904. They assisted employers in formulating policies and processed **logs of claims** served on their members by unions. Their main role today is to act on behalf of employers (especially small businesses) in collective bargaining sessions and before industrial tribunals, courts, commissions and committees. They:

- provide advice (especially to small businesses) on such matters as awards, unfair dismissals and discrimination issues
- make submissions to safety net wage cases
- negotiate agreements
- lobby governments and other organisations with the views and interests of employers, industries and trade.

Unlike unions, employer associations represent employers on a broader range of issues beyond human resource and industrial relations matters.

Employer associations may function as professional bodies, such as the Australian Medical Association, or as marketing bodies, for example, dairy cooperatives and Meat and Livestock Australia. Others are associations with an industrial relations function within their services, such as the Australian Chamber of Commerce and Industry (ACCI), and the Australian Industry Group (Ai Group) representing the Australian Chamber of Manufactures and the Metal Trades Industry Association.

employer association an organisation that represents and assists employer groups. They are usually respondents to the awards covering the employees of their members, and covering employers in the same or related industry.

log of claims a list of demands made by workers (often through their union) against their employers. These demands cover specific wages and conditions. Employers may also serve a counter-log of claims on the union.

SNAPSHOT

Case study: The Australian Industry Group (Ai Group) — representing business

The Australian Industry Group (Ai Group) is Australia's peak industry association and represents more than 60 000 businesses. It encompasses a number of different industry sectors including manufacturing, engineering, transport, IT, telecommunications and construction.



The focus of the Ai Group is to ensure that business views are represented to all levels of government. This includes matters relating to work health and safety, workplace relations, human resource management and workers' compensation.

The Ai Group identifies the following services as being integral to what it offers to members:

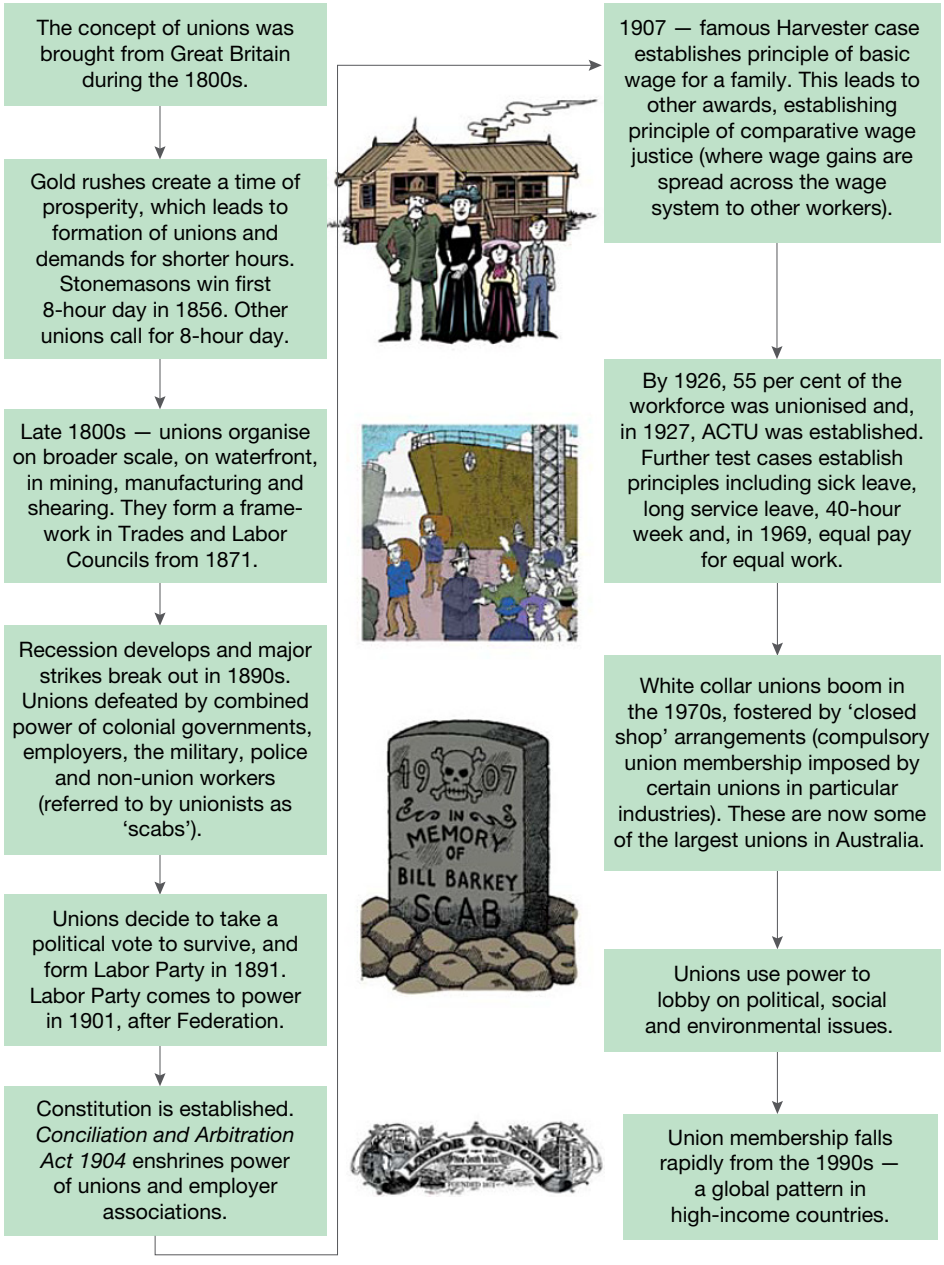
- how to deal with employees making a bullying complaint
- the introduction of new laws relating to payments to unions and their representatives
- access to online webinars regarding recent industrial relations matters before the Fair Work Commission
- state-specific industrial information
- current economic data relevant to Australian businesses
- case studies of real industrial issues.

18.2.4 Trade unions

Trade unions are organisations formed by employees in an industry, trade or occupation to represent them in efforts to improve wages and the working conditions of their members. The key factors and stages in their development in Australia are summarised in figure 18.3.

trade union an organisation formed by employees in an industry, trade or occupation to represent them in efforts to improve wages and working conditions of their members

FIGURE 18.3 The development of trade unions in Australia since 1800



The system for resolving industrial disputes, established in 1904 in Australia, gave unions a powerful role in human resources. It provided unions with an official bargaining position in the making of industrial agreements. Through test cases, unions won major improvements in terms and conditions of employment. These established key principles that flowed on to other workers.

BizFACT

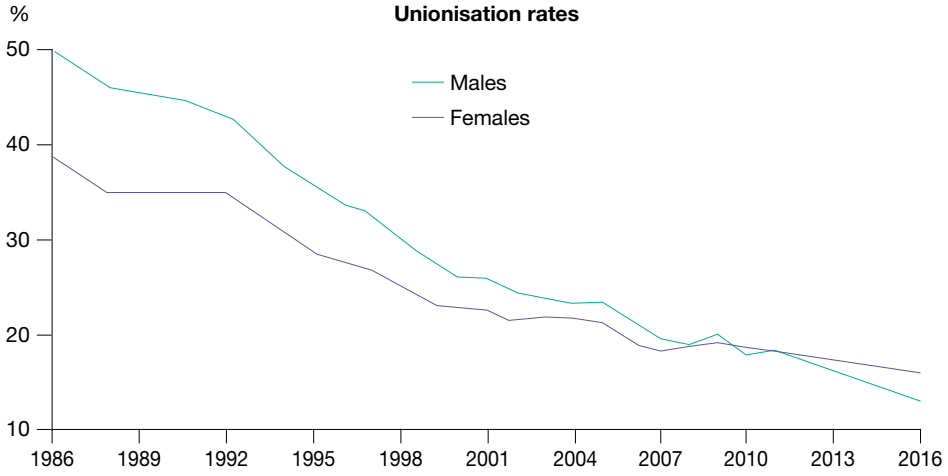
The peak trade union body is the Australian Council of Trade Unions (ACTU). Some of the larger unions include the following:

- Australian Services Union (ASU)
- Australian Workers' Union (AWU)
- Australian Manufacturing Workers' Union (AMWU)
- Construction, Forestry, Maritime, Mining And Energy Union (CFMMEU)
- Finance Sector Union (FSU)
- Maritime Union of Australia (MUA)
- Transport Workers' Union of Australia (TWU)
- Textile, Clothing and Footwear Union of Australia (TCFUA)

Union membership peaked at 51 per cent in 1976, falling to 46 per cent of all employees in 1986. It has fallen dramatically since, as seen in figure 18.4, reaching the current level of 14 per cent of the workforce, where it has remained steady for the last few years. In addition:

- 16 per cent of full-time and 12 per cent of part-time employees belong to a trade union
- 38 per cent of government workers compared with 9 per cent of private industry workers are trade union members
- the highest levels of trade union membership are in education and training (37 per cent) and the industries with the lowest levels of union membership are real estate services and professional, scientific and technical services with 3 per cent
- 68 per cent of workers have never belonged to a trade union.

FIGURE 18.4 Trade union membership in Australia has fallen dramatically.

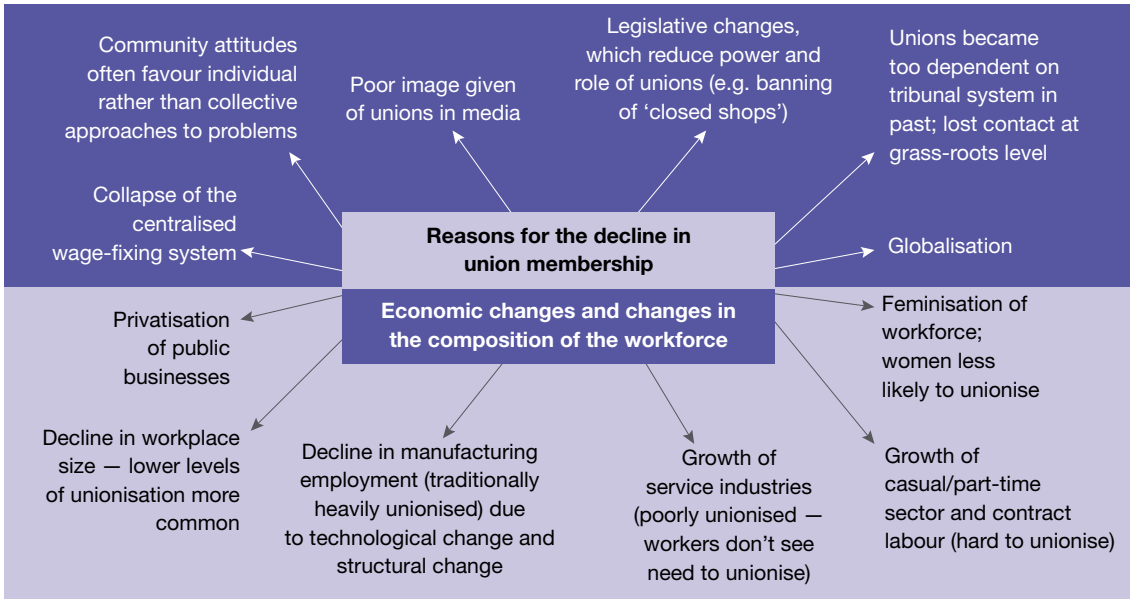


Having contributed so much to winning employee rights over the last decades, unions are now under pressure globally as membership declines to historically low levels. In response, unions are expanding their range of services and becoming more active in recruiting to regain membership numbers. As well as providing

representation in disputes, the range of services offered by a union to members might now include free or discounted legal services, superannuation schemes, cheap home loans, training programs through TAFE, insurance, cheap holiday units to rent, income protection against illness or accident, work health and safety (WHS) advice, and many more.

The major reasons for the decline in union membership are shown in figure 18.5.

FIGURE 18.5 Reasons for the decline in union membership



SNAPSHOT

Case study: Maritime Union of Australia (MUA)

The Maritime Union of Australia (MUA) is a division of the CFMMEU trade union and has been in existence since 1872 when (as the Seamen's Union of Australia) it was the first maritime union anywhere in the world.

The MUA evolved when the Seamen's Union of Australia and the Waterside Workers' Federation amalgamated in 1993. It draws its 16 000 members from industries such as diving, ferries, offshore oil and gas, port services, shipping and stevedoring.

The MUA is affiliated with the Australian Council of Trade Unions (ACTU), operates nationally and has a rich history as a trade union in Australia. In one of the most significant examples of industrial conflict in recent history, the MUA engaged in an 80-day dispute with employers Patrick Corporation on Australia's waterfronts when the jobs of some 1400 members were threatened and would be replaced by non-union contract labour.

The MUA encourages active participation in its charter especially among its younger members (21%) . Its more recent industrial campaigns include:

- **Stand up. Speak out. Come home**.
  This was a recognition that many of its members worked in dangerous industries in Australia and that every six minutes a worker suffers a serious injury or dies in the workplace.
- **Securing safer boats and ships**
  Preserving and improving standards for vessel safety that are related to issues around the lowering of standards in relation to crewing, qualifications and training.

- **Build offshore wind and fund a just transition**
  The development of an offshore wind industry to be used in generating electricity for commercial and household use. This renewable industry offers potential employment opportunities for its members and they are seeking government funding to support this program.
- **Save Australian shipping — take back our coast**
  A 10-point plan for reviving the domestic shipping industry as a viable and energy efficient mode of transport.

18.2.5 Governments and government organisations

Governments are important stakeholders in the human resource management process. Over time, they have significantly affected the industrial relations system as a result of their key roles, as follows.

- *Legislator*. Our elected representatives pass laws in parliaments (state and federal), which provide the legal framework for industrial relations. Legislation has also led to the growth of the judicial system, and the institutions and processes used by employers and employees to conduct bargaining and resolve disputes.
- *Employer*. Federal and state governments employ almost one-third of Australian workers, as teachers, nurses, clerks, police officers, postal workers, transport workers and in other roles. They are often regarded as pacesetters in terms of responsible industrial relations policies, having introduced practices such as maternity leave, flexitime and affirmative action for women that were eventually adopted in the private sector.
- *Responsible economic manager*. Governments operating at the macro level are keen to ensure non-inflationary, stable economic growth and a high standard of living for all Australians. At times there may be conflict between governments' economic goals, which impact on industrial relations. For example, a decision to cut spending through reductions in the size of the public service in order to reduce a budget deficit may conflict with its desire to maintain employment.
- *Administrator of government policies on industrial relations*. Through the departments and agencies established, governments are able to implement the legislation they enact. This is achieved through publishing information and guidelines providing advice to the government and the public and investigating breaches of legislation.
- *Representative of Australia in the international arena, in foreign affairs, trade and international labour matters*. Australia is a foundation member of the International Labour Organization and has been represented on its governing body. As a result of its membership of such organisations, the government generally implements legislation based on the treaties and conventions it signs with international organisations. Social justice legislation passed in relation to discrimination, and human rights originated in these treaties and conventions.

BizFACT

The Department of Education, Skills and Employment has been established to support Australia's economic growth by providing policies and programs that assist people looking for employment, supporting small businesses (especially those owned by families) and maximising opportunities for all through quality skills and training.

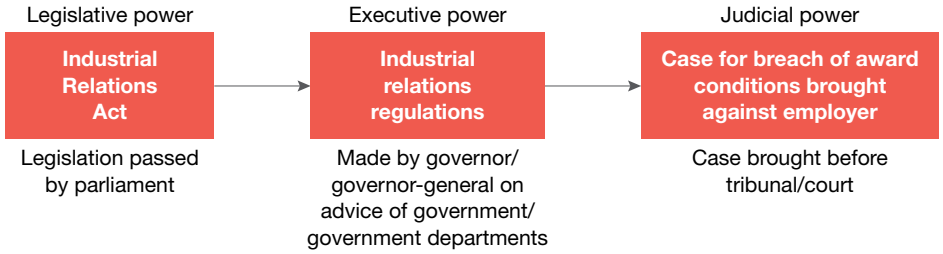
FIGURE 18.6 Governments (both state and federal) perform many roles that have an impact on the human resources process; for example, the roles of legislator, employer, economic manager, policy administrator and representative of Australia on the international stage.



Governments have attempted to increase their power to regulate the industrial relations system through use of the External Affairs and Corporations powers (among others) given under the Constitution of Australia. Recent government policy has focused on reducing the powers of industrial tribunals and encouraging decentralised bargaining in the workplace (enterprise).

Since and the introduction of the Fair Work Australia Act, all the states, except Western Australia, referred their industrial relations powers to the Commonwealth. The aim of the federal government was to create a national system, which would simplify industrial relations so that employers were not forced to negotiate under multiple jurisdictions and to stop employees and unions from 'shopping around for the best deal'. These arrangements were intended to reduce business costs through creating greater certainty and efficiency in dealing with industrial matters.

FIGURE 18.7 The functions of government (state or federal) in workplace relations



Statutes

Statutes are laws made by federal and state parliaments; for example, laws relating to employment conditions (see table 18.1). Until recently, Australia has operated a dual system of industrial relations since federation. This has arisen as the Constitution awards the Commonwealth Government limited powers to make laws about industrial issues and allows the states to make laws about matters not covered under the Constitution, known as residual powers.

statutes laws made by federal and state parliaments; for example, laws relating to employment conditions

These statutes provide the framework for awards and agreements and the resolution of disputes, and require employers to:

- meet WHS requirements
- maintain workers' compensation insurance
- provide all employees with superannuation, annual leave and long-service leave
- ensure employment practices in the workplace are free from discrimination on the basis of age, sex, physical or mental disability, marital status, family responsibility, pregnancy, union membership, political opinion, race or social origin
- give each new employee, covered by the national industrial relations system, a Fair Work Information Statement. This statement provides basic information about employee rights.

TABLE 18.1 Federal legislation

Law or test case	Date	Features
Conciliation and Arbitration Act	1904	Gave the Conciliation and Arbitration Commission power to prevent and settle industrial disputes extending beyond the limits of the state.
Harvester case	1907	Established the basic wage for full-time male worker with wife and two children.
Equal Pay case	1969	Principle of equal pay for equal work established for women.
Trade Practices Act	1974	Secondary boycotts (provisions) made illegal. Jurisdiction for this later moved to Australian Industrial Relations Commission, as ILO (International Labour Organization) report suggested it interfered with the right to strike.
Racial Discrimination Act	1975	Discrimination in employment on the basis of race, colour, national or ethnic origin prohibited.
Maternity Leave case	1979	Test case on maternity leave won by ACTU.
Sex Discrimination Act	1984	Prohibited sexual harassment and discrimination on basis of sex, marital status and pregnancy.
Affirmative Action (Equal Opportunity for Women) Act	1986	Required all private sector employers and all higher education institutions to implement affirmative action programs for the employment of women and to submit annual reports on their progress.
Industrial Relations Act	1988	Award restructuring introduced under the structural efficiency principle (SEP).
Parental Leave test case	1990	Federally covered male employees given opportunity to take leave to mind newborn children, etc.
Industrial Relations Reform Act	1993	Improved safety net provisions for employees, through the award system and minimum entitlements. Improved arrangements for direct bargaining through both certified enterprise agreements (between employers and unions) and enterprise flexibility agreements (non-union individual agreements). Protection against unfair dismissal.
Workplace Relations Act	1996	Revised framework for enterprise bargaining, allowing for collective and individual agreements, with or without union involvement. Tighter restrictions on industrial action. Limited arbitration role for AIRC.
Fair Work Act	2009	National framework for industrial relations implemented. Covers most private employees. All states refer powers with exception of WA. Ten National Employment Standards set. Collective bargaining emphasised.

BizFACT

Section 51 (xxxv), the most important section of the Constitution for industrial relations, gave the federal government the power to: '. . . make laws for the peace, order and good government of the Commonwealth with respect to: . . . (xxxv) Conciliation and arbitration for the prevention and settlement of industrial disputes extending beyond the limits of any one State'. The effect of this Section was that:

- a dispute (actual or pending) must exist before the tribunal could intervene
- the dispute must be an 'industrial matter'
- the dispute must extend beyond one state.

Australia has a dual industrial relations framework whereby all private sector employees are covered by a federal industrial relations system and public sector workers in several states, including New South Wales, remain in state-based system.

This system, implemented under the *Fair Work Act 2009*, is administered by the federal government. It covers all employees of **constitutional corporations** in all states and most private employees formerly covered under state awards and enterprise agreements. The system gives employers and employees the same workplace rights and obligations, regardless of the state they work in.

Key elements of the framework include:

- a national framework for industrial relations covering most private employees of all states except Western Australia
- ten National Employment Standards (NES) developed to provide basic protections to employees
- collective bargaining and good faith bargaining required by all parties
- modern awards for specific industries and occupations
- enterprise bargaining continued
- annual National Wage Case sets minimum wage
- protection from unfair dismissal
- Fair Work Commission administers the *Fair Work Act 2009* and the Fair Work Ombudsman is responsible for promoting unified, supportive and productive workplace relations that comply with the Fair Work laws.

The 122 **modern awards** cover most employees in a wide range of industries, and replace thousands of previous state and federal awards. Together with the NES and the national minimum wage order, they make up a safety net for employees covered by the national workplace relations system. They do not replace enterprise awards, which are made with a specific enterprise.

constitutional corporation one that falls under section 51(xx) of the Constitution of Australia — identified as foreign corporations and trading or financial corporations formed within the limits of the Commonwealth

modern award an industry or occupation-based award that covers all private sector employers and employees who perform work that falls within their scope. They replace all existing national system awards (except those applying to a single enterprise). They do not cover employees earning higher incomes.

award the legally enforceable minimum terms and conditions that apply to a business or industry

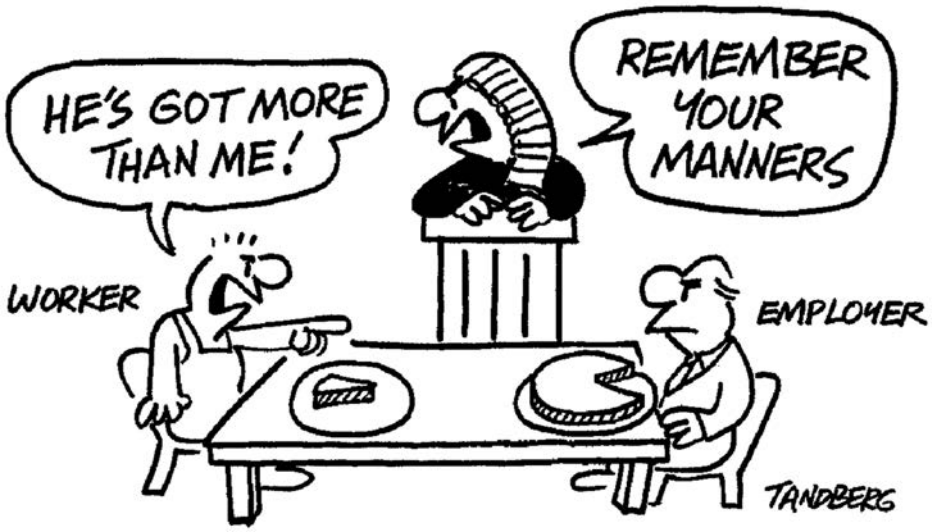
award simplification the process of reducing the number of matters in each award and eliminating inefficient work practices

Industrial tribunals and courts

Industrial tribunals exist at the federal and state levels to enforce laws established by governments. The Fair Work Commission today plays a role in ensuring that the bargaining process and any associated industrial action occur according to law.

The Fair Work Commission follows in the footsteps of the longstanding Australian Industrial Relations Commission (AIRC), formerly the Australian Conciliation and Arbitration Commission. Its primary functions include settling disputes through conciliation, supervising the making of agreements or **awards** and **award simplification**, hearing appeals and handling unfair dismissal cases. The Fair Work Commission assists in resolving disputes involving employers, employees, unions and employer associations who are covered by the national workplace relations system. Through these functions and specific cases, the Fair Work Commission determines questions about future rights of employees and employers.

FIGURE 18.8 A cartoonist's interpretation of the role of tribunals



BizFACT

A full panel (bench) of at least three Fair Work members, including a Deputy President, is needed to:

- hear matters of significant national interest such as test cases on matters, concerning family leave, superannuation and public holidays, and establish principles for making and varying awards
- certify multiple business agreements
- hear appeals against orders, or cancel and suspend awards and orders arbitrate after a bargaining period is terminated.

Much of the Fair Work Commission's work is conducted by individual members or groups of members who are responsible for specific industries or disputes, and are skilled in mediation, conciliation and arbitration. The Fair Work Commission members come from a diverse range of employment backgrounds and must have knowledge or experience in one or more of the fields of workplace relations, economics, social policy, business, industry or commerce.

A panel of seven senior members, the Fair Work Commission's Expert Panel, is responsible for hearing annual wage cases and setting minimum wages for employees in the national workplace relations system.

Breaches of the Fair Work Commission's orders can lead to fines of up to $12 600 for individual workers or $63 000 for a corporate entity.

Federal Court

The Federal Court of Australia is a judicial court. Under the Australian Constitution, only courts have the **judicial power** to determine disputes about existing rights and to make decisions about these matters. The Federal Court of Australia has a division that enforces industrial relations legislation by administering court actions that arise under Australian industrial laws. It handles cases relating to industrial action and breaches of industrial laws, interprets industrial legislation, and is able to impose penalties for the breach of an award or order, and discrimination or victimisation under industrial and human rights legislation. It also has the power to approve the disamalgamation (splitting up) of unions, declare unauthorised action taken during a dispute and hear cases under the *Corporations Act 2001*.

judicial power refers to the power of courts to interpret and apply laws

Other government agencies

A number of other federal and state government agencies are also stakeholders in the human resources process. For example, the roles of the Australian Human Rights Commission (AHRC) the Workplace Gender Equality Agency (WGEA) and state organisations such as Anti-Discrimination New South Wales are to implement particular areas of government legislation.

In the area of work health and safety, the federal *National Occupational Health and Safety Commission Act 1985* established the National Occupational Health and Safety Commission, now Safe Work Australia. Safe Work Australia began operating as an independent statutory agency in 2008. Its primary responsibility is to improve work health and safety and workers' compensation arrangements across Australia.

Recognising the need to standardise and harmonise work health and safety systems around Australia, the federal government developed, in collaboration with each state government through the Australian Chamber of Commerce and Industry (ACCI) and the Australian Council of Trade Unions (ACTU), a new framework for a national occupational and work health and safety system.

18.2.6 Society

In 1948, the General Assembly of the United Nations, consisting then of 56 countries, passed the Universal Declaration of Human Rights, recognising the importance of work to people's lives, and the need for fair and just conditions and rights for those at work (see figure 18.9).

One of the most significant issues for any voter is their job. If there are threats to employment or conditions at work, whether as a result of planned legislation, economic conditions, pressure arising from global competition or adverse social impacts, voters make their views clearly known. The relationship between employers and employees has often been a battleground, as reflected in frequent disputes and changes in legislation in Australia over the last decades.

FIGURE 18.9 Key points from Articles 23 and 24 from the Universal Declaration of Human Rights

There are two key articles in the UN Declaration of Human Rights that deal with work — **Article 23** and **Article 24**.

Key points include:

- The right to work
- The right to freely choose your employment
- Fair conditions of work
- Equal pay for equal work.
- Just and favourable (i.e. fair) remuneration
- The right to form and join a trade union
- The right to leisure and rest i.e. limits on working hours and some holidays.

As global competition increases the pressure on businesses to become leaner, the need for more efficient operations, global business consolidation and rationalisation of production has increased. Multinational corporations increasingly use contractors to supply or manufacture key components or services, creating opportunities globally for suppliers with the most cost effective operations. Often the process of relocating production offshore, or shifting production regularly to lower cost locations, leads to dislocation and structural unemployment in the communities left behind. For other communities, there is constant pressure to 'do more with less', to work longer hours and to accept hard working conditions to retain jobs.

Community demands for safety and wellbeing at work have increased over recent decades, as has the pressure to eliminate discrimination against female, indigenous and disabled members of the working community.

For businesses, it means an ongoing battle between the need for the business to find ways to reduce its biggest cost — labour — as pressure increases from global competition, and the needs of employees, particularly those with dependent families.

KEY IDEAS

- The major stakeholders in the human resources process are employers, employees, employer associations, trade unions, government and government agencies, and industrial tribunals and courts.
- Each stakeholder has perspectives that may conflict or be shared with those of other stakeholders, leading to conflict or cooperation.
- Stakeholders are increasingly operating at a variety of scales and developing global networks in response to the globalisation of business.
- Membership of trade unions has declined dramatically over the last decades at a global level in response to many factors, including the shift to less hazardous work in the increasingly dominant service sector.
- To simplify industrial relations and improve efficiency, a national system of industrial relations has been created.
- Government statutes provide the framework for employment conditions.
- Since January 2010, Australia has shifted to a dual industrial relations framework with most workers covered by a federal award and some workers, mostly public servants, teachers and essential service employees such as police and nurses continuing with state-based awards.
- The system is implemented under the *Fair Work Act 2009*.
- Industrial tribunals and courts enforce the employment laws.
- The Fair Work Commission is the national industrial tribunal that replaced the Australian Industrial Relations Commission. Its powers have been expanded to allow it to hear and settle disputes, supervise agreement making and award simplification.
- Other government agencies are also stakeholders in the human resources process including the Australian Human Rights Commission (AHRC).
- Society has a number of expectations regarding employment conditions.

18.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

18.2 Quick quiz on | **18.2 Exercise** | **18.2 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 6, 8, 9, 11, 14	7, 10, 12, 13, 15, 16, 18	5, 17

18.2 Exercise

Revision

1. **Identify** the major stakeholders in the human resource management process.
2. **What** are the major objectives of employers and trade unions in the human resource management process?
3. In small groups, use the brainstorm technique to **identify** the advantages and disadvantages of employers being given greater power to make agreements for a specific individual, workplace or enterprise.
4. **Summarise** the major factors changing the nature of work today.
5. With employees being more educated today, **evaluate** the need for unions.
6. **Summarise** the aim of the federal government in introducing the *Fair Work Act 2009*.
7. 'Since January 2010, Australia has shifted to a dual federal and state industrial relations system.' **Explain**.
8. **State** the main elements of the *Fair Work Act 2009*.
9. **Describe** the role of the Fair Work Commission.
10. **Explain** the impact of increased global competition on (a) employees and (b) employers.

Read 'The Australian Industry Group (Ai Group) — representing business' case study and answer questions 11 to 13.

11. **Describe** the role of the Ai Group.
12. **Examine** the current focus areas of the Ai Group.
13. **Justify** the importance of employer associations for society.

Read the 'Maritime Union of Australia (MUA)' case study and answer questions 14 to 16.

14. **Outline** the role of the MUA.
15. **How** does the MUA represent the views of its members?
16. **Investigate** the 1998 Australian waterfront dispute involving the MUA. Outline the role of the stakeholders in the dispute and how the matter was eventually resolved.

Extension

17. **Evaluate** the potential success of global links developed by unions.
18. After researching online, **explain** the issue of shifting to a national system of work health and safety.

18.2 Exam questions

Question 1 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q11

Whose interests is an organisation most likely to be representing when it meets with government to discuss business flexibility, expansion and competitiveness?

A. Employees
B. Employers
C. Society
D. Unions

Question 2 (4 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q22b

How does the government influence employment contracts?

Question 3 (4 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q23a

How do employer associations influence human resource management? In your answer, identify a specific employer association.

Question 4 (1 mark)

Source: Adapted from HSC 2002 Business Studies Exam, Section II, Q22a

> Ace Tyre Fitters Pty Ltd has a majority of employees who are union members. The management team is not satisfied with the work performance of a number of employees and would like to take action that may ultimately lead to the dismissal of some workers.

Identify TWO stakeholders of human resource management.

Question 5 (1 mark)

Which of the following are the main interests of employees in the human resources process?

A. Wages and costs
B. Profits and working conditions
C. Job security and profits
D. Wages and job security

More exam questions are available in your learnON title.

18.3 Legal influences: The employment contract

SYLLABUS LINK In this subtopic you will learn about the employment contract, including common law (rights and obligations of employers and employees), minimum employment standards, minimum wage rates, awards, enterprise agreements andother employment contracts.

***Source**: Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

The employment contract creates obligations for both employer and employee, and all businesses operate within a legal framework of common law and statute law — that is, law passed by federal and state parliaments in Acts.

Legislation covers the nature of employment contracts and agreements; dispute-settling methods (as a result of our international agreements); protection of human rights in employment; and employer responsibilities for tax payments on behalf of employees. Employee welfare is provided for through work health and safety legislation and specific legislation such as the Superannuation Guarantee, under which all employers are obliged (either under awards or the legislation) to pay superannuation contributions for employees, whether or not they are on awards.

Changing community and worker expectations on **social justice** (equal employment opportunity, anti-discrimination), safety and environmental issues are increasingly reflected in legislation and work practices.

Following the election of the Rudd Labor government in 2007, a new legislative framework for industrial relations was enacted through the *Fair Work Act 2009*.

Unregistered individual common law contracts of employment, casual work and independent contracting remain common options for individual employment arrangements, with many employees indicating they are offered employment under these conditions on a 'take it or leave it' arrangement. These arrangements shift the responsibility of organising employment conditions, such as sick and carers leave, onto the employee. This has led to community concerns about the 'financialisation' and 'privatisation of risk' occurring, as responsibility for support is shifted from governments and employers to employees. 'Flexibility' works for employers, but less so for employees.

We have, nevertheless, shifted from a strongly **centralised industrial relations system** in the 1980s to a **decentralised** and more fragmented system today, based increasingly on bargaining at the workplace (enterprise) level.

Successive Australian federal governments since the 1980s have supported a decentralised view of industrial relations. The Fair Work legislation referred to above was aimed at ensuring that the government's role in determining the details of employment contracts would be limited to creating the legal framework that facilitated the negotiation of enterprise agreements, the National Employment Standards, minimum wage hearings and awards.

social justice in the workplace involves businesses being responsible or behaving in a fair and ethical manner towards their employees, customers and the broader community

centralised industrial relations system a collectivist approach in which disputes are referred to industrial tribunals, such as the Fair Work Commission, for conciliation and arbitration

decentralised industrial relations system a system in which employers and employees negotiate wages and working conditions in the individual workplace, through collective or individual bargaining and without the involvement of tribunals

The influence of government on the process of determining employment contracts

The government's role in the process of determining employment contracts has diminished since the introduction of the Rudd government's Fair Work legislation in 2007 and the removal of the Howard government's Australian Workplace Agreements.

Its main role in the employment of Australia's workers is undertaken by the Department of Education, Skills and Employment. This department has a number of strategic priorities that relate to people's working lives and seeks to:

- ensure quality, affordable and accessible early education and care for families
- improve schooling outcomes for children
- prepare our future workforce through globally competitive tertiary education, training and research sectors
- help people find and keep a job, create their own job, change jobs, reskill and enjoy fulfilling careers
- develop a strong evidence base for effective policy that reflects and understands the varied needs of the Australian population, business and industry.

At the state level the task falls to NSW Industrial Relations (NSW IR) whose responsibility it is to monitor wages, employment rights, obligations and employment conditions for its public servants and other workers such as teachers, police officers, nurses and essential service workers. It actively participates as a partner in the Commonwealth's national workplace relations framework.

BizFACT

The federal government's Department of Education, Skills and Employment has been assisting employers to cope with the fallout from COVID-19.

This government department has provided a range of services to assist employers with retaining staff, recruiting new staff and where necessary providing information to help displaced workers in transitioning to new employment.

The federal government's strategies have included providing wage subsidies, advice and support for hiring staff, directing staff when workers need to be retrenched and changed work limits for student visa holders.

The current workplace relations system maintains that employment contracts between employees and employers cannot provide for less than the legal minimum set out in the National Employment Standards (NES), awards or enterprise agreements. All employees are covered by the NES whether they have signed a contract or not — the contract cannot leave them worse off than their minimum legal entitlements.

As indicated previously, successive Australian federal governments (and to some extent most state governments) have sought to decentralise the industrial relations system. The most recent change, in the form of the *Fair Work Act 2009* ensured that the government's role in determining the details of employment contracts would be indirect and limited to ensuring that it maintains the integrity of organisations such as the federal Fair Work Commission (and state-based NSW Industrial Relations). This process seeks to guarantee that employees and employers, whether through a written or verbal contract, can be assured there are procedures in place to rectify concerns that their arrangements do not accord with the existing framework.

18.3.1 The employment contract

The most basic relationship in employment and the workplace is between employer and employee. An **employment contract** is a legally binding, formal agreement between employer and employee. Every employee has a contract with an employer. A written contract gives more protection to both parties than a verbal contract, as disputes often occur over contracts if working arrangements are not clear and it is one person's word against another. Usually employment contracts will be of two forms: contracts of indefinite duration and contracts of a fixed term.

employment contract a legally binding, formal agreement between employer and employee

Contracts of an indefinite duration are the most common type of employment contract and allow for the employee to remain employed by the business until either the employee or the employer gives notice that they wish to terminate the employment. The relevant laws or the contract itself determines the period of notice.

Contracts of a fixed term are ones that expressly define a date or upon completion of a specific task; for example, the employee is engaged for a period of 12 months and the contract does not exist beyond that period, or the employee's period of work will cease to exist at the completion of a project and the relationship comes to an end.

A written contract encourages the parties to clarify the key duties and responsibilities of a job (see figure 18.10).

FIGURE 18.10 An example of an employment contract

Dear Blake

This letter confirms your appointment to the Overboard Surf Store as its new Manager. Your employment commences on 25 July 2020 under the following conditions:

1. Your conditions of employment as full-time Manager are established in the Overboard Enterprise Agreement.
2. You will carry out all duties as a manager (as attached) within the store, together with any other duties as may reasonably be directed and requested by the employer.
3. Your wages will be subject to review by the company on the basis of individual performance assessment undertaken on a six monthly basis. Your annual salary will commence at $80 000 per annum.
4. During the first month of probationary employment, your employment may be terminated by either party giving immediate notice.
5. You will be given half a day's paid absence per week for six weeks to complete our management course.

Please complete the acceptance of this offer on the attached form.

Our store's policies and Enterprise Agreement are attached for your information. Please note the termination provisions.

We look forward to a rewarding relationship in the future and welcome you to our organisation.

Yours faithfully,

I Tuncay

Irem Tuncay

General Manager

Overboard Surf Company

BizFACT

Independent contractors are typically self-employed and have a contract for services (between a principal and a contractor) as opposed to the contract of service that employers have with employees on individual contracts of employment. Independent contractors do not have the same rights as employees, have control over their work, are responsible for their own tax payments and may work for a number of businesses. By using independent contractors, firms bypass many of the requirements of a contract of employment, such as sick leave entitlements and maternity leave provisions.

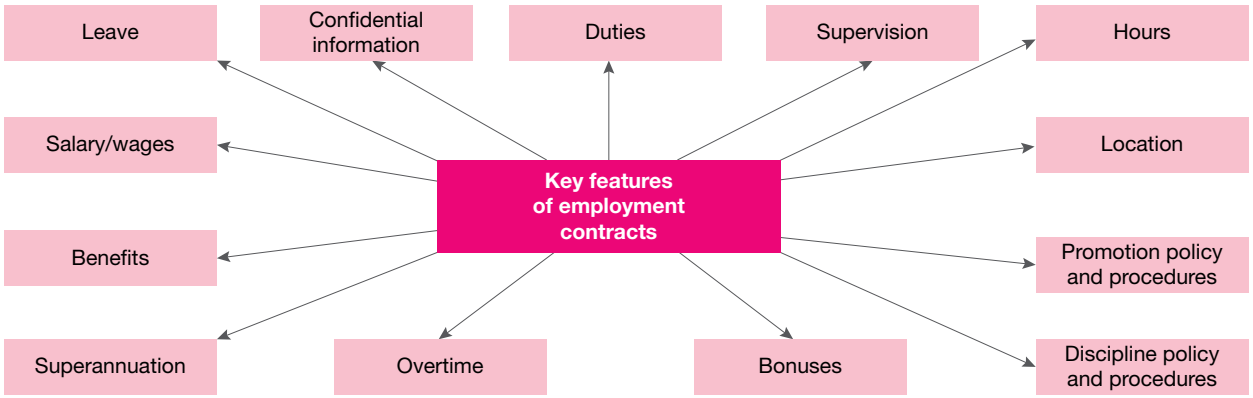
In the event of a dispute between a business and a contractor, a 'control test' is used by the courts in cases where the extent of the employer/employee relationship is unclear. If an independent contractor is working for a company and the company clearly had the right of continuous, dominant and detailed control over the contractor, the company could be seen as acting as an employer. Further evidence of the employer–employee relationship can be found in regular payments of salary or wages, regular and specific hours of work, and deduction of PAYG tax.

The contract does not need to be written, but it is valid and legally enforceable when:

- the parties involved intend to create a legal relationship
- one party offers and the other accepts the offer
- both parties obtain a benefit
- both parties have the capacity to contract; for example, they are old enough to make the contract
- consent is genuine and not pressured
- the offer does not contravene any public interest.

Employment contracts need not be overly complex, but a correctly drafted employment contract will be of benefit to both parties in the long term. Attention to detail at the outset ensures that expensive litigation and negative public relations is avoided. A well-written employment contract ensures that the employment relationship commences on the right footing and should contain the essential terms shown in figure 18.11. Independent contractors also have an employment contract, although it is a little different from the conventional employer-employee contact (see the BizFACT on independent contractors).

FIGURE 18.11 Key features of employment contracts



Apart from statutes, the employment contract and other aspects of human resources are governed by common law, awards and agreements.

SNAPSHOT

Case study: Avalon Airport — contract dispute



When George Haros accepted an offer from Linfox to be its Business Manager at Avalon Airport, leaving a secure and long-term relationship elsewhere, he contended that a range of representations had been made to him with respect to the security of the role (at least three years), the longevity of the role (as long as the current GM/MD remained in post) and the exclusivity of the role (only he and the GM/MD would discharge the business management/commercial function). He argued in the Federal Court that all of these representations were misleading and deceptive and contrary to what was then the provisions of the *Trade Practices Act 1974* (now replaced by the *Competition and Consumer Act 2010*). After some four months employment, he was retrenched after his position was determined to be 'redundant'.

His claims were rejected at first instance and on appeal. The Full Bench found on the facts that Haros:

- was himself a qualified lawyer with experience in employment law
- had negotiated the terms of and had signed a written contract which provided for a probation period and termination on three months' notice
- had confirmed that contract to be the 'entire agreement' between the parties, superseding any previous 'negotiations, representations, warranties or Commitments . . . ' (*Haros v. Linfox Australia* [2012] FCAFC 42).

On that basis, it was held that:

Mr Haros did not seek, and was not given, employment for a fixed term; he accepted the position on terms that were negotiated freely; he was under no disability in negotiation, but was an astute lawyer with relevant experience in employment law; he reviewed the draft contract; he did not demur to any of the terms proposed by Linfox; he proposed additional terms which were accepted; and he signed the contract, thereby representing to Linfox that he approved its content or was willing to take the chance of being bound by those contents . . . He was not misled or deceived, so that he was not induced by any such representations to accept Linfox's offer of employment.

The Court also found that although Linfox had frequently used language such as 'potential' and 'opportunity' in describing the role, these terms did not, in this context, equate to 'a promise of any certainty'.

Common law

The **common law** is developed by courts and tribunals. Unlike statutes, it is not made by a parliament. Under common law, judges make decisions based on the facts of a case, guided by precedent (decisions made in the past). The body of common law (also known as case law) is therefore developed from decisions made over time by judges.

Under common law, both parties — employers and employees — have basic obligations in any employment relationship, regardless of whether it is in a formal or informal contract. The obligations of each party are reflected in the rights of the other party.

Employer obligations and rights

Employer obligations include the following.

- *Providing work*. Employers are not allowed to 'stand down' employees if there is no work. They are not generally required to provide work if there is none; however, they must pay the correct wages.
- *Payment of income and expenses*. Employers are required to pay the income (including wages, commission, fees) stipulated in the award, enterprise agreement or contract, and reimburse employees for expenses legitimately incurred as a result of performing their work.

Employers also have rights in the workplace. These include:

- Employees working with care and responsibility, especially in respect to WHS
- Employees carrying out their work according to their agreement/award, including good customer relations and accountability for money or property
- Being notified according to agreement/award of an employee's intention to take their leave entitlements
- Receiving formal advice of a workers intention to leave the business in accord with the award/agreement
- Meeting requirements of industrial relations legislation. This includes
  - providing a workplace and work practices, such as **equity** policies and promotion that are free from discrimination, as required by the sex discrimination, anti-discrimination and equal employment opportunity legislation of the federal and state governments
  - ensuring that workers are protected against unfair dismissal, where this legislation applies. Employers only have the right to dismiss employees who do not obey lawful instructions (insubordination); neglect their duties; are guilty of theft or dishonesty; exhibit wilful or serious misconduct; fail to meet the conditions of the employment contract; and fail to perform satisfactorily over time

common law law developed by courts and tribunals

equity the provision of equal opportunities for all employees to gain access to jobs, training and career paths

- Duty of care. Employers are legally bound under the federal and state Work Health and Safety Acts to provide reasonable care for the safety of the employees by:
  - providing a safe system of work, without risks to health
  - providing and maintaining premises that do not unreasonably expose an employee to risk of injury
  - providing resources, information, training and supervision necessary to ensure the health and safety of workers
  - protecting workers against risks arising out of their work activities.

BizFACT

Convenience store 7-Eleven has paid back 4000 workers $173 million in income in one of the largest cases of wage theft in Australia's corporate history.

Employee obligations and rights

All employees are obliged to observe the following:

- Carry out duties in a way that is beneficial to the business.
- Ensure that they maintain confidentiality and not use information such as sales figures in a way that is detrimental to the operation of the business.
- Account for all money that comes into the business.
- Take reasonable care and act safely in the workplace.
- Follow written and verbal procedures and policies.
- Be honest, fair and work with integrity in all dealings with both colleagues and customers.
- Obey lawful commands that are considered reasonable even if they may not be part of their primary responsibilities.
- Complete forms related to taxation and its deduction from income.
- Give appropriate notice of termination of employment in accordance with the relevant award.

BizFACT

Before you start work you should find out as a minimum:

- what your duties and conditions are
- whether your job is full-time, part-time or casual
- what your wages and allowances are
- your job classification/title
- whether there is a probationary period.

You should not generally be required to work for a trial period if you will not be paid for that period, unless it is part of an approved training course.

Employees also have certain rights when carrying out their work. These include:

- being paid for all the time they work, including overtime where applicable
- receiving the minimum set out in the award or enterprise agreement
- having all pay recorded by the employer (some awards/agreements state that employees must receive a pay slip)
- receiving extra pay such as loading for casuals and penalty rates for work outside of usual hours
- receiving allowances for tools and uniforms if applicable
- having access to paid and unpaid leave entitlements.

FIGURE 18.12 Work health and safety is a responsibility for both employees and employers.



Minimum employment standards

Ten National Employment Standards have been developed in consultation with business, unions and the community. They must be provided by employers and state minimum conditions for employees. They have been planned to provide a greater safety net for employees, particularly for the most vulnerable and low-paid employees in the workforce. They provide the basis from which modern awards and enterprise agreements are constructed.

FIGURE 18.13 National Employment Standards

National Employment Standards

1. **Maximum weekly hours of work** — 38 hours per week, plus reasonable additional hours
2. **Requests for flexible working arrangements** — parents or carers of children under 18 are allowed to request a change in working arrangements to assist with the child's care.
3. **Parental leave and related entitlements** — up to 12 months unpaid leave for every employee, plus a right to request an additional 12 months unpaid leave, and other forms of leave
4. **Annual leave** — four weeks paid leave per year, plus an additional week for certain shift workers
5. **Personal/carer's leave and compassionate leave** — 10 days paid personal/carer's leave, two days unpaid carer's leave as required, and two days compassionate leave (unpaid for casuals) as required.
6. **Community service leave** — unpaid leave for voluntary emergency activities and leave for jury service, with an entitlement to be paid for up to 10 days for jury service
7. **Long service leave** — a transitional entitlement for employees who had certain LSL entitlements before 1/1/10 pending the development of a uniform national long service leave standard.
8. **Public holidays** — a paid day off on a public holiday, except where reasonably requested to work
9. **Notice of termination and redundancy pay** — up to four weeks notice of termination (five weeks if the employee is over 45 and has at least two years of continuous service) and up to 16 weeks redundancy pay, both based on length of service
10. **Provision of a Fair Work Information Statement** — employers must provide this statement to all new employees about major employment matters and bodies.

BizFACT

In July 2020, the Fair Work Commission handed down an increase in the national minimum wage to $753.80 (before tax) for full-time workers or $19.84 per hour plus 25 per cent loading for casuals.

Employees under 21 years of age receive a percentage of this hourly minimum, depending on their age.

Minimum wage rates

The minimum wage rate in Australia is an employee's base rate of pay for the number of ordinary hours that they have worked and is generally determined by a modern award, enterprise agreement or the national minimum wage. The minimum wage rate is reviewed by a the Fair Work Commission's Expert Wage Panel each year and will take effect from the first pay period after 1 July of that year. Both employees and employers cannot agree upon a pay rate that is less than the minimum wage.

SNAPSHOT

Case study: Shocking yet not surprising — wage theft has become a culturally accepted part of business

Many Australians were shocked by celebrity chef George Calombaris being caught for underpaying employees $7.8 million. It didn't help, of course, that the television personality was also reported at the time to be seeking a huge pay rise for appearing in the television program *MasterChef Australia*. But what should not be a surprise is the how common wage theft — typically underpaying award rates and entitlements such as overtime, superannuation and penalty rates — is in Australia.



In recent years there have been equally large cases of wage theft involving businesses such as Caltex, 7-Eleven, Pizza Hut and Domino's Pizza.

The Australian Taxation Office has estimated that in 2014–2015 Australian workers had been short-changed $2.5 billion on superannuation payments alone.

Workplace audits by the federal Fair Work Ombudsman over the past decade suggest wage theft is rising. Most vulnerable are the young, the low-skilled and temporary migrants.

And the sectors where wage theft appears most common: food services and in certain types of business structures such as franchise operations, outsourcing, insecure work and the gig economy.

Wage theft seems to have become accepted as a fact of life, maybe even a necessity, in certain sectors and workplaces. As a result, employers have developed a lack of responsibility while workers have become resigned to underpayment as unavoidable.

More than three-quarters of international students and backpackers, for example, know they're being underpaid but accept it because they believe it's standard treatment for anyone on their type of visa. Cultural acceptance such as this translates into weak enforcement rules.

Wage theft is not considered a criminal offence, in the same way as stealing money from a company. Those caught face low penalties. Calombaris, for example, has to pay his employees what they are owed, but his penalty is limited to $200 000.

The federal government has indicated it will propose new laws to make wage theft a criminal offence, punishable with prison time. Along with tougher laws, more resources for enforcement are also needed.

Other reforms could help too. Supply chain certification, similar to the schemes used to guarantee fairtrade coffee or sustainably caught fish, are an example. The Fairwork Ombudsman has partnered with business and unions to create a pilot certification scheme for the cleaning industry.

Modern slavery legislation now requires large companies to report on their efforts to keep their supply chains slave-free. Acceptance of such reporting obligations could pave the way for the expectation that companies pay more attention to stamping out all forms of worker exploitation.

Source: Sarah Kaine & Emmanuel Josserand, 'Shocking yet not surprising: wage theft has become a culturally accepted part of business', *The Conversation*, 31 July 2019.

Awards

An award is a determination that explains the legally enforceable minimum terms and conditions that apply to a business or industry. 'Modern awards' are a key feature of the current industrial relations system that sought to simplify some 2400 older existing awards into industry or occupation-based categories. This was undertaken to reduce the confusion surrounding proper minimum employment entitlements. Examples of awards include the Air Pilots Award (2020) and the Real Estate Industry Award (2020).

There are more than 100 industry or occupation awards that cover most workers in Australia. This number changes as the Fair Work Commission continues to review all modern awards every four years, The contents of modern awards are as follows:

- base pay rates
- conditions and requirements for different types of employment (for example, full-time, part-time or casual)
- overtime and penalty rates
- allowances (such as travel allowances)
- leave and leave loading
- hours of work (for example, rosters, making changes to working hours)
- requirements for annual wage or salary arrangements
- superannuation entitlement
- conditions and procedures for consultation, representation and settling disputes
- outworkers
- redundancy conditions.

The conditions in the modern award apply on top of the minimum conditions in the National Employment Standards (NES). Awards are used as the basis for the negotiation of an enterprise agreement.

Modern awards also have a 'flexibility term' that allows employers and employees to negotiate changes to some of the conditions in the modern award. These are called **Individual Flexibility Agreements (IFA)**. They allow an employer and an employee to come to an agreement that varies the modern award or enterprise agreement in order to address individual circumstances. The arrangement must not undermine minimum employee entitlements and must leave the employee better off (usually assessed financially) on the IFA compared to the award or enterprise agreement.

The IFA can only address the following areas:

- arrangements for when work is performed, such as working hours
- overtime rates
- penalty rates
- allowances, and
- leave loading.

Individual Flexibility Agreements (IFA) allow an employer and an employee to come to an agreement that varies the modern award or enterprise agreement to address their individual circumstances

For example, Chicka works at Famous Johnny's Fishing and Tackle on the mid-north coast, NSW. His son Sal is a keen fisherman who sometimes takes a few risks when he goes rock fishing and Chicka thinks it's a good idea for him to accompany Sal when he goes. Chicka asks his supervisor Zoe if it would be possible for him to leave an hour early so that he can escort Sal every Tuesday afternoon on his fishing jaunts.

FIGURE 18.14 The Real Estate Industry Award (2020) was one of the recently reviewed awards.



Chicka knows he would be finishing ahead of his regular finishing time, but indicates that he's happy to stay back another afternoon to make up the time. Zoe explains to Chicka that his enterprise agreement contains an IFA that allows for him to finish early one day and then make up the time later in the week. Chicka is happy with such a flexible arrangement and his employer does not lose out as he still works the same hours.

SNAPSHOT

Case study: Modern awards — changes to penalty rates

The four-yearly review of modern awards was handed down by the Fair Work Commission (FWC) in early 2017. The focus of its decision was the need to modify weekend and public holiday penalty rates. There was much discussion about the merits or otherwise of changing entitlements for those (often younger) workers toiling away outside more traditional work hours.



Many casual staff had become accustomed to the additional rates of pay that had been a feature of Australia's workplaces for more than 100 years. The extra pay was seen as recognition that many social events (including religious services) are organised for Sundays and public holidays and that workers sacrificed the benefits of time spent with family and friends if they worked to provide services for others on those days.

The FWC received thousands of submissions from both industry and union groups as well as individuals regarding the proposed changes to penalty rates. Ultimately its decision was to:

- reduce Sunday penalty rates for those covered by the fast-food, hospitality, retail and pharmacy awards
- phase in changes over a number of years; to be finalised by 2019 or 2020
- cut penalty rates for full-time and part-time workers in retail and pharmacy from 200 per cent to 150 per cent of current rates and for casuals from 225 per cent to 175 per cent
- change penalty rates for full-time or part-time workers in the fast-food industry from their current Sunday rate of 150 per cent to 125 per cent and for casuals from 175 per cent to 150 per cent
- decrease penalty rates for hospitality workers so that Sunday pay rates will fall from 175 per cent to 150 per cent.

While the transitional nature of many of these reductions will be gradual, changes for public holidays would begin immediately. The changes across the aforementioned industries mostly resulted in a reduction in penalty rates from 250 per cent to 225 per cent for full-time and part-time workers and from 275 per cent to 250 per cent for casuals.

The FWC decision affects approximately 4 per cent of Australia's workforce and is aimed at assisting the small business sector (including franchisees) in particular, which had indicated that existing penalty rates were a financial burden that made opening on weekends and public holidays costly.

Those against the cut including major unions suggested that those workers affected by the changes to penalty rates would now need to work extra hours to make up for the loss.

Source: Adapted from Michelle Grattan, 'Sunday penalty rates to be phased down', *The Conversation,* 5 June 2017; Shirley Jackson, 'Cutting Sunday penalty rates will hurt young people most', *The Conversation*, 23 February 2017.

Enterprise agreements

Enterprise agreements are **collective agreements** made at a workplace (enterprise) level between an employer and a group of employees about terms and conditions of employment. They offer broader terms and conditions than a modern award, and are an alternative to a modern award.

Under the *Fair Work Act 2009*, there are three types of enterprise agreements.

- *Single-enterprise agreements* — made between a single employer and a group of employees. They can involve more than one employer in limited cases (e.g. where two or more employers are engaged in a joint venture).
- *Multi-enterprise agreements* — made between two or more employers and groups of their employees. This may occur if they share common funding, operate collaboratively and have a common regulatory system, such as a group of hospitals.
- *Greenfields agreements* — single-enterprise and multi-enterprise agreements relating to a genuine new enterprise of the employer(s) that are made before any employees to be covered by the agreement are employed. Greenfields agreements are made with one or more relevant unions.

The key features of enterprise agreements are:

- They may cover rates of pay, penalty rates and overtime, allowances, hours of work, personal and annual leave, any matters related to the relationship between the employer and the employees, plus their representative organisations involved, and how the agreement will operate, including a nominal expiry date.
- They must be approved by the Fair Work Commission, who must be satisfied that the agreement
  - has been made with the genuine agreement of those involved
  - passes a **'better off overall test' (BOOT)** compared to the modern award
  - does not include any unlawful terms or designated outworker terms
  - covers a representative group of employees
  - covers matters that may be included in an enterprise agreement
  - has a specified nominal expiry date (within four years of the Fair Work Commission's approval)
  - includes a dispute settlement procedure, including an option for disputes to be brought before an independent person, such as the Fair Work Commission, for arbitration if the parties agree to it
  - includes a flexibility clause and a consultation clause, allowing for variations if required
  - provides opportunities for employees to be represented by a bargaining representative and to bargain in good faith during the negotiation of an agreement.

enterprise agreement a collective agreement made at a workplace level between an employer and a group of employees about terms and conditions of employment

collective agreement an agreement made between a group of employees (or one or more unions representing employees) and an employer or group of employers

'better off overall test' (BOOT) requires that each of the employees to be covered by the agreement is better off overall than under the relevant modern award

BizFACT

The most common method of setting pay for full-time employees is by collective agreement, such as an award or enterprise agreement.

To ensure that the parties bargain in good faith, there are strict rules relating to the enterprise bargaining process. They must make a serious attempt to negotiate the issues in a timely and fair manner, and genuinely make an effort to consider all proposals tabled.

Other employment contracts

As the nature of work changes, greater variety is occurring in the types and features of employment contracts available.

Individual common law employment contracts

These **individual contracts** of service cover employees not on federal agreements or specific state agreements, particularly for those earning higher incomes.

Individual contracts are more common in the private sector, particularly in non-union enterprises, in partly or wholly owned foreign firms, in the wholesale trade, and in property and business services. They are also more common at the professional and managerial level and for workers currently earning more than $153 600 per year. This figure changes annually.

Such contracts may be written or verbal. Many are informal and offer much less protection than other agreements. Although around half vary significantly from their related awards, they are generally required to provide conditions that equate with minimum provisions of related awards; if they do not, they are in breach of the law.

Comparing the process of negotiating enterprise/collective agreements with the negotiation of individual contracts

Enterprise agreements between one or more federal system employers and employees are negotiated by the parties through the collective bargaining process and for the most part at the enterprise (any kind of business, activity, project or undertaking) level.

According to the Fair Work Act an enterprise agreement should include:

- terms about the relationship between the parties to the agreement
- deductions from wages for any purpose authorised by the employee
- how the agreement will operate, a nominal expiry date that is no longer than four years from Fair Work Commission approval
- dispute settlement procedure about matters relating to the modern award or National Employment Standards
- reference to Individual Flexibility Agreements (IFA)
- consultation terms in the event of any major changes likely to affect employees significantly.

Enterprise agreements are an example of a registered agreement that can apply to one business or a group of businesses. Although no longer possible, Australian Workplace Agreements (AWAs) could previously be made with individual employees. In the event that there is an agreement it must be formally approved and registered by the Fair Work Commission.

The process of making an enterprise agreement is summarised in figure 18.15 and complies with the framework identified under the Fair Work Act, which assists employers and employees in this process.

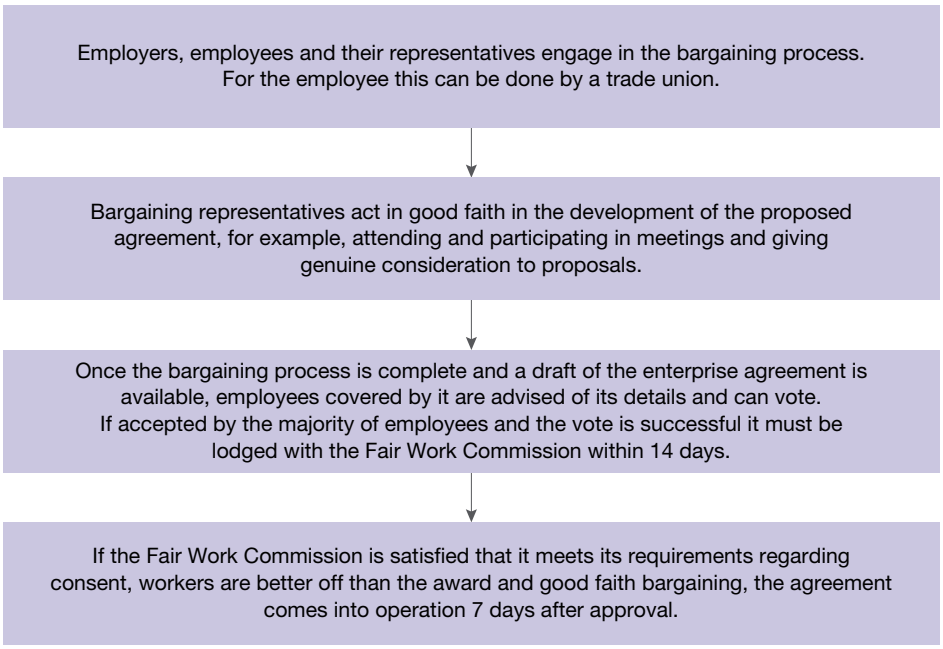
individual contract when an employer and an individual employee negotiate a contract covering pay and conditions

BizFACT

The Fair Work Commission permits an official to:

- investigate suspected breaches of the Fair Work Act 2009 and other workplace laws
- investigate breaches relating to textile, clothing and footwear industry outworkers
- hold a meeting with employees
- exercise rights under work health and safety laws.

FIGURE 18.15 The process of making an enterprise agreement



For most workers the process outlined in figure 18.15 applies. However, all employees do have an individual contract with their employers and this determines the rights and obligations of both parties. This contract must meet the minimum requirements under the Fair Work Act, which includes the conditions identified in the National Employment Standards (NES) and the national minimum wage.

While many employees will be protected by an award or enterprise agreement, there is provision for those not covered and who do not fit the usual enterprise agreement mould.

These employees are considered to be award and agreement free. In the event that this occurs, an employment contract will apply to them. This contract must include remuneration, hours of work, breaks and overtime, public holidays, leave and termination of employment and must not leave them worse off than the minimum entitlements.

For example, Simon is a senior manager of a group of hotels in the inner west of Sydney. His salary is $150 000 per year. While there is provision for some management to be covered in the relevant hospitality award this does not apply to Simon because he is considered a senior manager. As such Simon had to establish his entitlements when he commenced work with the hotel group through his employment contract and the Fair Work Act. While not covered by the award his contract must still meet minimum requirements of the NES even if he agreed to less. For example, his contract states that he is entitled to five days of sick leave per year, however, he would be still entitled to 10 days paid leave, which includes personal/carer's leave as per the NES.

Awards have not usually covered managers like Simon and other professionals such as accountants, IT specialists and those in the human resources field. They often earn high incomes and more traditional awards do not apply to them. Currently the measure of the high-income threshold is $153 600, but changes annually. The employee must have accepted a guarantee of such earnings, which can include a cash and non-monetary benefit upon commencement.

Independent contractors

Independent contractors, often known as consultants or freelancers, undertake work for others; however, they do not have the same legal status as an employee. This is a growing area of employment comprising 9 per cent of the workforce.

independent contractor often known as a consultant or freelancer, independent contractors undertake work for others; however, they do not have the same legal status as an employee

BizFACT

The Australian Bureau of Statistics identifies independent contractors as operating as employees, owner managers of incorporated enterprises and owner managers of unincorporated enterprises.

Most contractors are male (72%) and older than 45 (55%).

Independent male contractors were technicians and trade workers (36%) and professionals (19%) whereas independent women contractors were professionals (38%) and clerical and administrative workers (18%).

Independent contractors generally undertake a contract, service or project for another business, and work for multiple clients. Contractors tend to have a set term or specific project for their contract, control their own work and may delegate some of their work to others. They generally submit an invoice on completion of a task, stage or project.

The Fair Work Commission, through the *Independent Contractors Act 2006*, provides a clear set of criteria, developed through past test cases, to determine whether someone is a contractor or employee. A contractor carries most of the risk on a job undertaken, including covering their own superannuation, tax, insurances and leave. This is why many employers prefer to rely on independent contractors as it allows employment risks such as sickness to be shifted to the person undertaking the work.

Contracts for casual work

There are 2.6 million casual workers (25 per cent of the workforce) in Australia (2019). Women account for 50 per cent of casual employees and 40 per cent were aged between 15 and 24 years. **Casual employees** have contracts with employers for short-term, irregular or seasonal work. Their work period may vary, they are paid on an hourly or daily basis, and are not entitled to paid leave. Most casuals are female or young people, and often students. Many employers prefer casual staff as it reduces costs for recruitment and dismissals and other **on-costs**. They often receive a 20–25 per cent loading (extra pay) to compensate them for their lack of entitlements and job security.

Casual employees receive two days unpaid carer's leave and two days unpaid compassionate leave per occasion, five days unpaid family and domestic violence leave (inside a 12-month period) and unpaid community service leave.

If they are employed regularly, or for a long period of time, they may be eligible for some benefits such as superannuation and long-service leave and after at least 12 months of regular employment (and if it is likely that the relationship will continue) a casual employee can request flexible working arrangements and/or take parental leave.

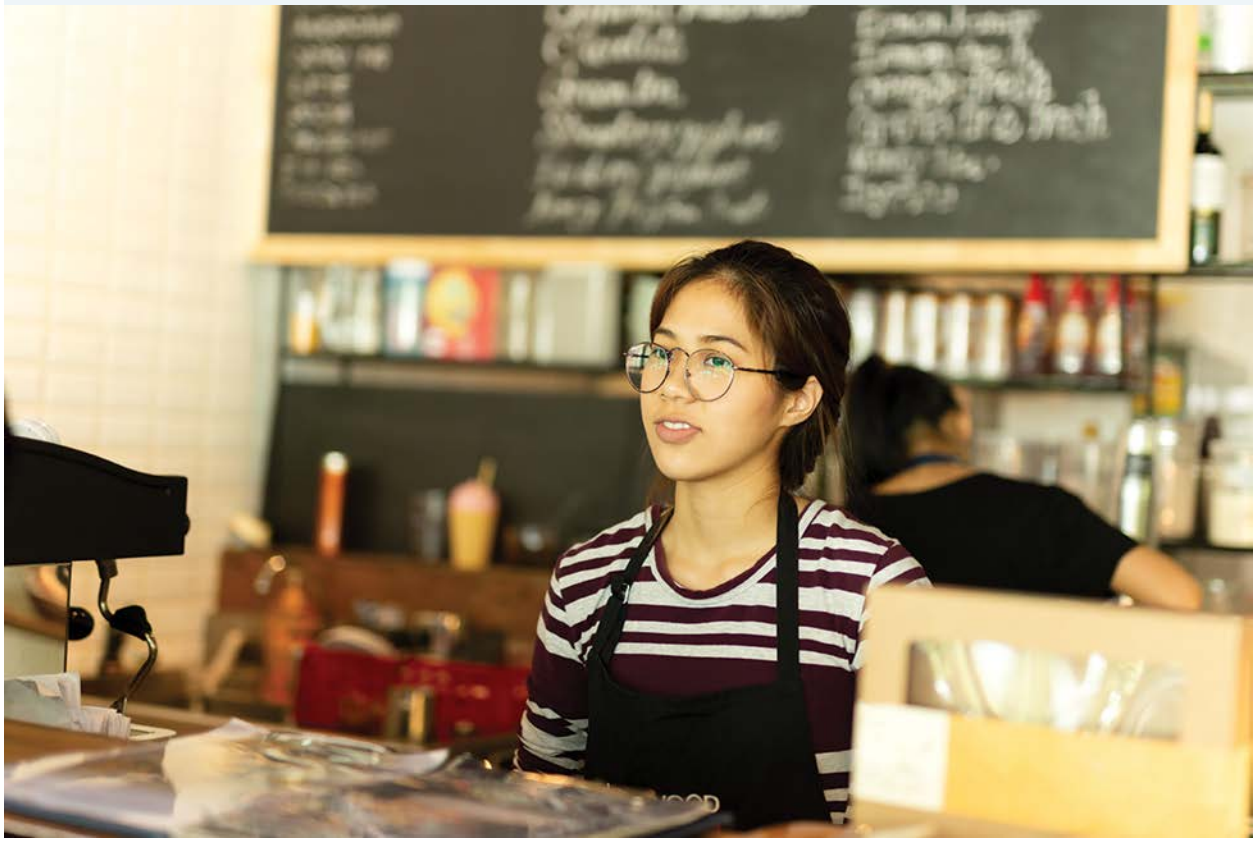
In the event that the employee and employer agree then the casual employee can change to full-time or part-time employment at any time.

Many casual employees find they miss out on training and promotion, experience fluctuating income, and have difficulty obtaining credit. They are also more likely to experience workplace accidents and are less committed to the organisations that employ them.

casual employee an employee in employment that is short term, irregular and uncertain; they are not entitled to paid holiday or sick leave

on-costs additional costs involved in hiring an employee, above the cost of their wages. These costs traditionally add around 25 per cent of the cost of the wage and include sick leave, holiday leave, leave loading, superannuation, retirement and redundancy payments, and other costs.

FIGURE 18.16 Twenty-six per cent of employees aged 15 to 24 years are casual workers.



BizFACT

The most popular occupations for casual workers are sales assistants and salespersons, hospitality workers, carers and aides, sales support workers and food preparation assistants.

The decision by the federal government to slow the spread of COVID-19 by reducing opportunities for social gatherings affected many of the industries identified above.

In response the government introduced a JobKeeper payment of $1500 per fortnight to those employees that have lost their job due to significantly reduced sales turnover where they work, and a JobSeeker payment of $550 per fortnight for short-term casual workers who have lost their job (and who meet eligibility requirements).

Part-time contracts

The trend towards part-time work is increasing in Australia, with 32 per cent of all employees now employed on a part-time basis. During the global financial crisis and the early stages of the COVID-19 pandemic, employers reduced work hours for some employees in response to the subsequent economic downturn. This trend has continued and with the rise of two income households and the desire for a greater work–life balance, part-time contracts will continue to grow. Around 25 per cent of part-time employees are underemployed and would like more work. Forty-three per cent of women work part-time compared to 13 per cent of men.

Part-time employees have a continuing employment contract and work less than 38 hours per week. Unlike casual employees, they do have access to the employment entitlements offered to full-time employees, but on a pro rata basis (in proportion to the percentage of time they work compared to a full-time employee).

SNAPSHOT

Case study: Employment contracts — a mixed bag



Fifi, Moshe and Ozkan, old high school mates, are having a coffee in a local shopping centre, while discussing issues related to their jobs. Moshe works as a casual employee for a clothing store and is studying full time at university. Fifi is a supervisor at the local bank and Ozkan runs the local pet shop and boarding kennels.

***Ozkan**:* All this legal stuff is giving me a headache!

***Fifi**:* What legal stuff?

***Ozkan**:* I have to make sure all my staff are being treated as it says in the award or we will be fined again.

***Fifi**:* Why is it such a problem?

***Ozkan**:* Have you seen an award? It goes on for pages, with lots of details about hours, rates for juniors, leave arrangements, shift length (which got us into trouble last time), consultation procedures and arrangements for managing change (which I must admit I ignored last time). I've also got to worry about work health and safety all the time, like slips and trips. What kind of work arrangements have you got?

***Fifi**:* I'm on an enterprise agreement. I'm a bit luckier than the others though because my boss pays me a little more than the award. I'm prepared to work long hours and the customers like my style, apparently.

***Ozkan**:* How much did you pay the customers to tell the bank that?

***Moshe**:* What do the other supervisors think?

***Fifi**:* Well, they don't really know I'm paid more. Some of them seem to think I do earn a bit more, but I haven't told them how much I'm getting.

***Ozkan**:* I bet the others would love to know that. They must be so cooperative with you at work.

Fifi: Well, they gossip a bit, but I just get on with my work. I don't care about the others that much; they're not that friendly and they don't talk to me much.

***Ozkan**:* (rolls eyes) I wonder why. Do you think any others get paid more?

***Fifi**:* No, someone in management told me I'm the highest paid.

***Ozkan**:* Do you think any deserve more?

***Fifi**:* There is one guy who does a great job, but his English is not quite where it needs to be, so he is not paid the extra amount.

***Moshe**:* That sounds like a bit of discrimination to me. I bet if he were a union member the union would sort that out.

***Fifi**:* Oh, unions just make trouble.

***Moshe**:* Mate, the reason your safety and leave conditions are so good is due to all the groundwork unions did in the past! There was a time when you could have been sent to jail for going on strike. You just take it all for granted!

***Fifi**:* Yes, we needed unions then. But I don't see the need for them now in this sort of job. It would be different if I were a miner. How does it all work in your job?

***Moshe**:* Well, I'm in the union just in case I need help one day, even though I'm a casual. How are you going to cope if you have a problem? You haven't got much bargaining power. What if you and Eren have kids? How will your letter help you then? I'm on a casual rate, which is okay as I get 25 per cent more per hour than full-timers

to make up for all the benefits I miss out on, such as sick and long service leave. There is no way I would stay a casual in the long term because you can't get credit easily, so there goes the car or home loan.

Ozkan: You don't get training or career development either. We've found that if you have too many casuals coming and going, no one knows what's going on, mistakes happen and can't be followed up.

Moshe: Yeah. It's hard to survive on a yo-yo income too. If your employers don't need you, they don't call you. If they don't want you anymore, they just reduce your hours and you can't do anything about it. And, of course, if you get sick, bad luck!

Ozkan: Well, maybe awards and agreements aren't so bad after all. At least all my staff get on well, their hours are regular and they get minimum wage increases regularly.

Fifi: Yeah, but you know workers on awards are the lowest paid workers of all! Lots of them are women too — women often seem to work in award-based, poorly paid occupations.

Ozkan: Yeah, but you have hardly any protection if you have a problem at work with your deal. At least they have their rights down on paper. The owner is talking to the union about developing an enterprise agreement for all the staff so we can add more incentives, such as more flexible working hours for staff who are parents or carers. I must admit, they try to be helpful. Sarita is allowed time off when her dad needs to be taken to the hospital and I'm sure Jenna uses most of her sick days to look after her kids. It's tough at times because the animals bark and howl if we don't feed them on time!

Fifi: Yeah, yeah — a likely story!

on Resources

Weblink Fair Work Commission

KEY IDEAS

- From 2007, under the Labor government, most Australian states and territories formed a national system for industrial relations to improve efficiency through more uniform laws and regulations.
- Australia had a centralised system of industrial relations until 1991 when enterprise bargaining was introduced.
- All employees are covered by an employment contract, even if it is not written.
- A written contract provides more comprehensive protection than a verbal contract.
- Independent contractors are self-employed and do not have the same rights as employees.
- Workplace relations are governed by common law, statutes made by parliament through legislation, and awards and agreements supervised by industrial tribunals.
- All employees and employers have legal rights and responsibilities.
- Employers must pay income and work expenses, comply with industrial laws, and provide a safe workplace for employees.
- Employees must obey lawful and reasonable demands made by the employer, use care and skill in their work, and act in good faith and in the interests of the employer.
- Under the national system, from 2010, ten minimum employment standards were established to provide a safety net for employees, particularly the low paid.
- Replacing many functions formerly conducted by the Australian Industrial Relations Commission, the Fair Work Commission was set up to manage awards and agreements, hear and help resolve industrial disputes, determine annual minimum wage cases, and supervise award restructuring.
- Employee wages and conditions are primarily determined by awards, enterprise agreements and minimum employment standards.
- From 2010, minimum wage rates for ordinary hours worked have been determined by:
  - award or agreement that covers the employee
  - the national wage minimum for employees not covered by awards or agreements and reviewed annually by the Fair Work Commission.

- Awards are legally binding documents containing the minimum terms and conditions of employment.
- Enterprise agreements are collective agreements made at the workplace (enterprise) level between an employer and a group of employees about terms and conditions of employment.
- Individual contracts of service exist when an employer and an individual employee negotiate a contract covering pay and conditions.
- Independent contractors, often known as consultants or freelancers, undertake work for others but do not have the same legal status as an employee.
- The government, both federal and at state level, has the role of ensuring that Australia has a flexible, modern workplace that supports a national industrial relations framework with clear and enforceable minimum national employment standards.

18.3 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

18.3 Quick quiz on	18.3 Exercise	18.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 3, 5, 9, 11, 12, 13, 16, 17, 18, 20, 21, 22, 23, 24, 25, 27, 28	1, 4, 6, 7, 8, 10, 15, 19, 26, 29	14, 30

18.3 Exercise

Revision

1. **Distinguish** between a centralised and a decentralised industrial relations system.
2. **Define** the term 'employment contract'.
3. **State** the conditions that need to exist for an employment contract to be valid and legally enforceable.
4. **How** is common law used to determine employment conditions?
5. Complete the table below to **summarise** the obligations of employers and employees in an employment relationship. The first one has been started for you.

Obligations in an employment contract under common law	
Employers	**Employees**
• Provide work: cannot 'stand down' employees if there is no work	

6. **Justify** the requirement to 'act in good faith' as an employee.
7. **Why** are the National Employment Standards necessary?
8. Select what you consider to be the two most important National Employment Standards. **Account** for why you think they were included.
9. **Outline** how minimum wage rates are determined.
10. **Examine** the current minimum wage rates, which can be found on the **Fair Work Commission** website. In July 2011, the national minimum wage was $589.30 per week (before tax), or $15.50 per hour. **Compare** this with the current rate and account for the difference.
11. Apart from wage rates, **identify** seven factors contained in an award.
12. **Describe** the process that occurs if an employee reports a breach of an award.
13. **a. Define** the term 'enterprise agreement'.
    b. Why are they sometimes referred to as collective agreements?
14. **Create** a PowerPoint presentation that compares the major types of agreements. Write a profile for each type of agreement, illustrating the typical type of person who would use each agreement.

15. 'Employee wages and conditions are primarily determined by awards, agreements and minimum national standards.' **Explain**.
16. **What** are the features of the 'other employment contracts'?

Read the 'Avalon Airport — contract dispute' case study and answer questions 17 to 19.

17. **Outline** the guarantees that Mr Haros believed were given to him regarding the nature of his employment.
18. **Identify** what law Mr Haros believed the company was breaking.
19. **Explain** how the matter was dealt with by the Federal Court.

Read the case study 'Shocking yet not surprising — wage theft has become a culturally accepted part of the business' and answer questions 20 to 24.

20. **What** is wage theft?
21. **List** some of the businesses identified as engaging in wage theft.
22. **Identify** the most vulnerable workers, sectors and business structures of the community when it comes to wage theft.
23. **What** evidence is there to accept that wage theft is becoming a cultural 'norm' in Australia?
24. **Outline** examples of wage theft reform practices that have become apparent.

Read the 'Modern awards — changes to penalty rates' case study and answer questions 25 to 28.

25. **What** was the decision made by the FWC?
26. **Why** were penalty rates originally introduced?
27. **Summarise** the changes to the industries affected by the FWC decision.
28. **List** the advantages and disadvantages of the changes to penalty rates for the industries identified in the article.
29. **Examine** the information given in the case study 'Employment contracts — a mixed bag' to complete the following table.

Agreement	Main features	Advantages	Disadvantages
Collective agreement	Legally binding document stating minimum terms and conditions of employment		
Enterprise agreement		Can be tailored to fit needs of employee(s) and employer	
Contract for employment	Independent contractors		
Casual employment	25 per cent loading		

Extension

30. More than half of all newly hired employees do not discuss their conditions of employment with their employer before starting work. Many of these are young or less educated people.
    a. **Create** a short script with your classmates to help a young person ask a prospective employer about their conditions of employment.
    b. Identify the major items that should be in an employment contract. Next to each, explain why these are necessary.
    c. Use information from the Fair Work Commission website to investigate pay and conditions.
    d. **Analyse** the risks of failing to discuss conditions of work with a new employer.
    e. Explain how membership of a trade union may help you avoid these risks.

18.3 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q2

Betty believes she is eligible to ask her employer for flexible working arrangements.

Which of the following is a provision of the *Fair Work Act 2009* (Cth) that gives Betty the right to make this request?

A. A modern award
B. A common law contract
C. An enterprise agreement
D. Minimum employment standards

Question 2 (6 marks)

Source: HSC 2019 Business Studies Exam, Section II, Q23a & b

a. Outline ONE employer obligation in an employment contract. **(2 marks)**
b. Distinguish between awards and enterprise agreements. **(4 marks)**

Question 3 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q1

Sarah works 40 hours per week. Her contract entitles her to sick leave, paid annual leave and superannuation.

What type of employment is this?

A. Casual full-time
B. Casual part-time
C. Permanent full-time
D. Permanent part-time

Question 4 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q20

An independent web designer has a legal agreement with a department store to improve its online shopping site in time for the Christmas sales.

The web designer's working conditions are specified in

A. an award.
B. the contract for service.
C. an enterprise agreement.
D. the National Employment Standards.

Question 5 (2 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q22a

Describe ONE common law obligation of an employee.

More exam questions are available in your learnON title.

18.4 Legal influences: Work health and safety and anti-discrimination

SYLLABUS LINK In this subtopic you will learn about:
- work health and safety and workers compensation
- anti-discrimination and equal employment opportunity.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

18.4.1 Work health and safety (WHS)

Growing community and worker awareness of safety and environmental issues, along with ballooning compensation costs in recent decades, have prompted both federal and state governments to improve work health and safety (WHS). In 1985, the Commonwealth Government, concerned at the high levels of injury, accidents and disease in the workplace, introduced the *National Occupational Health and Safety Commission Act 1985*.

BizFACT

On 1 June 2011 the New South Wales government passed the *Work Health and Safety (WHS) Act 2011*. Many aspects of the original occupational health and safety legislation have been carried over to the new WHS Act. WHS has as its core the safety and protection of employees.

Safe Work Australia, formerly WorkSafe, was established to conduct research and develop national standards, codes of practice and common approaches to WHS legislation, which are endorsed by state governments. However, due to constitutional limitations, the ability to enact and enforce WHS legislation has always been passed to the states. Common law supports legislation developed by the states, by requiring that employers provide competent staff and a reasonably safe system of work. Since then, Safe Work Australia has worked with state governments to harmonise WHS laws. This is intended to lead to a national system of WHS and workers' compensation, which will improve productivity by reducing the compliance costs of businesses and improve the quality of WHS conditions for all Australians.

BizFACT

In 2019 there were 183 worker deaths in Australia compared to 144 in 2018. Agriculture, forestry, fishing, transport, postal and warehousing represent the industries with the highest worker fatalities.

WHS legislation covers employees, employers and the self-employed. In New South Wales, under the *Work Health and Safety (WHS) Act 2011*, the following is required:
- Employers must ensure the health, safety and welfare at work of all employees by providing a safe system of work; ensuring that plant and substances are used, handled, stored and transported safely; giving employees the necessary information about the plant and substances, and training and supervision in their work; maintaining the site in a safe condition; and ensuring that the goods they design, make, supply, install or repair will not injure or damage the health of others.
- All employers must take out workers' compensation insurance, or face imprisonment or a substantial monetary fine. The compensation scheme generates its funds via the premiums paid by employers, and provides medical and financial support to injured workers. The premium paid will depend on the industry that the business is in, the amount of wages paid to workers, the costs of any claims made by injured workers and the dust diseases levy.

- Employers must take steps to ensure that people on-site who are not employees are not exposed to risks arising from work being undertaken.
- Employees are required to take reasonable care for the health and safety of others, to cooperate with employers and comply with WHS requirements.
- Employees who engage in bullying, skylarking or interfering with machinery or any other behaviour that puts other employees at risk are breaching their duties and could be fined.
- Health and safety committees must be established at workplaces with more than 20 employees if requested by a majority of employees or if directed by SafeWork NSW.
- SafeWork NSW inspectors may inspect the workplace, collect information, and issue improvement and prohibition notices under the *Factories, Shops and Industries Act 1962 (NSW)*. This may, in some cases, mean that work ceases.
- SafeWork NSW must be notified of any deaths or serious injuries in the workplace, and any plans to carry out dangerous work.
- The highest penalty under the WHS Act is for industrial manslaughter where a person conducting a business or undertaking (PCBU), or a senior officer, negligently causes the death of a worker. Where a PCBU, or senior officer, commits industrial manslaughter, a maximum penalty of 20 years' imprisonment for an individual, or $10 000 000 for a body corporate, applies.
  There are other categories of penalties where the fine ranges from $3 463 000 (corporation) to $50 000 (individual/worker) and/or jail depending upon the severity of the breach.

SafeWork NSW recommends employers use a six-step approach to WHS to prevent accidents, disease, injuries and work-related ill health (see figure 18.17).

FIGURE 18.17 A six-step approach to WHS



BizFACT

Q: Who is responsible for work health and safety:

- Employers
- Manufacturers
- Designers and suppliers
- People in control of workplaces
- People who erect and install plant and equipment
- Employees?

A: Everyone!

FIGURE 18.18 Workplace accidents resulting in death are most common in transport, postal and warehousing industries.



BizFACT

Safe Work Australia produced a fact sheet to assist employers with keeping workers safe and limit the spread of the virus during the COVID-19 pandemic.

The key features of the document included: encouraging staff to work from home where they could, avoiding close contact through social distancing, engaging in good hygiene such as frequent hand washing or sanitising, displaying signage and posters to remind workers of the risks posed by the virus, cleaning and disinfecting the workplace regularly and self isolation if a worker has COVID-19 or has been in close contact with a confirmed case.

SNAPSHOT

Case study: Woolworths — health and safety

Organisational management at businesses such as the Woolworths Group and its range of companies is expected to consider work health and safety in its corporate responsibility report, which is often a component of annual reporting requirements. To this end it constantly assesses how to ensure safety for both workers and customers. Its current initiative Destination Zero is a core focus that considers ways to ensure there is no harm to its people, environment or the communities it serves. Its aim is embodied in the philosophy, 'No task is so urgent and no service so important that we cannot take time to do it safely'. This commitment is reflected in:

- continued reductions in 'lost time' (time lost through workplace injury)
- National Safety Council of Australia highly commended award for introducing safer loading docks for the delivery of groceries
- reduced manual handling injuries through more ergonomic technology when workers engage in heavy lifting
- improved safety in its band saws that cease operating when it comes into contact with a special glove used by the operator
- use of an external contractor to conduct an independent risk analysis of stores
- improved employee nutrition and health through staff Lunch and Learn sessions that were also uploaded to the wellbeing website for staff unable to attend
- Employee Assistance Program that offers confidential counselling in partnership with external specialists.

Unions also play an active role in WHS. The Australian Council of Trade Unions (ACTU) conducts its own surveys; for example, a recent study of around 10 000 employees, about employment security and working hours, found that 49 per cent of employees suffered health problems because of their working arrangements, including stress (76 per cent) and continual fatigue (72 per cent), and 25 per cent experienced accidents or near misses.

BizFACT

It is an offence to dismiss an employee or alter an employee's job to his or her detriment because the employee has pursued a WHS matter. Managers must visibly and actively support supervisors in solving WHS issues.

In best practice businesses, management undertakes regular safety audits, benchmarks their performance and implements comprehensive safety programs. Policy statements, safety signs and reminders are visible, and there is regular ongoing training for staff who are aware of safety rules and prepared for emergencies.

18.4.2 Workers' compensation

State legislation covers employees for **workers' compensation** matters, unless they are Commonwealth Government employees. In New South Wales, workers' compensation matters are administered by the State Insurance Regulatory Authority (SIRA) and Insurance & Care NSW (icare). SIRA regulates workers' compensation to ensure an equitable system and support workers with injuries related to their employment.

icare assists with insurance and care services for people injured in the workplace to improve their quality of life and where possible assists with their return to work. In accordance with regulations all employers must:

- take out a policy with a licensed insurer. Under recent legislation, there has been a strong focus on getting injured employees back to work as soon as possible.
- keep time and wages records, a register of injuries, and complete accident and internal investigation forms, or face substantial financial penalties or six months jail
- notify insurers of significant injuries within 48 hours
- establish, in consultation with the insurer and the employee's doctor, an injury management plan and a return-to-work plan for all injured workers, when fit

workers' compensation a range of benefits to an employee suffering from an injury or disease related to their work. It is also provided to families of injured employees when the injury/disease was caused by, or related to, their work.

for ‘suitable duties’. Failure to display and comply with the plan (which may include employing a rehabilitation coordinator) may result in increased premiums for the employer, or loss of benefits for the employee (if they don’t comply).
- pass on compensation monies to the person entitled as soon as possible. Premiums are closely linked to the number, frequency and size of claims, so it is in the employer’s interest to focus on achieving high standards for WHS.

Employees must notify their employer as soon as possible of an injury or work-related illness. Compensation (financial benefit) is provided to employees (and/or their dependants) suffering injuries or illnesses (including psychological illnesses) substantially developed from their work.

The workers’ compensation system supports injured workers through providing the benefits and assistance needed to recover and return to safe, ongoing work, if that is possible.

Benefits are payable if employees experience total or partial incapacity to perform work; there is a need for medical, hospital or rehabilitation treatment; or if there is permanent or partial loss of use of parts of the body. This includes facial disfigurement and damage to body organs, including bowel injuries. A lump sum payment and weekly payment to dependants are payable if a worker dies as a result of the injury. If an employee on a journey to or from work substantially increases the risk by deviating from or interrupting the journey, benefits may not be payable.

BizFACT

In New South Wales, an employer may be breaking the law if an injured employee is dismissed within six months of being injured or their position offered to a replacement employee within two years of the date of injury without the employee being first advised that she or he might not be reinstated. Full-time injured employees unfit for work receive their award wage for 26 weeks and then a fixed rate until they are fit for some work.

An injured employee may claim compensation, a lump sum payment or sue for common law damages for negligence. Compensation today is subject to thresholds and caps on claims.

There are different types of claims that have specific eligibility criteria:
- medical treatment and rehabilitation expenses
- weekly payments
- psychological injury
- permanent impairment
- work break and journey injuries
- hearing impairment.

When making a claim, medical evidence is required to indicate that a person has suffered from an injury or illness as a result of their employment.

Legal assistance may be provided to support a claim.

Benefits may not be payable if employees have deliberately injured themselves, or are solely responsible for the injury through their wilful misbehaviour or misconduct. Permanent disablement or death in these circumstances does, however, allow the payment of benefits.

Since 2000, legislative amendments have been successively introduced, some in response to a massive blow-out in the value of compensation awarded. For most employees, ‘provisional liability payments’ are made for up to 12 weeks after an injury, and claims for medical expenses compensation up to $10 000 are accepted generally on the basis of verbal or written notification. Formal claims are generally made for matters extending beyond this period or for medical costs greater than $5 000, and should be made within six months of the date of injury or accident, unless the claim relates to serious or permanent injury, death or disablement. In such cases the time limit is extended.

Eligibility for lump sum payments and the calculation of these payments under statutory law is now based on the principle of thresholds for degree of body 'permanent impairment' (loss of use, rather than disability). Through the workers' compensation system, injured workers may be entitled to weekly payments, lump sum payments for permanent impairment (and pain and suffering), payment of medical bills, the provision of legal support to pursue a claim and intensive rehabilitation assistance.

If a worker suffers an injury in the workplace, the employer, injured worker, insurer and treatment provider each have responsibilities to ensure that the injured worker is provided with benefits and assistance to recover and return to work.

Provisional payments enable the insurer to begin paying weekly payments (and medical expenses) to a person while they await the processing of their claim. These payments can include this weekly payment (within 7 days of notification) for a period up to 12 weeks and payment of medical expenses up to $10 000. Weekly payments are structured in such a way that they are consistent with the policy of assisting employees back to work. To facilitate this there is a higher payment in the first 13 weeks and the maximum weekly compensation is capped at $2224. Most workers return to work at this time and it also serves to provide workers with an incentive to return to work.

FIGURE 18.19 Workers' compensation provides payments for employees who are injured or become ill and are unable perform their duties at work.



Workers' payments will cease after 2.5 years, unless there is total incapacity for work. Payments will then cease for those with total incapacity after 5 years, unless there is 20 per cent whole person impairment. Previously, payments continued until the person was able to return to work or until their retirement.

Workers will also receive payments from day one (95 per cent), with a further drop to 80 per cent at 18 weeks (although they retain 95 per cent if working at least 15 hours a week). Payments remain at 80 per cent (or 95 per cent) until they cut out altogether.

The maximum penalty for a false claim under the NSW Workers Compensation Act is $55 000 or 12 months' imprisonment, and for insurers who delay commencing payments penalties up to $50 000 apply.

Common law redress

Employees may take action against an employer when the employer or another employee has been negligent or breached their duty, if the employee has a permanent body impairment of more than 15 per cent and if the injury occurred at least six months prior to the claim. Common law action (known as work injury damages) has been taken for serious diseases such as those caused by asbestos (see the following case study). Such claims are heard in the District or Supreme courts (depending on the size of the claim), and once an employee has successfully achieved a settlement, there are no further payments. If employees are unsuccessful in their actions, they will continue to receive workers' compensation as required under statutory law.

BizFACT

The Workers Compensation Commission is a free service and conducts face-to-face conferences or teleconferences to resolve issues between injured workers and employers.

Legal advice must be considered before seeking damages obtained under common law redress. Employees injured may not claim both damages at common law and lump sum compensation for permanent impairment under statutory law.

SNAPSHOT

Case study: James Hardie Industries — compensation for asbestos victims

The James Hardie Industries asbestos case has been referred to as Australia's largest corporate scandal.

Hardie had been Australia's largest asbestos manufacturer. Asbestos is a building material present in an estimated one-third of homes and buildings built before 1970. Asbestos-related diseases such as mesothelioma and other asbestos-related lung diseases are expected to affect up to 30 000 Australians in the future. The death rate from mesothelioma has risen in recent years, from 1.9 deaths per 100 000 people in 2012, to 2.9 per 100 000 in 2019. The increased death rate in 2019 largely reflects changes in historical exposure to asbestos because the disease takes many years to develop and cause symptoms.

The James Hardie asbestos compensation issue was very controversial.

Two members of Hardie's senior management resigned in 2004, including its CEO, under pressure from a commission of inquiry, which found it had not fully told the truth to the New South Wales Supreme Court, and its management had been less than honest with the Australian Securities Exchange and the community on the issue of asbestos. It had not put enough money into a compensation fund to compensate future claims, and its chief financial officer was prepared to be deceitful where asbestos was concerned. Claims alleged that Hardie management had deliberately restructured operations to a Netherlands base to avoid their obligations for compensation of victims of asbestos. The two members of senior management who resigned are alleged to have received executive payouts totalling $10 million.

Under pressure from victims' lawyers, the ACTU and other groups, James Hardie signed a landmark agreement in December 2004, providing asbestos sufferers with compensation valued at over $4 billion, over a 40-year period.

James Hardie's then CEO, Meredith Hellicar, hailed the agreement as a 'compassionate' outcome, which is 'fair and equitable for all parties' and she hoped it 'convinces the Australian community that we are seriously committed to that responsibility'. The company placed payments into a special purpose fund for current and future victims, at 35 per cent of its free cash flow. A key feature of the agreement is recognition by all parties that ongoing James Hardie viability is essential to long-term benefits for its victims.

When this agreement was later shown to leave the victims underfunded by around $1 billion, further action was taken against the non-executive directors by ASIC. The action failed in the NSW Court of Appeal in December 2010.

BizFACT

The 'average' Australian with mesothelioma is male, around 75 years of age, exposed to asbestos in occupational and non-occupational settings and lives for around 11 months after diagnosis.

Australia's consumption of asbestos peaked at around 700 000 metric tonnes between 1970 and 1979. Asbestos was both mined and imported, and used in the construction industry due to its durability and fire and chemical resistance.

The import and use of asbestos and asbestos-containing products is prohibited in Australia; however a large amount of asbestos still remains in the built environment.

18.4.3 Anti-discrimination

Discrimination occurs when a policy or a practice disadvantages a person or a group because of a personal characteristic that is irrelevant to the performance of the work. It includes harassment (offending behaviour or intimidation) and vilification (a public act which is discriminatory and incites hatred).

Anti-discrimination legislation has been enacted to protect employees from direct and indirect discrimination (see figure 18.20) in recruitment, selection, training, promotion, remuneration, termination and opportunities to access any other employment benefits or practices. To prevent discrimination and to avoid large fines, employers need to:

- comply with legislation
- audit all policies and practices to ensure they do not discriminate.

Employers and managers working in human resources need to be familiar with the following legislation:

- *Human Rights and Equal Opportunity Commission Act 1986 (Cwlth)*
- *Affirmative Action (Equal Employment Opportunity for Women) Act 1986 (Cwlth)*
- *Sex Discrimination Act 1984 (Cwlth) and the Anti-Discrimination Act 1977 (NSW).*

The agencies available to support the legislation are the Australian Human Rights Commission, the Workplace Gender Equality Agency and the Anti-Discrimination Board (NSW).

Under discrimination laws it is illegal to take adverse action in employment on the grounds of a person's:

- race, sex, sexual preference, colour or age
- physical or mental disability
- religious faith or political opinion
- social origin or national extraction
- marital status and carer responsibilities
- pregnancy or potential pregnancy.

discrimination when a policy or a practice disadvantages a person or a group of people because of a personal characteristic that is irrelevant to the performance of the work

BizFACT

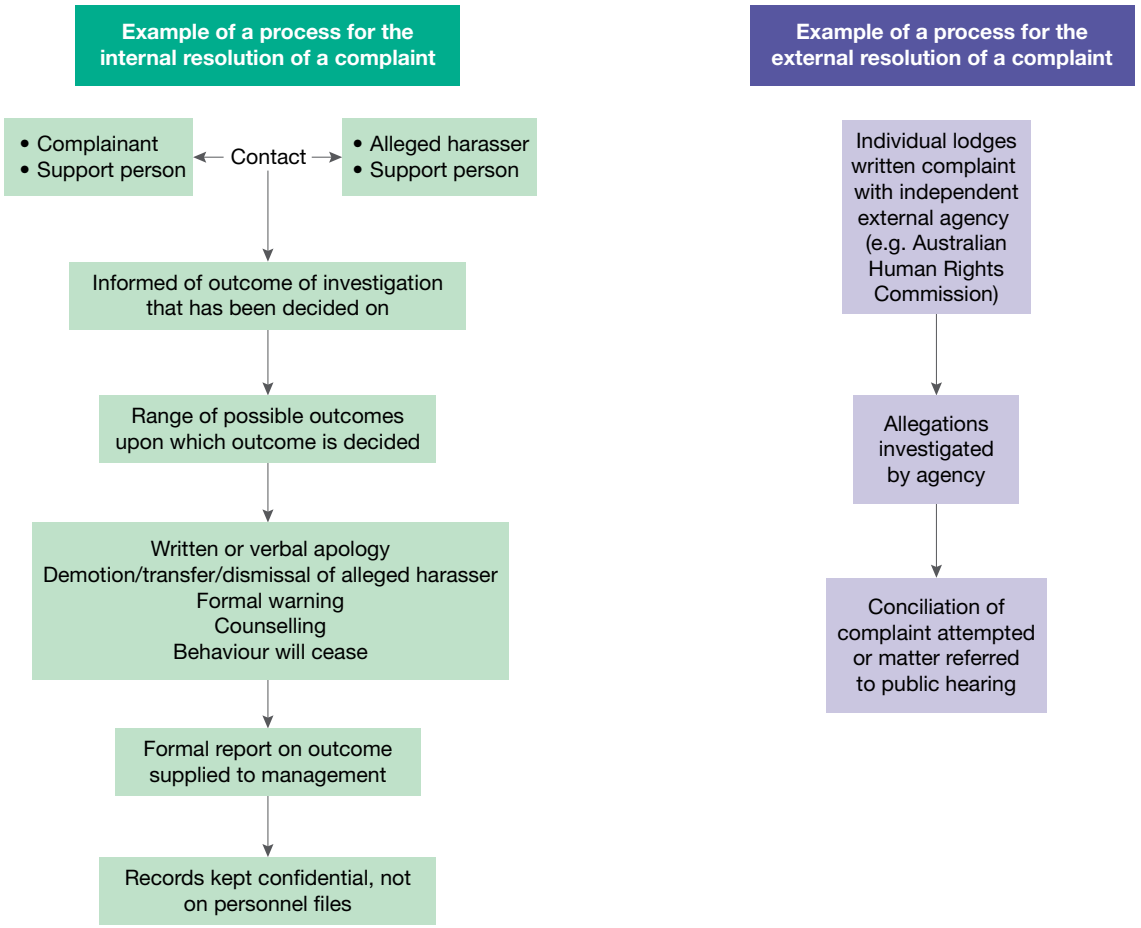
In 2014, the Fair Work Ombudsman was successful in its first court case relating to discrimination on the basis of age. The case involved a Brisbane restaurant employee who had been dismissed upon turning 65. The employer was fined $20 790.

FIGURE 18.20 Direct and indirect discrimination



Protection has been further enhanced under the Fair Work Act. It allows freedom of association for members or non-members of a union and protection in a wider range of employment aspects. This may include dismissing an employee, damaging their ability to do their job, changing an employee's job to their disadvantage, treating one employee differently to other employees, refusing to employ a potential employee, and not offering a potential employee all the terms and conditions normally in a job. People who suffer discrimination may take a range of actions internally, formally or informally (see figure 18.21).

FIGURE 18.21 Options available in resolving a complaint of discrimination



Strategies used increasingly by businesses to eliminate discrimination include:

- committing to a workplace free from discrimination
- writing and communicating policies to prevent discrimination and harassment, including a code of conduct
- making sure all policies and procedures are clearly documented and accessible to employees, offer informal and formal options, and guarantee timely responses, confidentiality and objectivity
- training managers and staff in cultural diversity issues and ways to prevent or deal with discrimination and harassment, primarily using face-to-face and interactive training programs
- appointing a grievance officer and specifying grievance procedures involving issues such as sexual/racial harassment
- regularly evaluating record keeping, implementation and effectiveness of policies, workplace culture and action taken to resolve complaints.

BizFACT

Typical outcomes from a complaint may include:

- a formal apology
- counselling
- official warnings
- mediation or conciliation
- disciplinary action.

Outcomes will be influenced by the evidence, previous incidents, the wishes of the person experiencing discrimination, and the severity and frequency of the discrimination or harassment.

All employers are required to take reasonable steps to eliminate discrimination. Whether reasonable steps have been taken is considered on a case-by-case basis, as a large corporation is clearly capable of a different level of action than a small business. Employer associations and anti-discrimination agencies can help businesses develop a strategy that ensures consistency and fairness in handling of complaints.

BizFACT

An employer may be held liable if any of the following discriminates against or harasses an employee: an employee or a group of employees, agents, contract worker, partner, director, supervisor, manager or trade union representative.

SNAPSHOT

Case study: Report reveals high levels of workplace inequality

On 5 March 2018, the Sydney University Australian Women's Working Futures Project released its first report. The project team surveyed over 2000 working women aged under 40, 500 working men aged under 40, and 50 Indigenous working women aged under 40. They also carried out a series of focus group interviews with working women under 40. Their report indicates that inequality for women in the workplace remains a serious issue for large numbers of working women.

When asked about the most important aspects of a job, 80 per cent of women surveyed said that having a job where they would be treated with respect was of greatest value. This finding suggests that a large percentage of women currently believe they are not treated with respect at work. This aspect of the workplace was considered more important than the level of pay or workplace flexibility. In reality, only 68 per cent felt they were genuinely treated with respect, while only 48 per cent felt they received adequate recognition at work and 56 per cent said that they felt valued at work.

Less than a third of women surveyed (31 per cent) believed that men and women were treated equally at work, and only 53 per cent expected gender equality to improve over the next decade. Ten per cent of women said they have experienced sexual harassment in the workplace, a finding described as 'shocking' by one of the researchers, Dr Elizabeth Hill of Sydney University. In addition to issues of direct sexual harassment, many women in focus groups pointed to other forms of gender-based discrimination in the workplace, such as being targeted for their physical appearance.

Forty per cent of the women surveyed had at least one child, and over 50 per cent said they expected to have a child in the future. However, many recognised that they faced a serious conflict when choosing between furthering their career and having children. Many women said that they were either delaying having children or choosing not to have a family in order to safeguard their careers. It was clear that many women felt that they had to choose between having children and having a successful career and were concerned at the apparent barriers to them doing both.

SNAPSHOT

Case study: Age discrimination in the workplace

Almost a third of Australians perceived some form of age-related discrimination while employed or looking for work in the last 12 months — starting as early as 45 years of age, our study finds.



We conducted a national survey of 2100 men and women aged 45 years and over, and 100 telephone interviews. The most common form of perceived discrimination was negative assumptions about older workers' skills, learning abilities or cognition.

Survey participants also reported limited or no opportunities for promotion or training, working in an organisation that undervalued them and difficulty securing work due to age.

Our findings align with previous research from the Australian Human Rights Commission where 27 per cent of Australians aged 50 years and over had recent experience of age-based discrimination in the workplace. In this survey the most common forms were limited employment, promotion or training opportunities and perceptions that older people have outdated skills or are too slow to learn new things.

Older adults in our study described a subtle pressure from their colleagues and management to stop working in order to 'make room for the younger generation'. This was regardless of their experience, enduring capabilities or working preferences.

Workers also faced patronising attitudes, where employers or colleagues assumed they would struggle to pick up new technology or work systems quickly, due to their age. Some survey participants felt they were not afforded the same promotional or training opportunities as their younger colleagues.

Experiences differed for men and women in our survey. Men were more likely to suggest discrimination based on assumptions about their physical abilities or working pace, and women reported the organisation they worked for undervaluing older workers as a group.

To avoid discrimination interviewees reported using strategies such as minimising health conditions, concealing their age or maintaining a 'youthful' appearance.

Although there has been some research into industry specific experiences of age discrimination, there are limited comparisons in research of prevalence and type of discrimination between industries.

Our data indicates that age-related discrimination traverses all industries in worrying proportions. Industries where age discrimination was particularly common included construction, administrative services, education, manufacturing, essential services, information technology and professional service industries.

Hiring and firing of older workers

Over two-thirds of retirees in our study, who had experienced age-related discrimination, attributed their retirement to involuntary factors such as 'having no choice', redundancy or dismissal. Negative experiences at work (with a colleague, management or client) or dissatisfaction with organisational changes were often the trigger events for retirement.

Older job seekers reported being candidly or surreptitiously rejected through recruitment processes on the basis of age alone. Education, training and a steady working history were not guaranteed to help study participants in their search for employment.

Some interviewees had found it necessary to accept work for which they felt overqualified. Job seeker services in particular were considered ill-equipped to assist older, highly experienced and often well-educated adults.

These findings are in line with similar research in which study participants interpreted suggestions from potential employees that they were over qualified or experienced for a role, to mean they were 'too old'.

Our interviewees believed that younger managers can feel intimidated by older workers. This may be based on concerns regarding an older employee's ability to take instruction from somebody younger, learn new work methods and technologies or readily adopt change.

Why we should fight age discrimination

Beyond the moral and ethical issues of how older adults are treated, the experiences recorded in our study can have tangible implications for individuals and employers.

The government is trying to reduce dependency on the aged care pension by encouraging workers to stay in the workforce longer and accumulate sufficient superannuation (and other assets). Employment in high quality work can support and protect the health of men and women as they age.

But adults who feel devalued in their workplace, or unable to find suitable employment, are more likely to enter retirement earlier than anticipated and less inclined to re-enter the workforce.

Our survey results also suggest that people experiencing work-related ageism tend to report poorer health, lower household incomes and lower total superannuation fund balances, than those who have not had this experience.

Mature aged workers bring with them a range of favourable characteristics such as stability, reliability, loyalty, experience, wisdom and maturity. One way to tackle work related ageism is to firstly address negative perceptions regarding the competency of older workers.

This may be best addressed by employment services and human resource staff who are often on the front line of helping these workers find suitable employment. These workers can be skilled to respond to the needs of mature age job seekers. The introduction or reinforcement of policies supporting diversity in the workplace is another important step to support older worker participation.

Source: Justine Irving, 'Age discrimination in the workplace happening to people as young as 45: study', *The Conversation*, 26 April 2017.

18.4.4 Equal employment opportunity

Equal employment opportunity (EEO) refers to equitable policies and practices in recruitment, selection, training and promotion. EEO ensures that the best person for the job is chosen, the business gains the person with skills and abilities most appropriate to its needs, and a more positive work environment is promoted.

The level of equity in a business is reflected in the extent to which women and minority groups have access to different occupations and positions within the business. It is also reflected in the grievances expressed or legal action undertaken on the grounds of discrimination or sex-based harassment.

Employers with more than 100 employees, and all higher education institutions, are obliged to develop an **affirmative action** program in consultation with employees, and to provide a progress report to the Workplace Gender Equality Agency (WGEA).

The *Equal Opportunity for Women in the Workplace Act 1999* has been replaced by the *Workplace Gender Equality Act 2012* and aims to promote and improve gender equality and outcomes for both women and men in the workplace.

WGEA was created to reflect this new focus and achieves this by:

- advising and assisting employers to promote gender equality in the workplace
- reviewing compliance with the legislation
- providing research findings and educational programs to improve gender equality outcomes
- establishing a workplace profile and analysing the issues in the specific workplace
- reporting on the actions taken by the employer to address priority issues
- describing action plans for the following period and evaluating the strategies used.

Businesses are then assessed as complying or not complying with requirements.

equal employment opportunity (EEO) refers to equitable policies and practices in recruitment, selection, training and promotion

affirmative action measures taken to eliminate direct and indirect discrimination, and for implementing positive steps to overcome the current and historical causes of lack of equal employment opportunity for women

BizFACT

Firms failing to lodge a report or submitting a report that does not comply with the Act may be publicly named in a report tabled in parliament that also receives significant media publicity. They are also excluded from government contracts and industry assistance grants.

The aim of the program is to remove discriminatory employment barriers and take action to promote equal opportunity for women in the workplace.

Businesses also need to comply with the discrimination provisions in the Fair Work Act, which includes broader provisions relating to most areas of employment. The Fair Work Commission must now take action (including making orders) to ensure that no existing or proposed award or enterprise agreement discriminates on a wide variety of grounds.

WGEA recommends that businesses focus on six areas to improve equity within their business: recruitment, promotion and separation; access to all occupations and areas; equitable total remuneration; training and career development; work and life balance; sexual harassment and working relationships.

The aim of gender equality in the workplace is to achieve equal outcomes for both women and men. In order to achieve this, workplaces:

- must provide equal pay and conditions for women and men for work of equal or similar value
- should remove anything that prevents the full participation of women in the workforce
- must facilitate access to all jobs and industries, including leadership roles for women and men
- must eliminate discrimination on the basis of gender, particularly in relation to personal responsibilities including family and caring for both women and men.

BizFACT

Most gender discrimination happens in the recruitment stage, according to WGEA.

Gender equality in the workplace is important as it encourages stronger applicants, especially women, entices more highly educated (often female) applicants, reduces costs associated with staff turnover, and encourages varied perspectives and views which results in stronger business performance, both internally and nationally.

SNAPSHOT

Case study: Chevron and the advantages of a diverse, culturally competent workforce for a global business



The US multinational energy company Chevron has operated since the end of the nineteenth century. In recent years it has been recognised for its commitment to the work health and safety, human rights, development and diversity of its workforce. Its Australian operation is a wholly owned subsidiary, Chevron Australia Pty Ltd. It, like its parent company, understands its role as an ethical employer and invests in community programs, often in the area of the country where its projects are located.

It is particularly committed to pursuing programs that provide for a diverse and culturally competent workforce that it attributes to:

- recruitment and outreach programs that target underrepresented groups such as women and indigenous people
- diversity councils, employee networks and personnel development committees
- an emphasis on diversity of thought, education, origin, gender, skills and experience.

A recent initiative has been its education programs that aim to increase the number of women in engineering roles in Western Australia. The Women in Engineering Program seeks to provide women with the skills and confidence to pursue engineering careers in the oil and gas industries and its Women in Future Leadership Program aims to equip women with basic employment skills relevant to the energy industry. The programs provide female students with an environment where they can gain insights into engineering from a female perspective with access to mentors and successful female engineers. Each program attempts to give insight into how to break down barriers that often prevent women from choosing a career in engineering, including options for part-time work that support women with existing family responsibilities.

on Resources

Weblink Australian Human Rights Commission

KEY IDEAS

- Work health and safety (WHS) legislation is in the process of being made uniform around Australia to improve business productivity.
- The relevant act in New South Wales is the *Work Health and Safety Act 2011*.
- Employers must provide a safe system of work, and ensure employees are trained and supervised in their work.
- All employers must take out workers' compensation insurance.
- Employees are also responsible for taking reasonable care for the health and safety of others.
- In New South Wales three organisations — SafeWork NSW, the State Insurance Regulatory Authority (SIRA) and Insurance and Care NSW (icare) — are the organisations responsible for WHS, workers' compensation, and insurance and care services for injured workers respectively.
- Common law redress can be sought where the employer or another employee has been negligent or breached their duty, leading to serious injury or death.
- Discrimination occurs when a policy or a practice disadvantages a person at work because of a personal characteristic that is irrelevant to the performance of their work.
- All employers must implement anti-discrimination legislation, as well as audit all policies and practices to avoid large fines, legal orders and damages, and loss of reputation.
- Anti-discrimination legislation is supported by government agencies, including the Australian Human Rights Commission, the Workplace Gender Equality Agency and the Anti-Discrimination Board (NSW).
- Equal employment opportunity refers to equitable policies and practices in recruitment, selection, training and promotion.
- Affirmative action refers to measures taken to eliminate direct and indirect discrimination and for implementing positive steps to overcome the current and historical causes that result in a lack of equal employment opportunity for women.
- There is significant gender inequity in management roles in Australia.
- All employers with more than 100 employees, and all higher education authorities, must report annually, unless exempted, on equal opportunity programs they develop in consultation with employees and progress achieved.
- Businesses that do not comply are likely to be named in parliament, and excluded from government contracts and industry assistance grants.
- Strategies commonly used to resolve a complaint of discrimination include apology, counselling, official warning, mediation, conciliation or disciplinary action.
- Developing a code of practice and making equal opportunity awareness a criterion in promotion and performance appraisal are two of the practical strategies that can be used to improve affirmative action and gender equity.

18.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

18.4 Quick quiz on	18.4 Exercise	18.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 9, 10, 12, 14, 15, 17, 20, 21, 22, 23, 26, 27, 28, 29, 30, 31, 32, 33, 34, 37, 38, 39	4, 5, 6, 7, 8, 11, 13, 16, 18, 19, 24, 25, 35, 40, 41	3, 36, 42, 43

18.4 Exercise

Revision

1. Look at figure 18.18 and **identify** some safety concerns associated with the workplace.
2. **What** are the WHS risks faced by people in the following jobs: auto mechanic, teacher, ship refueller, scientist, process worker in a textile factory, hairdresser, miner, bank officer, police officer, truck driver, airline pilot?
3. **Analyse** the most common factors contributing to accidents at work.
4. **Construct** a table listing employer and employee responsibilities for workplace safety.
5. Management may use a range of strategies to evaluate the effectiveness of WHS programs; for example, safety tours of a plant, reviewing specific aspects on a random basis, risk assessments for changes in the workplace and specific job safety analysis. **Propose** some additional strategies that you would use.
6. The industries in which accidents and injuries are most likely to occur are manufacturing, transport and storage, agriculture, forestry and fishing. **Investigate** safety risks in these industries.
7. Male employees who are either young or aged between 45 and 49 are more likely to experience injuries and accidents at work. **Propose** reasons for the high number of accidents within these two groups.
8. Substance abuse is becoming a problem in many workplaces in which employees experience stress. **Discuss** whether employers have the right to drug test employees.
9. **Identify** the organisation responsible for managing workers' compensation.
10. **Identify** the cost of failing to take out workers' compensation if you are an employer.
11. **Why** were legal limits on compensation introduced from 2000?
12. **Describe** the main ways in which injured employees are assisted today under workers' compensation.
13. **How** can an employee seek common law redress?
14. **What** is meant by the term 'discrimination'?
15. **Identify** the grounds under which a discrimination complaint may be made.
16. Look at figure 18.20 and **distinguish** between direct and indirect discrimination.
17. **Recall** a range of possible outcomes for a discrimination complaint.
18. **Why** are most employers keen to avoid such complaints?
19. Select the strategy you consider to be the most effective in eliminating discrimination in business (see section 18.4.3). **Justify** your selection.
20. **Outline** the consequences for employers who do not comply with the legislation.

Read the'Woolworths— health and safety' case study and answer questions 21 to 23.

21. **Where** does Woolworths refer to its policy on worker health and safety?
22. **Outline** the concept of 'Destination Zero'.
23. **What** are some examples of a 'safety first' approach at Woolworths?

Read the 'James Hardie Industries — compensation for asbestos victims' case study and answer questions 24 to 26.

24. **Why** did management behave in such an unethical manner for so long?
25. Do you think the Hardie executives who resigned as a result of the commission of inquiry into their management practices should have been paid $10 million? **Justify** your response.
26. **What** are the reasons for the capping of annual payments at 35 per cent of the company's free cash flow?

Read the 'Report reveals high levels of workplace inequality' case study and answer questions 27 to 29.

27. **Which** aspect of the workplace did the largest percentage of women feel was most important?
28. **Why** did Dr Elizabeth Hill describe the figures on sexual harassment as 'shocking'?
29. Other than sexual harassment, **identify** another form of discrimination reported by women in the survey.

Read the 'Age discrimination in the workplace' case study and answer questions 30 to 36.

30. **What** percentage of Australians have experienced age-related discrimination?
31. **List** the common forms of age-related discrimination experienced by those interviewed.
32. **How** does the age-related discrimination identified in this case study agree with the research carried out by the Australian Human Rights Commission?
33. **Outline** how the experiences of men and women were different in respect to age-related discrimination.
34. **List** the industries where age-related discrimination is of greater concern.
35. **Explain** the link between retirement and age-related discrimination.
36. **Analyse** the costs and benefits to society of having an older workforce.

Read the 'Chevron and the advantages of a diverse, culturally competent workforce for a global business' case study and answer questions 37 to 39.

37. **What** are Chevron's main business interests?
38. **List** reasons for Chevron's diverse workforce.
39. **Identify** its recent education programs and their objectives.

Extension

40. A high-volume, internet-based financial services business operates 24 hours a day. Some of its 100 staff work a rotating night shift, while others take turns to be 'on call'. The majority of staff operate from 7.30 am to 7.00 pm, although official working hours are 9 am to 5 pm.
    a. Using this example, identify the factors that could lead to high levels of stress.
    b. **Discuss** how high levels of staff stress could affect the business.
    c. **Explain** why substance abuse could be a problem in this business.
41. Tamara has recently applied for a promotion. She informs her manager that she is pregnant and will be taking parental leave in three months. Tamara fails in her application for promotion. Although she is highly qualified for the job, Tamara's manager advises her that she was not promoted because she will be able to do the job for only a short time before she goes on parental leave.
    Tamara comes to see you, an adviser at the Australian Human Rights Commission. **Explain** the advice you would give Tamara. To help, use information available from the **Australian Human Rights Commission** website.
42. **Evaluate** the legal requirement for large employers to provide a regular equal opportunity report.
43. **Create** a script in which you support a group of women experiencing sexual discrimination at work. Propose strategies to resolve the problem.

18.4 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q12

A NSW employer develops a return to work plan in consultation with an insurer and an injured employee.

Which legislation requires the employer to undertake this action?

A. *Fair Work Act 2009* (Cth)
B. *Workers Compensation Act 1987* (NSW)
C. *Work Health and Safety Act 2011* (NSW)
D. *Australian Human Rights Commission Act 1986* (Cth)

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q5

An employee is treated unfairly because she is pregnant.

What legislation prohibits this behaviour?

A. *Trade Practices Act 1974* (Cth)
B. *Affirmative Action (Equal Employment Opportunity for Women) Act 1986* (Cth)
C. *Sex Discrimination Act 1984* (Cth)
D. *Competition and Consumer Act 2010* (Cth)

Question 3 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q18

Hannah is a permanent employee at XYZ Ltd who has been injured in a workplace accident.

Who is ultimately responsible for paying Hannah's medical expenses for this injury?

A. Hannah
B. Medicare
C. WorkCover NSW
D. XYZ Ltd's insurance company

Question 4 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q16

Riley has 150 employees. She is preparing a report outlining her company's plans to ensure women have better access to senior positions.

Which workplace issue is Riley addressing?

A. Anti-discrimination
B. Equal employment opportunity
C. Occupational health and safety
D. Workers compensation

Question 5 (1 mark)

Source: HSC 2011 Business Studies Exam, Section I, Q18

Under what legal framework is it the responsibility of employees to use care and skill in performing work activities?

A. Common law
B. *Fair Work Act 2009* (Cth)
C. *Workplace Relations Act 1996* (Cth)
D. The National Employment Standards

More exam questions are available in your learnON title.

18.5 Economic, social, technological and ethical influences

SYLLABUS LINK In this subtopic you will learn about:

- how economic influences affect human resource management
- how technological influences affect human resource management
- how social influences such as changing work patterns and living standards affect human resource management
- how ethics and corporate social responsibility affect human resource management and learn to explain how businesses exhibit corporate social responsibility in the management of human resources.

***Source**: Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

18.5.1 Economic influences

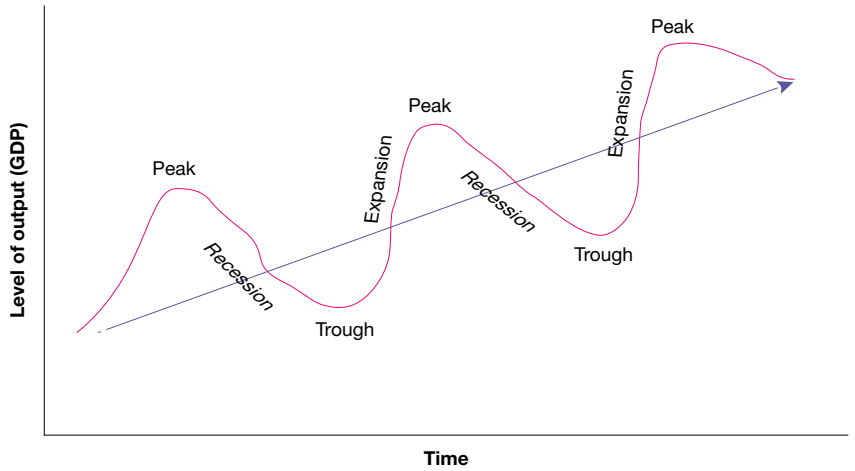
The economic cycle

The demand for labour (employees) is determined by the demand for goods and services within the economy. If labour shortages develop during periods of economic growth, such as during a peak or during the expansion phase in the business cycle, shown in figure 18.22, employers compete for employees by offering higher wages. Unions may use their stronger bargaining power to demand significant wage increases, which may then put upward pressure on costs and prices, creating inflation. During downturns in the economic cycle, as indicated in a trough, or the recession phase of the business cycle, the demand for goods and services falls. Businesses are forced to reduce the size of their workforce (downsize) and limit their capacity to provide significant wage increases.

BizFACT

Subdued wage growth has plagued the Australian economy for the past two years. Low pay increases persist and growth is at its slowest since the end of the twentieth century. Among reasons for the sluggish growth are the need for Australia's economy to become more competitive, technological change, higher rates of casual employment, global trends and existing spare capacity in some sectors.

FIGURE 18.22 The business cycle



SNAPSHOT

Case study: Open letter from 265 Australian economists — don't sacrifice health for 'the economy'

A growing chorus of Australian commentators has called for social distancing measures to be eased or radically curtailed.

Some have claimed the lives saved by the lockdowns are not worth the damage they are causing to the economy.

Others have claimed the case for easing is strengthened by the fact many of the hardest hit by COVID-19 are elderly or suffering from other conditions.

Some might expect economists, of all people, to endorse this approach.

But as economists we categorically reject these views, and we believe they do not represent the majority of our profession.

We believe a callous indifference to life is morally objectionable, and that it would be a mistake to expect a premature loosening of restrictions to be beneficial to the economy and jobs, given the rapid rate of contagion.

It is wishful thinking to believe we face a choice between a buoyant economy without social distancing and a deep recession with social distancing.

In a world with COVID-19, there are no good choices.

The best we can do is limit the spread of COVID-19 as much as practicable and rely on the strength of the government's balance sheet to cushion the impact on the workers and businesses hardest hit.

Our success to date is a direct result of the measures taken, but we cannot afford to be complacent.

We recognise there are trade-offs on some margins, but we urge the government to work closely with public health experts to carefully determine at what time, in what ways, and in which sectors, to begin lifting restrictions.

There should be no doubt the cost of getting this wrong is very high.

Open Letter from Australian Economists, 19 April 2020

Dear Prime Minister and Members of the National Cabinet,

The undersigned economists have witnessed and participated in the public debate about when to relax social-distancing measures in Australia. Some commentators have expressed the view there is a trade-off between the public health and economic aspects of the crisis. We, as economists, believe this is a false distinction.

We cannot have a functioning economy unless we first comprehensively address the public health crisis. The measures put in place in Australia, at the border and within the states and territories, have reduced the number of new infections. This has put Australia in an enviable position compared to other countries, and we must not squander that success.

We recognise the measures taken to date have come at a cost to economic activity and jobs, but believe these are far outweighed by the lives saved and the avoided economic damage due to an unmitigated contagion. We believe strong fiscal measures are a much better way to offset these economic costs than prematurely loosening restrictions.

As has been foreshadowed in your public remarks, our borders will need to remain under tight control for an extended period. It is vital to keep social-distancing measures in place until the number of infections is very low, our testing capacity is expanded well beyond its already comparatively high level, and widespread contact tracing is available.

A second-wave outbreak would be extremely damaging to the economy, in addition to involving tragic and unnecessary loss of life.

Source: Steven Hamilton, Bruce Preston, Chris Edmond & Richard Holden, 'Open letter from 265 Australian economists don't sacrifice health for 'the economy'', *The Conversation*, 26 April 2020.

Structural change

Structural change occurring in the economy has led to a rapid employment growth in the services sector, which accounts for 86 per cent of total employment.

Employment is growing in property, business, retailing, trades, tourism, educational services, hospitality, and community and personal services. Some of these industries have been traditionally dominated by women. As each sector grows, recruitment, selection and remuneration become important industrial issues. With an ageing population, flexible staffing arrangements, retention and mentoring increase in importance. Effective training and staff empowerment are also critical to business success in such customer service-based industries.

structural change a change in the nature and pattern of production of goods and services within an economy. This includes a significant growth in the level of services in an economy compared to other sectors.

BizFACT

'New-collar workers' are technologically proficient, interpret data, understand trends, and know how to initiate technological improvements rather than just having traditional computer skills.

In the middle of the 20th century, manufacturing accounted for about 30 per cent of gross domestic product and one-third of the workforce. A wide variety of goods were produced including cars, footwear, clothes even washing machines.

In the post-World War II rebuild of global economies, manufacturing in Australia was supported by tariff walls encouraging consumers to buy the local goods. This protection of Australia's manufacturing businesses supported significant growth in the 1950s and 1980s and in some cases such as the car industry tariff levels reached 200 per cent. Governments decided that this ongoing protection was unsustainable and that the removal of protection would result in a more competitive manufacturing sector where only the best survived.

FIGURE 18.23 As the economy undergoes structural change, opportunities in some industries are created, leading to job creation. For example, tourism is a rapidly growing industry. Unfortunately, jobs are lost in industries that can no longer compete.



In 2020 the manufacturing sector accounts for only 6 per cent of gross domestic product and about 1 million jobs. The COVID-19 pandemic has exposed Australia's small manufacturing sector and disrupted global supply chains especially in much needed medical supplies. Local businesses have been faced with a shortage of goods often outsourced globally. An uncertain trade relationship with China has complicated matters further.

The government has appointed an advisory panel identifying potential growth areas in the manufacturing sector in a post-COVID-19 world. Possible industries include food, defence, mining, medical, engineering, space and renewable energy.

The science around global climate change has meant that alternative energy sources are needed and Australia has them in abundance — wind, sun and land. These natural resources present a once-in-a-lifetime opportunity to re-establish manufacturing but may mean that employment will need to be reconsidered. The most efficient factories run 24/7 but workers are compensated with higher pay rates.

For the wider economy, increasing Australia's manufacturing sector could add $180 billion a year in new output, add to gross domestic product by as much as $50 billion and create more than 650 000 direct and indirect jobs.

Globalisation

Globalisation of business has increased the level of international competition. Australian businesses compete every day with 'local' subsidiaries of transnational corporations. Many restructure, outsource non-core functions or subcontract production in order to compete effectively. Corporations, both domestic and transnational, are increasingly prepared to relocate production units in other cities, states or countries where dispute levels, labour and regulatory costs are much lower. In such an environment, there is an increased need to attract and retain motivated and effective core staff, and make continuous improvements in productivity, costs, innovation, quality and customer service. Enterprise bargaining has allowed many employers to trade-off restrictive/inefficient work practices for wage increases in industrial agreements. Business profitability has improved significantly.

Training in the management of multicultural workforces, with differing approaches to power, authority and the role of groups/individuals, is increasing with the globalisation of business.

There is also an increasing role for international organisations, such as the International Labour Organization and trade blocs (for example, the European Union and the World Trade Organization), to promote trade between countries that adhere to social justice principles (such as bans on child labour).

BizFACT

Tourism jobs declined between December 2019 (748 200 jobs) and November 2020 (611 700) due to the combined effect of bushfires and COVID-19.

The higher education sector has been similarly affected, with an estimated 21 000 job losses due to fewer international students because of Australia's border closures aimed at minimising the transmission of COVID-19.

18.5.2 Technological influences

As outlined in topic 1, technological change is the major source of improvement in productivity, communication and competition between businesses. It is causing the nature of production and services to change, and new jobs to be created, while others are made redundant. Many businesses are re-engineering and restructuring as networks, often offshore, make increasing use of 'virtual teams' using video technology. A suite of electronic communications options allow firms to operate 'anywhere, anytime' and to harness staff through telecommuting. This has provided a major opportunity for businesses to access employees at home, increasingly those in developing nations who would otherwise be disadvantaged through traffic congestion or distance from the business office. Use of new communications technology does increase the need for ongoing training programs and new protocols to ensure that work–life balance is maintained in an environment in which society often expects people to be 'always on call'.

FIGURE 18.24 Virtual team meetings are a feature of the new 'workplace' and a sign of how technology impacts human resource management.



BizFACT

Approximately 6 million Australians will require training in digital literacy by 2025 and at least 100 000 IT workers by 2022 to compete globally.

SNAPSHOT

Case study: Zoom meetings help marginalised staff feel included — we should keep having them even after offices reopen

Before the lockdown studies show that remote workers could often feel professionally and socially isolated.

The physical distance between remote workers and their on-site colleagues meant they missed out on learning opportunities. Those working remotely would also frequently miss casual conversations and collaborations in the workplace, formal and informal team meetings, and in-person social events, such as after-work drinks. Remote workers would often feel excluded from the team.

But when the pandemic struck many people usually based in the office were forced to work from home too. Businesses had to use technology in new and imaginative ways to allow teams to collaborate and perform work-related tasks. Our research suggests that this enforced working from home put remote workers on an equal footing with their office-working colleagues. We can learn from this to make sure remote workers don't feel excluded in the future.

How teams responded

In our study, we interviewed 29 knowledge workers — that is, people who work with information in a white-collar setting — about their experiences of team collaboration during the pandemic. Our participants came from countries all over the world, including New Zealand, Australia, the United Kingdom, Sweden, Denmark, Germany and Switzerland.

We found that during enforced working from home, digital collaboration platforms such as Zoom, Skype or Microsoft Teams operated as double-edged swords. They simultaneously served as an 'equaliser' by allowing greater collaboration with previously remote workers, but also created challenges.

With all knowledge workers operating remotely, digital platforms became the only channel for communicating and collaborating. To reduce the effect of the lack of in-person conversations and meetings, some teams started to hold frequent online check-ins and regular formal meetings, virtual coffee catch-ups, after-work drinks, and digital networking events with other colleagues and associates.

Many remote workers who had previously missed out on physical after-work drinks, catch-ups and meetings could join their colleagues virtually instead. They felt much more included and part of the team.

As one of our participants said:

'This has definitely removed some of the barriers between our offices in NZ, AUS and UK. We have a weekly social gathering on Friday afternoons, and this sometimes goes on for hours. I think the big difference from before is that people are already at home and don't need to worry about being late home from the office on a Friday.'

Being online also allowed employees working in different branches or countries to socialise, potentially leading to new opportunities for collaboration. This led to a new sense of equality and inclusion between habitual remote workers and their usually office-based counterparts.

One of our participants stated:

'We're speaking more frequently than we ever did before. Which I'm finding better just because I can communicate more regularly, and so I feel more connected than I ever did before when I used to go up once a month or once every two months.'

However, our study also revealed some challenges. Some participants reported that the virtual check-ins and meetings were too frequent and unnecessary. They can be especially challenging for those who need to take care of other domestic duties. They can also lead to virtual meeting fatigue and potentially promote longer working hours, upsetting work–life balance.

We also found that employees were struggling with group conversations due to the limitations of the digital platforms. In an online meeting, it's impossible for multiple people to speak at the same time. Virtual networking events can also be quite challenging as people cannot mix and mingle — everyone must listen to one person, making the event quite rigid.

Three lessons for the future

With lockdown easing, employees are gradually going back to the office. As they return, we must apply the evidence that we've found to create a more constructive and productive work environment for everyone.

It's important that we don't go back to square one. So, here are three changes we think should be made.

1. Digital platforms can and should be used to allow remote workers to join formal and informal meetings taking place in offices. Meeting facilitators also need to ensure that remote workers can contribute to the discussion that is being had.
2. Established collaboration habits — such as daily check-ins — could remain, even when back in the office. They create transparency, help distribute tasks and allow remote workers to be part of daily conversations.
3. In the wake of the pandemic, we're likely to see the introduction of more flexible working arrangements, leading to an increase in remote workers. In response to this, organisations should create a culture of inclusion — meaning that employers and team members should be mindful of challenges that remote workers face (such as threats to work-life balance, feelings of exclusion and missed opportunities). Businesses should take effective actions to tackle these issues by offering equal opportunities to remote workers through virtual platforms as far as is possible.

Applying these lessons would open up the opportunity for staff to make the best of both worlds — using the home office for focused, uninterrupted work (if the private circumstances allow) and accessing the corporate office for collaborating, innovating and socialising.

Source: Brad McKenna, Lena Waizenegger & Wenjie Cai, 'Zoom meetings help marginalised staff feel included — we should keep having them even after offices reopen', *The Conversation*, 12 August 2020.

BizFACT

The 2016–17 NSW Intergenerational Report (*Future State NSW 2056*) provides insight into how the state may look 40 years from now, with respect to demographic, workforce and housing trends. It identifies issues that the government of the day should consider in order to ensure the highest possible living standards for its citizens.

Its key findings in respect to influences on human resources were:

- growing services sector
- more flexible work patterns including outsourcing
- portfolio careers, telecommuting and remote working
- increased work opportunities beyond the traditional retirement age, especially women
- decreasing workforce participation for the 15–24 years age group as they stay longer in education
- increased skill levels for workers
- job growth in the aged care sector.

18.5.3 Social influences

Changing work patterns

Over the last two decades there has been a dramatic growth in part-time and casual work, largely due to growth in the finance, retail, hospitality and community service industries. Most part-time workers do not want to work additional hours and part-time work offers them flexibility in balancing their work and personal lives. Work patterns are changing and commentators refer to this trend as 'labour fragmentation'.

In recent years there has been an obvious drift away from traditional full-time employment towards part-time employment. In 1979 only 16 per cent of the workforce identified themselves as part-time employees, but by 2012 this had grown to 32 per cent. Part-time work is especially common among women.

Businesses in search of greater flexibility in the workplace are more likely to offer part-time options that are greeted favourably by workers in search of a better work–life balance. Other workers may be interested in undertaking additional education and training and/or want to ease themselves into retirement and are also keen to take advantage of such arrangements.

Other changes such as a 'casualisation' of the workforce are evident in changing work patterns and as businesses seek a more flexible workforce. The proportion of casual workers grew from 17 per cent in 1992 to approximately 25 per cent today.

Despite being popular in industries such as retail and hospitality, many casual workers would prefer to work additional hours. While casual workers are in search of more flexible work arrangements such as those provided by casual work, most would like to receive paid holiday or sick leave.

SNAPSHOT

Case study: When sharing is caring for the bottom line



Work flexibility may be mandatory under Commonwealth employment laws, but part-time work and job sharing have become a boon for smaller businesses seeking and retaining talent.

Employment arrangements such as job sharing are provided by the business above and beyond what is legally required. For employees, the demands of balancing family and work can be challenging. Offering employees the opportunity to job share may be mutually beneficial for the employer and the employee.

Human Resources adviser Jenni Pavlou observes that job sharing has become increasingly popular in administration positions.

Student Kelly Chandler job shares with Lee Anne Wolterman — who wanted to spend more time on her horses and equestrian interests — at law firm Maddocks in Melbourne.

'I'd recommend job sharing; I actually like it,' Ms Chandler said of her two-day-a-week job. 'You have to be organised. We've learned to work together.'

A lot of it still comes back to recruiting good staff.

'People will often be harder to select (for flexible arrangements) but the key thing is hiring well,' Ms Pavlou explained.

'The statistics show you (the employer) have a 50 per cent chance of getting it right. This is where you need compatibility of workers. They must have similar motivation, and drive. Most important is their willingness to share information, and to be secure about themselves; otherwise, that's a problem!'

Source: Extracts from J Dowling 2010, 'When sharing isttcaring for the bottom line', *The Age*, 25 March.

SNAPSHOT

Case study: The budget promises jobs, but does little for workers in the gig economy

Treasurer Josh Frydenberg promised a federal budget focused on 'jobs, jobs, jobs'. But it wasn't about all jobs.

While the budget devotes billions to getting unemployed Australians into traditional employment, it does little for those with diminishing opportunities to find work outside the "gig economy", where they are effectively treated as subcontractors, not as employees with rights secured by the Fair Work Act.

But largely missing from the government's considerations are those in sectors hit hardest by the COVID-19 pandemic where jobs are increasingly precarious.



It is not just workers in 'blue-collar' jobs in hospitality and delivery that increasingly face few opportunities to find a secure, full-time job.

Casualised, part-time and freelance 'gig' work is also increasingly common in 'white-collar' industries such the media, the arts and higher education.

The term 'gig economy' was coined in 2009, at the height of the global financial crisis, as scores of unemployed and underemployed workers picked up various odd jobs to cover their living expenses.

Journalist Tina Brown (a former editor of *The New Yorker*) predicted the gig economy was 'the new face of the job market' for knowledge workers.

A decade on, it's difficult to track the exact scale and shape of the gig economy — partly because terms like 'gig work', 'freelance work', 'flexible work and 'digital platform work' are used interchangeably.

One of the gig workers I interviewed was Joseph, who was delivering food around Perth for Uber Eats. As the first restrictions kicked in, his work evaporated almost immediately. He told me that one week he made $78 for 10 hours' work — about $7.80 an hour, less than half the national minimum wage of $19.84 an hour. After fuel and vehicle costs, he estimated he cleared just $20.

All five delivery workers I interviewed said they had earned less than the national minimum wage at one time or another. Joseph at least qualified for JobSeeker, but others were migrant workers with no right to welfare payments.

Source: Nat Kassel, 'The budget promises jobs, but does little for workers in the gig economy', *The Conversation*, 20 October 2020.

Career flexibility and job mobility

Career flexibility and job mobility have increased. Workers are taking more control over their own careers. Around 14–16 per cent of employees are considered job mobile, and only 44 per cent of full-time employees have worked for their current employer for more than five years. The most mobile employees are aged 20 to 24, Australian-born, or of English-speaking background, and found in retail or hospitality industries. Many leave full-time positions after developing specialist skills and experience to become independent contractors or consultants.

Creative and knowledge-based fields like education, design, writing and information technology provide the most flexibility in the workplace and many workers in these occupations, especially women, are seeking part-time, casual, flexible work day and work-from-home options. Both businesses and the government are recognising the need to address these demands and in doing so are providing increased options for employees.

Increased participation rates for women and older workers

The increase in the **participation rate** over the past three decades has been due to the increased participation by women and older people in the workforce. Since 1980, the participation rate of females aged 25 to 54 has increased by over 20 per cent, reflecting changing social expectations, increased education levels, improved access to child care and more flexible work arrangements.

The participation rate of people aged 55 and over has increased by 10 per cent as people have incentives to work longer, better employment opportunities, increased employment opportunities in the physically less demanding services sector, and better health and longer lives.

BizFACT

Australia's economic recovery from the COVID-19 pandemic will require that participation rates for women are increased.

Estimates by KPMG halving the gap between male and female participation rates would increase annual gross domestic product by $60 billion over the next 20 years.

Ageing of the workforce

Ageing of the workforce is likely to see a significant shortage of skills in the community over the next few years. Flexible working arrangements, including job share, part-time and contracting, will be critical in utilising this ageing workforce, particularly women, who are concentrated in health, education, and society and culture. Businesses and government will need to respond by upskilling the population, creating incentives to encourage staff to postpone retirement and implementing appropriate human resource strategies to transfer skills to those remaining in the workforce. Removing discrimination in the recruitment of older workers, providing opportunities to update skills, and offering targeted health and safety programs will also be essential.

BizFACT

Australia's female participation rate for women is 4 per cent lower than countries like New Zealand and Canada. Effective policies to increase female involvement in the workforce, such as childcare availability, flexible hours and removing discrimination, would substantially increase the size of the economy.

Early retirement

Early retirement from full-time work is popular today. The average age of retirement from full-time work has increased to an average age of 53 years (58 for males and 47 for females); however, participation in part-time work is much higher, suggesting older employees are using a gradual withdrawal approach to retirement. The most common reasons are eligibility for superannuation or for health reasons. A growing number of people are returning to work in a part-time capacity following retirement for financial reasons or to relieve boredom.

participation rate the percentage of a given group of individuals of working age who are employed or actively seeking work

ageing of the workforce refers to the increase in the average age of the population, due to sustained low fertility and increasing life expectancy. As a result, there are proportionally fewer children under 15 in the population, and more people in older age groups.

BizFACT

Compulsory retirement is now illegal unless someone is on a federal award/agreement that states a compulsory retirement age.

Living standards

Australians have one of the highest living standards in the world today. These high standards include work health and safety, regular wage increases, performance bonuses, fringe benefits, leave and superannuation benefits, which they remain keen to preserve. Australians are aware of the pressure from global competition on these hard-won benefits and our living standards. All political parties recognise the importance of these conditions to the average Australian at work, and are unlikely to challenge these rights in the future.

Companies who seek to undercut conditions through excessive outsourcing and casualisation of the workforce, or by shifting production or operations offshore to reduce costs and increase profits, will be challenged by unions keen to avoid erosion of our living standards. Casualised workers suffer from higher levels of stress due to difficulty in purchasing assets, including homes, and managing finances and debt with unstable or uncertain income.

FIGURE 18.25 Australians love extended shopping hours, but at what cost?



Social expectations in terms of home ownership, holidays and ownership of consumer goods are an important factor in the rising participation of women in full-time and part-time work, and in the rising retirement age for women.

Conflict between our desire for high living standards, achieved through our work–life balance, is evident in many surveys. We enjoy shopping on weekends and on holidays, which is reflected in liberalised trading hours.

Concerns are, however, frequently raised about the loss of weekends for families working flexible hours and shifts. The blurring of work and home lives, because of electronic communications such as email and mobile phones, is creating an expectation that employees and businesses will be 'always on'. Others cite the lack of support for carers in our community. Governments have responded by implementing legislation to encourage workplaces to become more family friendly, through providing carer's leave, job share, part-time and flexible working hours.

A recent report, *Shifting Risk: Work and Working Life in Australia*, prepared for the ACTU, indicates Australians had major concerns about their living standards and working life over the last few years. They are concerned about:

- increasing income inequality in Australia, as growth in real wages has lagged behind profit growth in recent years, and the widening gap between average male and female wages
- the casualisation of the workforce, with two million Australians now working part-time or casually, and the pressure this creates on family finances and life
- increasing pressure to manage the finances in their lives as governments retreat from welfare and encourage individual responsibility for retirement, healthcare, education and debt management
- a lack of work–life balance, with long working hours and loss of holidays and weekends with families.

Australians are keen to have 'quality jobs' that are safe, meaningful, secure and productive; where they are respected and consulted by their employer, and earn enough for a decent standard of living.

BizFACT

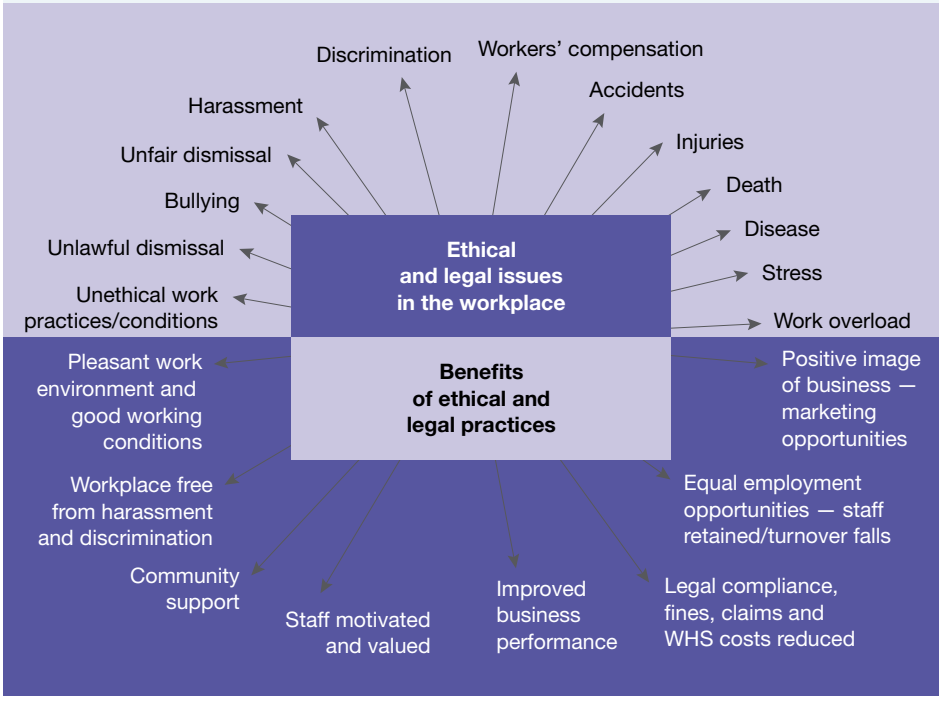
There is an increasing global trend for women to be the family's breadwinner and thus improve its financial security. Increased female participation rates, male unemployment or underemployment and the desire to achieve career goals are thought to be behind the greater contribution of women to family finances. The traditional male-breadwinner and female-homemaker view is being challenged and the social consequences of such a change will be an important research topic in human resources in the years ahead.

18.5.4 Ethics and corporate social responsibility

A wide range of human resource issues arise in the workplace (see figure 18.26) and, if they are not handled in an ethical, legal or socially responsible manner, they can lead to poor morale, low productivity, heavy costs and industrial disputes. **Ethical business practices** are those practices that are socially responsible, morally right, honourable and fair.

ethical business practices those practices that are socially responsible, morally right, honourable and fair

FIGURE 18.26 Some ethical and legal issues arising in the workplace and the benefits of dealing with them successfully



BizFACT

Corporate Social Responsibility (CSR) refers to the way that a business considers the financial, environmental and social impacts of its decisions and is often referred to as its 'triple bottom line'. The human resource policies and procedures of a business are often an integral component of its CSR.

How businesses exhibit corporate social responsibility in the management of human resources

A socially responsible, ethical employer recognises that:

- a pleasant working environment and good working conditions are valuable in motivating and retaining staff
- performance and motivation are maximised when staff feel secure, confident in their work, recognised, safe, equally valued and rewarded for their efforts
- an effective workplace benefits from good working relationships and teamwork
- the business depends on community support, as a source of staff and as a source of business (that is, customers) and resources
- management should be committed to an ethical workplace culture
- customers eventually find out which businesses are acting responsibly and which are not.

BizFACT

A recent study indicated that 90 per cent of business students would be willing to forgo a percentage of their income to work for an ethical business.

An ethical framework must be developed for the workplace, in collaboration with the major stakeholders. This framework may include a **code of conduct** and a **code of ethics**. Key principles may include ensuring equity in workplace processes, legal compliance and commitment to customers.

code of conduct a statement of acceptable and unacceptable behaviours in a business

code of ethics a statement of a firm's values and principles

best practice refers to business practices that are regarded as the best or of the highest standard in the industry

The benefits accruing from ethical practices are becoming increasingly evident from research and include the following:

- Staff retention and absenteeism rates improve as staff feel more valued and motivated.
- Business costs (such as recruitment and training) are reduced and business performance is enhanced.
- There are significant marketing and business opportunities — **best practice** employers enjoy regular publicity in the media, in journals and on the internet.

FIGURE 18.27 Managers are important role models for ethical and responsible behaviour.



Working conditions

An ethical employer can be expected to achieve safe and fair working conditions that improve the welfare of employees. This is achieved through:

- compliance with social justice and industrial legislation covering areas of WHS anti-discrimination and equity in all aspects of human resources.
- providing a safe and healthy working environment, safe working practices and equipment, appropriate supervision and training in safety and health, without which, workplace incidents may occur (see the following case study)
- creating challenging, interesting and meaningful work to stimulate intrinsic rewards for staff
- improving communication, and fostering teamwork and empowerment of staff
- providing study leave and training opportunities to reduce skills obsolescence and improve access to management positions
- offering equitable and open rewards and benefits subject to clear criteria
- offering flexible working hours and conditions that promote a balance between work and life
- a strategic plan supported by management that incorporates specific ethical responsibilities
- implementing change through collaboration with staff
- establishing a **code of practice** for customers, employees and suppliers
- evaluating and benchmarking its performance to ensure it is operating at best practice.

code of practice a statement of the principles used by a business in its operations. It generally refers to practices that are seen as ethical or socially responsible.

SNAPSHOT

Case study: Working conditions — ethical and legal issues

A case was brought to a local court in Sydney in which a 19-year-old pizza deliverer charged his employer with assault. The pizza store manager allegedly:

- locked him in the freezer for almost half an hour, ignoring his pleas to be released because of his asthma
- tied the teenager to the bonnet of his car while he drove it back and forwards
- sprayed a fire extinguisher under the door of a toilet cubicle where the teenager was hiding
- hit the teenager in the head, jammed his ankle in a door and cut his face with a wristwatch during a scuffle.

In court, the 27-year-old manager defended his actions, claiming they were part of the teenager's 'initiation' into the company. The manager was found guilty on four counts of criminal assault. He was fined $650 and placed on a 12-month $500 good behaviour bond.



Working conditions have come under focus over the last two decades as businesses have increasingly responded to global competition and sought to develop practices that improve efficiency and save on labour costs, which are generally around 60 per cent of most businesses' costs.

This pressure to become competitive has been reflected in the rapid growth of 'precarious employment' — employment that is predominantly casual and part-time — in which employees lack job security; are unable to obtain credit; often work multiple jobs and long shifts; and have no leave entitlements. Many are poor and suffer 'travel poverty', commuting long distances to work and on heavily congested highways.

Exploitation of adult workers through outworking and subcontracting locally and offshore is often raised as a major ethical issue. Many are concerned about the nature and extent of child labour globally, and what they see as a constant 'race to the bottom' to secure the cheapest cost of labour. Businesses argue that many jobs involve a high level of skill and education and only those jobs that are unskilled and offer a major labour cost differential are shifted offshore. They argue that shareholder pressure for ongoing profits requires them to constantly search for more efficient approaches to managing their most costly resource — employees. These factors are behind businesses' decision to shift offshore.

BizFACT

Investments that are acknowledged as 'ethical', have also experienced success, particularly when large occupational investment groups pressure their pension funds to invest in ethical businesses.

Businesses are sensitive to consumer concerns due to the success of consumer lobby groups and actions, and media scrutiny.

Ethical businesses have responded by demonstrating corporate social responsibility through such strategies as regularly undertaking audits of their factories abroad, and by working with agencies to support ethical practices in their local and offshore operations. In the clothing industry, traditionally renowned for 'sweatshops', businesses seek accreditation from agencies such as Ethical Clothing Australia and Fair Wear Foundation.

BizFACT

Ethical Clothing Australia is a not-for-profit organisation funded by the the Victorian Government that works for a more transparent textile, clothing and footwear (TCF) industry to ensure that consumers and buyers can identify and support ethically made Australian TCF goods.

SNAPSHOT

Case study: Ethical Clothing Australia — CSR in action



Marina is a journalist writing about Ethical Clothing Australia for a new TV fashion program and website.

Steph, Fina, Georgie, Matt and Rocco are friends interviewed by Marina, while out at a club.

Marina: Do you know where your clothes are made?

Steph, Matt: No idea!

Georgie: I made my own! Aussie Aussie Aussie, Oi Oi Oi!

Marina: Do you know any labels made in Australia?

Steph: Aussiebum?

Marina: Yes, and designers that produce under the labels Pure Pod, MHOO MHOO and Vodim. All committed to producing 100 per cent Australian made, ethical fashion. We have heard that sales of Aussiebum went up hugely when the story about that other major 'Aussie' business moving its production offshore appeared. They sacked nearly 2000 staff in the move.

Marina: As future fashion designers, are you aware of how and where our clothes are made?

Rocco: (Pulling at Fina's label) I'll check out your label Fina! Aha! Made in Vietnam.

Fina: It's cheap, and it's all I can afford right now. I should really be thinking about why it is so cheap. I guess even a child could have made this overseas. Now you make me feel guilty.

Rocco: Well, I know that around 92 per cent of all clothes sold in Australia are imported.

Marina: Well, Fina, your dress was made by someone probably earning less than $3.60 per hour, according to something I saw on the ABC the other day. It can be as little as 1 per cent of the selling price of the clothes.

Georgie: How come you know so much about this Rocco?

Rocco: My Business Studies teacher in high school used to work in the fashion industry, and I actually listened in class, not like you, always texting when the teacher wasn't looking.

Marina: Do you think we can assume all the clothes made here are made ethically too?

Fina: I have some friends who run a business here; they design the clothes and then get a contractor to make them. They only do small runs, so they don't get their stuff made overseas.

Marina: Do they know about the conditions worked by the garment workers?

Fina: I don't know how much they ask.

Marina: How many of you are aware that many of the clothes made here are subcontracted to garment workers working at home often earning only $8 per hour?

Steph: Yeh, I know. I have a friend whose mother does it at home; she works around 15 hours a day. She often works on shirts where she gets paid $3 per shirt and it takes 30 minutes to make. She has to stay home because her mum is unwell, so it's all she can do. She has bad eyesight now and her hands are a mess from the constant strain on her fingers.

Matt: There are sweatshops everywhere, but what can we do about it?

Steph: Well, she could join the union. I've told her but she does not want to cause trouble.

Marina: Are you aware of the Ethical Clothing Australia (ECA) program? It is encouraging businesses who use ethical clothing practices to use labelled swing tags on the clothes. All they have to do is get accredited. ECA helps 'map' your supply chain and verifies that all workers within it are receiving their legal entitlements. This means anyone who wants to buy from companies who treat employees fairly can see from the swing tag. Fashion brands like Cue and Veronika Maine and footwear businesses like R.M. Williams are all supporting it. If companies see that consumers are supporting ethical companies, here and overseas, and that they are getting government contracts and media attention, others will follow. Would you stay in touch with our website on this in future? What will you all do when you finish your course?

Georgie: Well, I'll be hassling the company I work for to do that or do it myself. I certainly will be asking about it when I buy clothes in future. I don't want to be buying things made by kids, and I want anyone who makes my clothes to get a fair deal.

Steph, Fina, Matt and Rocco: We will be following what your website and the ECA suggest too.

on Resources

Weblinks Shifting Risk: Work and Working Life in Australia
Ethical Clothing Australia

KEY IDEAS

- Economic factors have a major impact on the demand for labour and the pressure on wage growth. This affects the role of human resource management in planning to acquire or reduce staff, and in negotiating awards and agreements.
- Globalisation has increased competitive pressures on businesses, with many increasingly recruiting or outsourcing functions offshore.
- Technological change allows many employees to work from home or offshore, and assists business in providing 24-hour support.
- The workforce is increasingly more flexible in working arrangements, with a recent dramatic increase in part-time and casual work.
- The community is increasingly concerned that this flexibility is leading to difficulties for families in balancing their work and life responsibilities.
- Major social factors affecting the workforce today include increased participation of women and an ageing of the workforce.
- Global organisations are increasingly focused on promoting trade between countries and organisations that support ethical employment practices.
- Ethical business practices are those practices that are socially responsible, morally right, honourable and fair.
- Many businesses are realising the benefits of a more committed workforce and good public reputation achieved through embracing the ethical principles of corporate social responsibility.

18.5 Activities

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18.5 Quick quiz on	18.5 Exercise	18.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 4, 13, 14, 16, 19, 20, 21, 22, 24, 29	1, 3, 5, 7, 9, 10, 11, 17, 18, 26, 27, 30	6, 8, 12, 23, 25, 28

18.5 Exercise

Revision

1. The influences on human resource management include legal, economic, social, technological and ethical influences. Read the following scenarios, which each describe a change in workplace employment practices. Identify the type of influence that may have caused each change and **discuss** the likely impacts each may have.
   - **a.** An agreement is introduced to allow continuous production and changes in work practices.
   - **b.** Employees are more highly educated today, and seek greater challenges and rewards from work.
   - **c.** Affirmative action awareness is made a criterion for promotion to management positions.
   - **d.** Training in the management of employee complaints of discrimination is provided.
   - **e.** A call centre operating out of Fiji is set up to handle customer service calls.
   - **f.** Three hundred assembly line workers are being retrenched as their jobs are redundant. The human resource manager may offer younger staff the opportunity to 'up-skill' for jobs in other areas of the business.
   - **g.** Australian staff in the Vietnam office are being given cultural awareness training.
   - **h.** Two employees work out of Australia and four work out of the United Kingdom in a 'virtual team'. They hold regular video conferences to develop and improve product design.

2. **Match** the correct terms with the appropriate definitions.

multiskilling	restructuring	outsourcing	productivity
code of conduct	corporate social responsibility		feminisation of workforce

   a. Occurs when a firm changes its organisational structure and functions, often closing down sections or removing jobs that are no longer needed or too expensive for the business to operate
   b. Involves employees learning new tasks, which allows them to carry out a wider range of tasks in the workplace
   c. The efficiency of production of goods and services; officially output per unit of input per employee
   d. The increasing participation of women in the workforce
   e. Firms hire businesses or consultants to carry out tasks such as accounting or marketing for them on a contract basis
   f. A statement of acceptable and unacceptable behaviours in a business
   g. Employers making decisions that consider the welfare of employees and the community

3. **How** is structural change affecting the workforce?
4. **Describe** three impacts of globalisation on the management of human resources.
5. **Discuss** the impact of technology on employees.
6. a. For three minutes, identify your ideas about the meaning of and the perceptions associated with 'changing work patterns'.
   b. Select a partner. For about five minutes share your ideas with your partner. Then have your partner share his or her ideas with you.
   c. In your pairs, **create** a table that records shared views about changing work patterns using the headings: Positive views, Neutral views and Negative views.
   d. **Analyse** these views and explain each. It is important that you can support each explanation with reliable evidence (not unsubstantiated claims).
7. 'Having one of the highest living standards in the world has costs and benefits particularly in relation to working conditions.' Jesse Hancock, consultant, HRM Direct. **Discuss**. In your answer refer to the *Shifting Risk: Work and Working Life in Australia* report.
8. In small groups, use the brainstorm technique to **determine** the human resource management issues that may arise due to economic, technological and social influences. Share your answer with the rest of the class.
9. Write a report for a business magazine entitled *Managing people ethically.* **Explain** all the reasons corporate social responsibility and ethical practice are important for business today. Give examples from the cases provided in this chapter.
10. **Investigate** companies who are accredited for ethical clothing practices. The **Ethical Clothing Australia** website may help.
11. **Discuss** what students at school can do to encourage ethical employment practices in the clothing industry.

Read the 'Open letter from 265 economists — don't sacrifice health for the economy' case study and answer questions 12 and 13.

12. **Analyse** the statement 'We cannot have a functioning economy unless we first comprehensively address the public health crisis'.
13. **Outline** the effects of the inability to contain COVID-19 on the quality and quantity of the workforce.

Read the 'Zoom meetings help marginalised staff feel included — we should keep having them even after offices reopen' case study and answer questions 14 and 15.

14. **Discuss** the shift to online meetings that occurred during the pandemic.
15. Do you feel that working remotely should be a feature of the organisation of future work? Support your answer with examples.
16. Refer to the case study 'When sharing is caring for the bottom line'. According to Jenni Pavlou, **what** are the risks and benefits for employers considering job sharing in the workplace?

Read 'The budget promises jobs, but does little for workers in the gig economy' case study and answer questions 17 to 20.

17. **Why** is the recent budget not necessarily all about jobs, as indicated by the Treasurer Mr Frydenberg?
18. **Explain** why subcontractors are considered as the hardest hit by the COVID-19 pandemic.
19. **Outline** the term the 'gig economy' and how its definition has changed over time.
20. **Describe** the experience of Joseph as a food delivery driver. **Identify** concerns that you may have if you too worked in the 'gig economy'.
21. Refer to the case study 'Working conditions — ethical and legal issues'. **Identify** the ethical and legal issues arising from the treatment of the pizza deliverer.

Read the 'Ethical Clothing Australia — CSR in action' case study and answer questions 22 to 24.

22. **What** are the major concerns that consumers have about the fashion industry in Australia?
23. **Create** and conduct a short survey of those around you to investigate:
    a. general views about labour practices in the clothing industry
    b. the level of support for more ethical practices in the clothing industry.
24. **Summarise** your conclusions and share them with the class.

Extension

25. Collect information from annual reports, often under the heading of Sustainability, to **determine** how more businesses today are using a human resource management approach to managing people. Using the information, construct three cartoons that show a human resource management approach to managing people and three cartoons that show where a human resource management approach is not being used.
26. Use the internet to **investigate** trends in gender equity in Australia. Visit sites such as the Workplace Gender Equality Agency (WGEA). Why has gender equity improved slowly over time?
27. Rachel is a human resource consultant. Pretend you are Rachel and write a response to each of the letters below. **Compare** your answers with your classmates.

> Dear Rachel,
>
> I have just taken over my parents' piggery. I have been away studying physics at uni and have no idea about managing a pig farm. There are eight staff members, and some of them have slackened off a lot over the last few months. Two had a big punch-up yesterday. I'm at my wit's end. How do I start managing all these people? Can I just sack the ones who are the main problem? Who can help me?
>
> Peter

> Dear Rachel,
>
> I recently got work in a large supermarket chain. They told me I had to do two days' trial to see if I was any good at the job, and then they took me on probation for six months. They have not paid me for those two days, and I have only been paid twice. The owner often makes disgusting comments about me. He does the same thing with the other employees too. I really need this job, but I want to be paid on time and not be harassed by my boss. What do I do?
>
> Latife

> Dear Rachel,
>
> The toy company I work for is outsourcing the production of electronic dogs to India. Luckily, I am being retrained, but some will lose their jobs. Why doesn't the government stop this?
>
> Victoria

28. Write a report **analysing** the current state of labour practices in the global clothing industry and why these are a concern for society.
29. **What** are the reasons behind the demise of the Australian car industry? Discuss the implications of this for Australian workers.
30. 'Coles has developed a 2020 inclusion strategy aimed at building an inclusive workplace where all team members feel supported.' *Wesfarmers Annual Report 2017*

    Examine the issue of sustainability in the Wesfarmers annual report and analyse the strategies used by management to develop an inclusive culture across its range of businesses.

18.5 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q9

At which stage of the economic cycle is it most likely for a business to begin to reduce staff working hours?

A. Boom
B. Downswing
C. Recession
D. Upswing

Question 2 (5 marks)

Source: HSC 2019 Business Studies Exam, Section II, Q23c

Assess the impact of ONE social influence on human resource management.

Question 3 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q11

An increasing number of employees are seeking a better work–life balance. As a result, many businesses are adopting job sharing.

This is an example of establishing

A. communication systems in response to a social influence.
B. flexible working conditions in response to a social influence.
C. communication systems in response to an economic influence.
D. flexible working conditions in response to an economic influence.

Question 4 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q19

A business implements a new policy that limits the use of work-related email accounts before 8 am and after 8 pm.

Which consideration has most likely led to the development of this policy?

A. Economic
B. Legal
C. Social
D. Technological

Question 5 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q12

Work patterns in Australia have changed over the past 20 years.

An example of such a change is the decrease in

A. casualisation.
B. part-time positions.
C. female participation.
D. full-time male participation.

More exam questions are available in your learnON title.

18.6 Review

18.6.1 Summary

Stakeholders in the human resource management process

- The major stakeholders in the human resources process are employers, employees, employer associations, trade unions, government and government agencies, and industrial tribunals and courts.
- Each stakeholder has perspectives that may conflict or be shared with those of other stakeholders, leading to conflict or cooperation.
- Stakeholders are increasingly operating at a variety of scales and developing global networks in response to the globalisation of business.
- Membership of trade unions has declined dramatically over the last decades at a global level in response to many factors, including the shift to less hazardous work in the increasingly dominant service sector.
- To simplify industrial relations and improve efficiency, a national system of industrial relations has been created.
- Government statutes provide the framework for employment conditions.
- Since January 2010, Australia has shifted to a dual industrial relations framework with most workers covered by a federal award and some workers, mostly public servants, teachers and essential service employees such as police and nurses continuing with state-based awards.
- The system is implemented under the *Fair Work Act 2009*.
- Industrial tribunals and courts enforce the employment laws.
- The Fair Work Commission is the national industrial tribunal that replaced the Australian Industrial Relations Commission. Its powers have been expanded to allow it to hear and settle disputes, supervise agreement making and award simplification.
- Other government agencies are also stakeholders in the human resources process including the Australian Human Rights Commission (AHRC).
- Society has a number of expectations regarding employment conditions.

Legal influences: The employment contract

- From 2007, under the Labor government, most Australian states and territories formed a national system for industrial relations to improve efficiency through more uniform laws and regulations.
- Australia had a centralised system of industrial relations until 1991 when enterprise bargaining was introduced.
- All employees are covered by an employment contract, even if it is not written.
- A written contract provides more comprehensive protection than a verbal contract.
- Independent contractors are self-employed and do not have the same rights as employees.
- Workplace relations are governed by common law, statutes made by parliament through legislation, and awards and agreements supervised by industrial tribunals.
- All employees and employers have legal rights and responsibilities.
- Employers must pay income and work expenses, comply with industrial laws, and provide a safe workplace for employees.
- Employees must obey lawful and reasonable demands made by the employer, use care and skill in their work, and act in good faith and in the interests of the employer.
- Under the national system, from 2010, ten minimum employment standards were established to provide a safety net for employees, particularly the low paid.
- Replacing many functions formerly conducted by the Australian Industrial Relations Commission, the Fair Work Commission was set up to manage awards and agreements, hear and help resolve industrial disputes, determine annual minimum wage cases, and supervise award restructuring.
- Employee wages and conditions are primarily determined by awards, enterprise agreements and minimum employment standards.

- From 2010, minimum wage rates for ordinary hours worked have been determined by:
  - award or agreement that covers the employee
  - the national wage minimum for employees not covered by awards or agreements and reviewed annually by the Fair Work Commission.
- Awards are legally binding documents containing the minimum terms and conditions of employment.
- Enterprise agreements are collective agreements made at the workplace (enterprise) level between an employer and a group of employees about terms and conditions of employment.
- Individual contracts of service exist when an employer and an individual employee negotiate a contract covering pay and conditions.
- Independent contractors, often known as consultants or freelancers, undertake work for others but do not have the same legal status as an employee.
- The government, both federal and at state level, has the role of ensuring that Australia has a flexible, modern workplace that supports a national industrial relations framework with clear and enforceable minimum national employment standards.

Legal influences: Work health and safety and anti-discrimination

- Work health and safety (WHS) legislation is in the process of being made uniform around Australia to improve business productivity.
- The relevant act in New South Wales is the *Work Health and Safety Act 2011*.
- Employers must provide a safe system of work, and ensure employees are trained and supervised in their work.
- All employers must take out workers' compensation insurance.
- Employees are also responsible for taking reasonable care for the health and safety of others.
- In New South Wales three organisations — SafeWork NSW, the State Insurance Regulatory Authority (SIRA) and Insurance and Care NSW (icare) — are the organisations responsible for WHS, workers compensation, and insurance and care services for injured workers respectively.
- Common law redress can be sought where the employer or another employee has been negligent or breached their duty, leading to serious injury or death.
- Discrimination occurs when a policy or a practice disadvantages a person at work because of a personal characteristic that is irrelevant to the performance of their work.
- All employers must implement anti-discrimination legislation, as well as audit all policies and practices to avoid large fines, legal orders and damages, and loss of reputation.
- Anti-discrimination legislation is supported by government agencies, including the Australian Human Rights Commission, the Workplace Gender Equality Agency and the Anti-Discrimination Board (NSW).
- Equal employment opportunity refers to equitable policies and practices in recruitment, selection, training and promotion.
- Affirmative action refers to measures taken to eliminate direct and indirect discrimination and for implementing positive steps to overcome the current and historical causes that result in a lack of equal employment opportunity for women.
- There is significant gender inequity in management roles in Australia.
- All employers with more than 100 employees, and all higher education authorities, must report annually, unless exempted, on equal opportunity programs they develop in consultation with employees and progress achieved.
- Businesses that do not comply are likely to be named in parliament, and excluded from government contracts and industry assistance grants.
- Strategies commonly used to resolve a complaint of discrimination include apology, counselling, official warning, mediation, conciliation or disciplinary action.
- Developing a code of practice and making equal opportunity awareness a criterion in promotion and performance appraisal are two of the practical strategies that can be used to improve affirmative action and gender equity.

Economic, social, technological and ethical influences

- Economic factors have a major impact on the demand for labour and the pressure on wage growth. This affects the role of human resource management in planning to acquire or reduce staff, and in negotiating awards and agreements.
- Globalisation has increased competitive pressures on businesses, with many increasingly recruiting or outsourcing functions offshore.
- Technological change allows many employees to work from home or offshore, and assists business in providing 24-hour support.
- The workforce is increasingly more flexible in working arrangements, with a recent dramatic increase in part-time and casual work.
- The community is increasingly concerned that this flexibility is leading to difficulties for families in balancing their work and life responsibilities.
- Major social factors affecting the workforce today include increased participation of women and an ageing of the workforce.
- Global organisations are increasingly focused on promoting trade between countries and organisations that support ethical employment practices.
- Ethical business practices are those practices that are socially responsible, morally right, honourable and fair.
- Many businesses are realising the benefits of a more committed workforce and good public reputation achieved through embracing the ethical principles of corporate social responsibility.

18.6.2 Key terms

affirmative action measures taken to eliminate direct and indirect discrimination, and for implementing positive steps to overcome the current and historical causes of lack of equal employment opportunity for women
ageing of the workforce refers to the increase in the average age of the population, due to sustained low fertility and increasing life expectancy. As a result, there are proportionally fewer children under 15 in the population, and more people in older age groups.
award the legally enforceable minimum terms and conditions that apply to a business or industry
award simplification the process of reducing the number of matters in each award and eliminating inefficient work practices
best practice refers to business practices that are regarded as the best or of the highest standard in the industry
'better off overall test' (BOOT) requires that each of the employees to be covered by the agreement is better off overall than under the relevant modern award
casual employee an employee in employment that is short term, irregular and uncertain; they are not entitled to paid holiday or sick leave
centralised industrial relations system a collectivist approach in which disputes are referred to industrial tribunals, such as the Fair Work Commission, for conciliation and arbitration
code of conduct a statement of acceptable and unacceptable behaviours in a business
code of ethics a statement of a firm's values and principles
code of practice a statement of the principles used by a business in its operations. It generally refers to practices that are seen as ethical or socially responsible.
collective agreement an agreement made between a group of employees (or one or more unions representing employees) and an employer or group of employers
common law law developed by courts and tribunals
constitutional corporation one that falls under section 51(xx) of the Constitution of Australia — identified as foreign corporations and trading or financial corporations formed within the limits of the Commonwealth
decentralised industrial relations system a system in which employers and employees negotiate wages and working conditions in the individual workplace, through collective or individual bargaining and without the involvement of tribunals
discrimination when a policy or a practice disadvantages a person or a group of people because of a personal characteristic that is irrelevant to the performance of the work
employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.

employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees
employer association an organisation that represents and assists employer groups. They are usually respondents to the awards covering the employees of their members, and covering employers in the same or related industry.
employment contract a legally binding, formal agreement between employer and employee
enterprise agreement a collective agreement made at a workplace level between an employer and a group of employees about terms and conditions of employment
equal employment opportunity (EEO) refers to equitable policies and practices in recruitment, selection, training and promotion
equity the provision of equal opportunities for all employees to gain access to jobs, training and career paths
ethical business practices those practices that are socially responsible, morally right, honourable and fair
independent contractor often known as a consultant or freelancer, independent contractors undertake work for others; however, they do not have the same legal status as an employee
individual contract when an employer and an individual employee negotiate a contract covering pay and conditions
Individual Flexibility Agreements (IFA) allow an employer and an employee to come to an agreement that varies the modern award or enterprise agreement to address their individual circumstances
judicial power refers to the power of courts to interpret and apply laws
log of claims a list of demands made by workers (often through their union) against their employers. These demands cover specific wages and conditions. Employers may also serve a counter-log of claims on the union.
modern award an industry or occupation-based award that covers all private sector employers and employees who perform work that falls within their scope. They replace all existing national system awards (except those applying to a single enterprise). They do not cover employees earning higher incomes.
on-costs additional costs involved in hiring an employee, above the cost of their wages. These costs traditionally add around 25 per cent of the cost of the wage and include sick leave, holiday leave, leave loading, superannuation, retirement and redundancy payments, and other costs.
participation rate the percentage of a given group of individuals of working age who are employed or actively seeking work
social justice in the workplace involves businesses being responsible or behaving in a fair and ethical manner towards their employees, customers and the broader community
stakeholder any individual or group that has a common interest in or is affected by the actions of an organisation
statutes laws made by federal and state parliaments; for example, laws relating to employment conditions
structural change a change in the nature and pattern of production of goods and services within an economy. This includes a significant growth in the level of services in an economy compared to other sectors.
trade union an organisation formed by employees in an industry, trade or occupation to represent them in efforts to improve wages and working conditions of their members
workers' compensation a range of benefits to an employee suffering from an injury or disease related to their work. It is also provided to families of injured employees when the injury/disease was caused by, or related to, their work.

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Digital documents	Key terms glossary (doc-35672) Chapter crossword (doc-36223)
Interactivity	Chapter crossword (int-7175)
Exam question booklet	Chapter 18 Exam question booklet (eqb-0040)

18.6 Activities

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Exercise 1: Multiple choice questions

1. Why are employers' responsibilities in relation to human resource management increasing today?
   - **A.** Legal compliance demands are increasing.
   - **B.** Costs of confrontation with unions are too high.
   - **C.** Legislation and agreements require them to negotiate agreements and solve conflicts at workplace level.
   - **D.** Governments are focused on workplace reform.

2. Why are governments keen for employees to extend their planned retirement date?
   - **A.** Australia is experiencing labour shortages in a number of areas currently.
   - **B.** The ageing population will lead to further labour shortages.
   - **C.** Many Australians do not have sufficient funds for retirement.
   - **D.** All of the above

3. Key government roles in HRM include which of the following?
   - **A.** International representative, policy administrator, employer
   - **B.** Employer, legislator, economic forecaster
   - **C.** Legislator, policy administrator, employee manager
   - **D.** A and C

4. Statute law is a significant legal influence on human resource management. What does it refer to?
   - **A.** Law passed by state governments
   - **B.** Law passed by federal and state governments
   - **C.** Federal, state and common law
   - **D.** Commonwealth government legislation

5. Which of the following is not a recommended feature of a typical employment contract?
   - **A.** Superannuation
   - **B.** Confidential information
   - **C.** Job enlargement and enrichment
   - **D.** Promotion policy and procedures

6. Which of the following are not a responsibility of employers to their employees?
   - **A.** Duty of care, provide work
   - **B.** Duty to care, union membership
   - **C.** Safe system of work, right to know when employees intend to take leave
   - **D.** Payment of income, payment of expenses

7. Which body enforces industrial relations legislation, including breaches of laws?
   - **A.** Fair Work Commission
   - **B.** The Supreme Court
   - **C.** The Federal Court
   - **D.** The Human Rights Commission

8. What are two of the most significant influences on changing work patterns?
   - **A.** Reduced participation rates for women and a lower average retirement age
   - **B.** Career flexibility and early retirement
   - **C.** Ageing workforce and job mobility
   - **D.** Increased participation rate for women and increased retirement rates

9. Over the last few decades, global competition has led to which of the following?
   - **A.** Growth of unsafe work places where workers are often paid below minimum wages
   - **B.** Increased labour costs to 70 per cent of costs
   - **C.** Greater exploitation of child labour by Australian businesses as a response to consumer pressure
   - **D.** Fewer competitive pressures to manage HRM

10. Ethical Clothing Australia is focused on which of the following?
   - **A.** Ensuring all companies pay the same wage rates
   - **B.** Ensuring all companies support financially viable and ethical practices
   - **C.** Ensuring all companies use accreditation processes for staff
   - **D.** Encouraging textile, clothing and footwear businesses to seek accreditation from them to ensure that they comply with transparent and legal supply chains.

Exercise 2: Exam practice questions

Question 1 (5 marks)

a. **Identify** TWO stakeholders in human resource management. **(2 marks)**

b. **Describe** how these stakeholders influence human resource management. **(3 marks)**

Question 2 (4 marks)

Distinguish between work health and safety and worker's compensation and their influence on human resource management.

Question 3 (4 marks)

How can social influences affect human resource management?

Question 4 (5 marks)

Evaluate the role of ethics and corporate social responsibility in human resource management.

Question 5 (5 marks)

Analyse the influence of government in human resource management.

Question 6 (5 marks)

Critically analyse the changing role of anti–discrimination and equal employment opportunity in human resource management.

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19 Processes of human resource management

19.1 Overview

LEARNING SEQUENCE

19.1 Overview
19.2 Acquisition
19.3 Development
19.4 Maintenance
19.5 Separation
19.6 Review

19.1.1 Introduction

Human resource management is focused on acquiring, developing, maintaining and managing staff productively to achieve the business's goals. This involves managing the relationship between employer and employees effectively to develop and retain talented, competent, productive employees. Employees who feel committed to the business are empowered to respond quickly and positively to change.

Human resource management also involves managing the separation of staff, both voluntary and involuntary, in an ethical, transparent and fair manner, which will also assist in maintaining trust and commitment of remaining staff.

The four main human resource (HR) cycle/staffing process are:

- **acquisition**
- **development**
- **maintenance**
- **separation**.

The four main human resource elements are summarised in figure 19.1.

Managing the processes of human resources from a strategic view ensures that the business considers the quantity and quality of its staffing requirements. In some cases these processes, especially acquisition and development, may be outsourced.

Stakeholders, in particular employers and employees (and their representatives), will have a prominent role in human resource processes. The current legal framework will directly affect human resources processes, including the employment contract and the related work health and safety and workers' compensation, as well as economic, technological and social aspects of human resources.

Strategies in human resource management, such as recruitment, training and development, and rewards, will also impact all of the human resource processes.

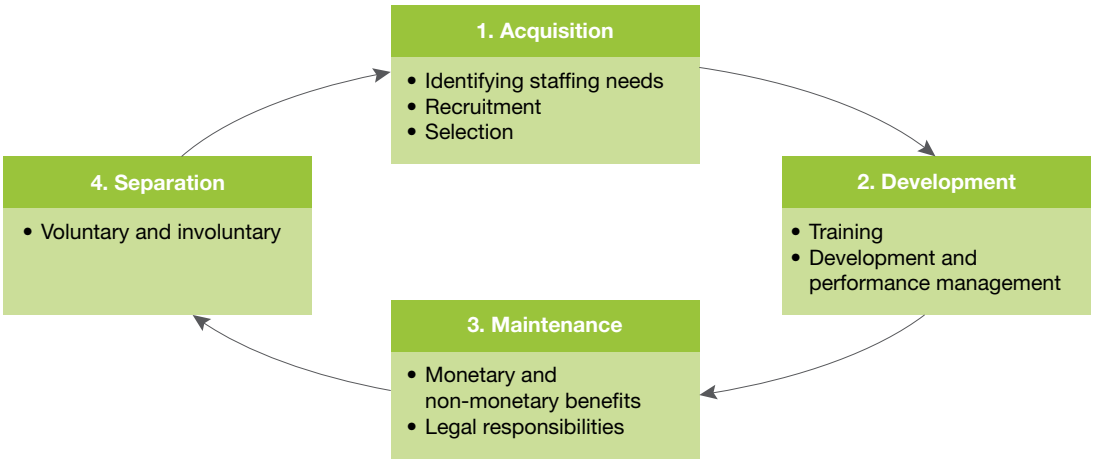
acquisition the process of attracting and recruiting the right staff for roles in a business

development refers to enhancing the skills of the employee in line with the changing and future needs of the organisation

maintenance the process of managing the needs of staff for health and safety, industrial relations and legal responsibilities, including compensation and benefits, of all staff

separation the process of employees leaving voluntarily or through dismissal or retrenchment processes

FIGURE 19.1 The four main elements of the human resource cycle/staffing process



The effectiveness of human resources management in areas such as staff turnover, absenteeism, levels of disputation and worker satisfaction is directly aligned with the way in which acquisition, development, maintenance and separation are dealt with in the workplace.

on Resources

Digital document Key terms glossary (doc-35674)
Exam question booklet Chapter 19 Exam question booklet (eqb-0041)

19.2 Acquisition

SYLLABUS LINK In this subtopic you will learn about how the process of acquisition occurs in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

19.2.1 Introduction

Acquiring the right staff is a critical process in managing human resource management processes. Acquisition involves analysing:

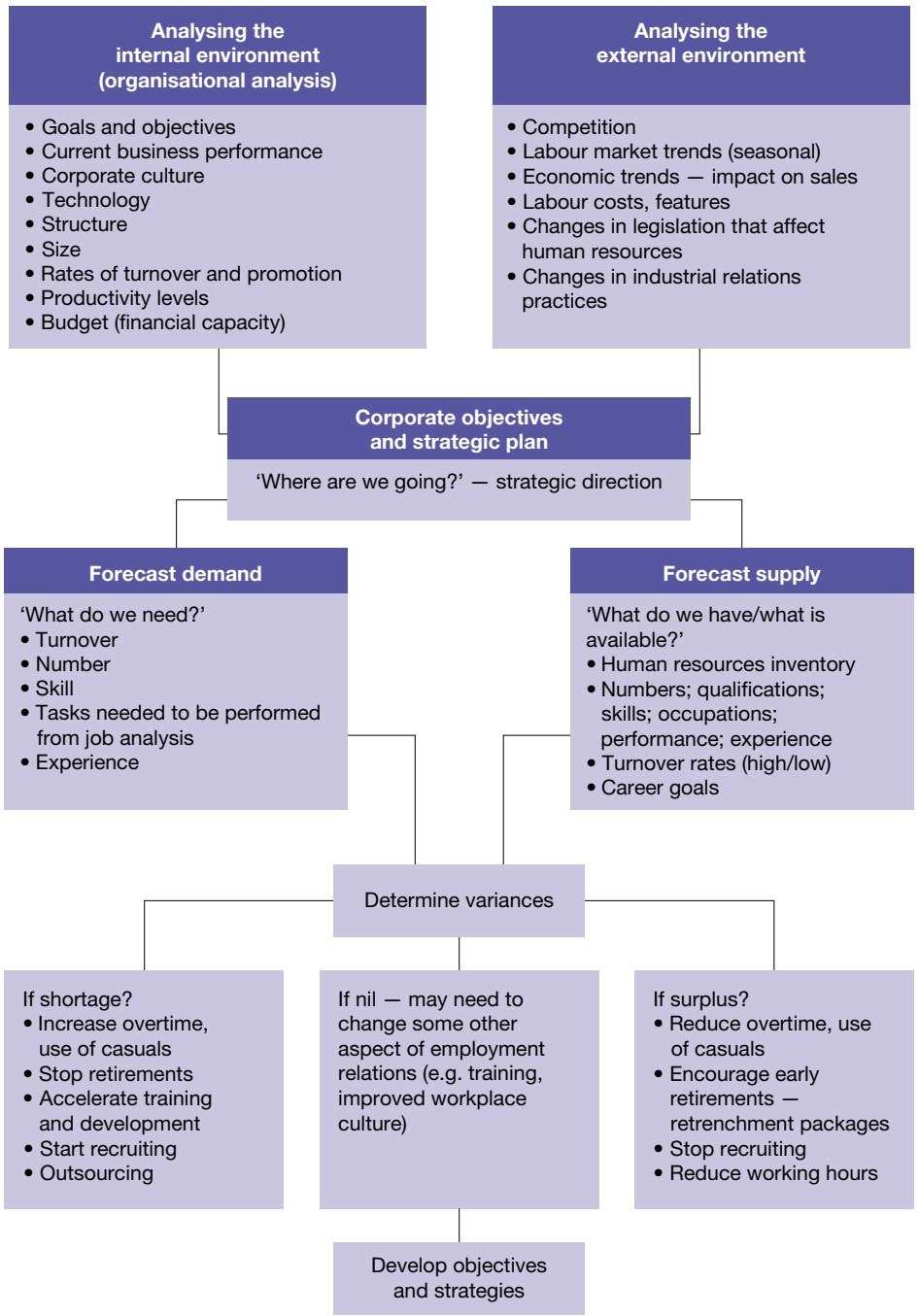
- *the internal environment* — particularly the business's goals and culture. The focus may be on cost containment, growth, downsizing, improved customer service or quality, or other internal goals. This influences the demand for specific skills now and in the future, and will help define the types of staff who will be a good fit for the organisational culture
- *the external environment* — including economic conditions, competition, technology, and legal, political and social factors.

BizFACT

The threat of labour shortages due to the ageing population is increasing the need for businesses to develop more part-time and flexible options for older staff keen to continue working.

Once the needs have been determined, options may be considered. These may include managing for a shortage or surplus of staff. Other options to strategically develop elements of the human resource plan are shown in figure 19.2.

FIGURE 19.2 Acquiring the right staff is a critical process in human resource management. It requires an analysis of the internal and external environment to determine the needs of the business.



Job analysis and job design are required to meet the needs of new positions. These are undertaken through staff interviews, observations, and reports from performance appraisals and evaluations. Job specifications and descriptions can then be developed and prepared for applications through external or internal recruitment.

SNAPSHOT

Case study: Job design for motivation

In the past, job specialisation — where production was broken down into distinct tasks that were performed by individual employees — often resulted in employee boredom and dissatisfaction. To counter this effect, three job design approaches have been used based on intrinsic rewards — the good feeling that one gets from doing something well.



1. *Job rotation:* employees switch, for a period of time, from one job to another. This provides variety and gives employees a more comprehensive view of the business or the production process.
2. *Job enlargement:* employees are given more things to do within the same job. This provides job variety and a greater challenge for employees.
3. *Job enrichment:* employees are given more control and independence over how they do their work. This makes the job more interesting and challenging and provides motivating opportunities for self-satisfaction.

19.2.2 Recruitment, selection and placement

Recruitment is the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost. **Employee selection** involves gathering information about each applicant and using that information to choose the most appropriate applicant.

Effective recruitment and employee selection involves:

- evaluating and hiring qualified job applicants who are motivated and have values and goals aligned with the business and its culture
- a fair, non-discriminatory and legally compliant selection policy and process
- giving applicants a realistic understanding of their job description and responsibilities
- using strategies that will prove useful for later selection and **placement** decisions. Smart businesses are using tools to identify gaps in skills and recruiting strategically to fill these gaps
- using strategies that are aligned with other human resource strategies and the business's needs. If the business is seeking to increase gender equity, there should be female representation on the selection panel, equitable remuneration and benefit packages, and training and promotion opportunities.

recruitment the process of finding and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost

employee selection involves gathering information about each applicant for a position, then using that information to choose the most appropriate applicant

placement involves locating the employee in a position that best utilises the skills of the individual to meet the needs of the business

SNAPSHOT

Case study: SEEK provides online recruitment services

SEEK is a public company operating a global online employment marketplace with a presence in 18 countries including Australia, New Zealand, China and across South-East Asia and Latin America. The business uses technology, data and artificial intelligence to meet the needs of job seekers and employers and support the matching of candidates to employers.



SEEK was founded in 1997 by Andrew Bassat, Paul Bassat and Matthew Rockman. The website was launched the following year, and

was an online version of the employment advertisements found in newspapers. SEEK has now grown to be one of the world's largest online recruitment agencies, employing 1000 people in Australia and over 10 000 people around the world. It has relationships with more than 215 million job candidates and over 1 million employers.

Allowing job candidates to create a profile on its website so that they can be contacted with opportunities from prospective employers, SEEK also provides job recommendations. Job adverts become visible when applicants search for a vacancy on SEEK, and are also matched and sent to the email inboxes of relevant candidates who have opted in to receive job alerts. Candidates who may not be actively applying for roles will also have job ads recommended to them.

Employers who have registered an employer account and who post job ads on the website can search the SEEK profiles to find relevant candidates for advertised positions. The database can be searched based on specific parameters; for example, role title, skills and/or location.

Resources

Weblink SEEK

KEY IDEAS

- The major elements of human resource management are: acquisition, development, maintenance and separation.
- A strategic approach to human resource management is proactive, considers the short- and long-term business needs, and uses a systematic approach that integrates all the human resource strategies to achieve the business goals.
- Acquisition involves analysing the internal and external environment of a business.
- An effective induction program is carefully planned to introduce a new employee to the job, their co-workers, the business and its culture.
- Recruitment involves locating and attracting the right quantity and quality of staff to apply for employment vacancies.
- Employee selection involves gathering information about each applicant and using that information to choose the most appropriate applicant.
- Placement involves locating the employee in a position that best utilises their skills to meet the needs of the business.

19.2 Activities

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19.2 Quick quiz	19.2 Exercise	19.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 5, 6, 7, 9	3, 4	8

19.2 Exercise

Revision

1. **Identify** the four elements of the human resource cycle/staffing process.
2. **What** are the main elements of the acquisition process?

3. **Distinguish** between selection and placement.
4. **Why** is induction necessary for all employees new to a business?
5. **Recommend** the strategies a human resource manager can use to help motivate and retain talented staff.
6. Use the **SEEK** website to find hints for applicants preparing for and attending an interview. **List** 10 hints for applicants to assist them to succeed at an interview.

Extension

7. Read the 'Job design for motivation' case study. Define the term 'job design' and **outline** one example of how a job design may be carried out.
8. Project into the role of a human resource manager and **construct** a PowerPoint presentation that identifies the key focus of the human resource cycle/staffing process.
9. The manager at Justin's Cycles has recognised the importance of induction in business. **Outline** the steps that you would recommend in the development of this new proposed induction process.

19.2 Exam questions

Question 1 (2 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q23b

A business has been rapidly expanding and requires additional staff.

Outline an issue that could arise during the acquisition process.

Question 2 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q2

Which of the following occurs during the acquisition stage of the human resources management process?

A. Training
B. Induction
C. Developing a job description
D. Conducting performance management

Question 3 (2 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q24a

TextMore is a global communications business that is facing increased competition. Management has decided to reduce the size of its factory workforce by 25% but also employ more information technology (IT) specialists.

Identify the TWO human resource processes that will be used in this situation.

Question 4 (1 mark)

Which of the following is a part of the acquisition process of human resource management?

A. On the job training
B. Induction and orientation
C. Promotion opportunities
D. Rewarding effort

Question 5 (4 marks)

Herman's Head Hunters (HHH) offers its services to help businesses in the acquisition process of human resource management.

Describe the services that HHH might provide in the acquisition process.

More exam questions are available in your learnON title.

19.3 Development

SYLLABUS LINK In this subtopic you will learn about how the process of development occurs in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

19.3.1 Introduction

Effective development programs ensure that experienced and talented staff are retained. They enhance employees' motivation and commitment to the business through promotion opportunities over the longer term. Research shows that employees who feel competent in performing their jobs and are recognised for their achievements are more motivated and satisfied at work. They achieve higher levels of performance.

Training and development needs change as an employee's career develops. In the early stages, employees may focus on gaining qualifications. As they move from one employer to another, younger employees focus on experiencing a variety of roles to determine their interests and talents. Later, the development of specialist or managerial competencies may become important as employees move into senior positions. Talented staff may need to be fast-tracked. For employees over 40, the focus may be on upgrading knowledge, mentoring or training, managing work–life balance and transition to retirement planning.

BizFACT

Today, many enterprise agreements focus on improving the functional flexibility of the workforce through multiskilling, job rotation, removal of restrictive work practices, reductions in work classifications and demarcations, job enlargement, and job enrichment. Ongoing training and development are key ingredients in this process.

Development focuses on enhancing the skills of the employee through:

- further professional learning
- mentoring or coaching
- performance appraisal and management to allow them to take advantage of opportunities to develop a career with the business.

A major role of the human resource manager is to establish effective training and development programs, train managers to implement them, and then evaluate training programs to determine whether performance has improved as a result of these programs.

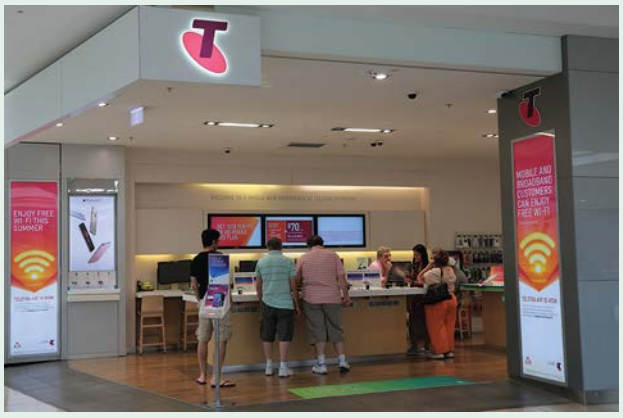
19.3.2 Induction

An effective induction program is carefully planned to introduce a new employee to the job, their co-workers, the business and its culture. Supervisors, co-workers and the human resource department (if a larger business) may be involved in the process. Most employees who leave a business depart in the first three months; therefore, the need for support is greatest when an employee is in a new job. A well-prepared induction program:

- gives employees a positive attitude to the job and the business
- builds a new employee's confidence in the job
- stresses the major safety policies and procedures, and explains their application
- helps establish good working relationships with co-workers and supervisors.

SNAPSHOT

Case study: Telstra turns to TOBI



Telstra retail stores are located in shopping centres all over Australia and are a major setting for interaction between customers and the telecommunications company. People come into the stores to purchase new equipment and to solve questions relating to their existing Telstra products and services. The retail workers employed in these stores need to have expertise in a wide variety of areas of technology to be able to assist customers with the broad range of issues they may bring to these stores.

When Telstra was seeking to implement a new induction program for these workers, it approached the training and educational company Be Learning to assist in the development of such a program. The result was the Telstra OnBoarding & Induction program, known as TOBI. TOBI is a 90-day learning app that is provided to all new employees to teach them the skills necessary to work successfully in the Telstra retail network.

The app provides a one-stop dashboard that allows workers to track their own journey through the induction program. The first 30 days is directed learning that takes new employees through all the essentials of the job. The remaining 60 days are learner initiated, allowing the employee to access elements such video and games, as well as on-the-job activities to broaden their experience and deliver highly competent sales consultants.

19.3.3 Training

The aim of training is to seek a long-term change in employees' skills, knowledge, attitudes and behaviour in order to improve work performance in the business. It is essential in overcoming business weaknesses, building on strengths and maintaining staff commitment. A focus on acquiring new skills and knowledge helps a business adapt to change and stay ahead of the competition.

FIGURE 19.3 Training keeps businesses competitive. Multiskilled employees are better able to adapt to a rapidly changing technological environment, are more productive, and gain the opportunity for promotion.



Most businesses today offer training in some form, whether as a requirement for competency in the role or as a tool to develop and expand workers' skills. Around half of employees who have worked for their employer for more than one year receive some kind of education or formal training. The majority of employees who attend a formal course or study for an educational qualification receive some assistance from their employer.

A business's ability to remain competitive can be affected by the extent of training it offers. A lack of training, for example, may be damaging in the long run because it could result in higher turnover rates as staff seek development in other businesses.

Benefits of training for employees:

- Opportunity for promotion and self-improvement
- Improved job satisfaction through better job performance
- A challenge — the chance to learn new things
- Adaptability — greater ability to adapt to and cope with changes

Benefits of training for the business:

- Higher productivity through better job performance and more efficient use of human resources
- Goals and objectives more effectively met
- Reduced costs due to less labour turnover and absenteeism, and fewer errors and accidents
- A more capable, 'mobile' workforce

The key features of an effective training program include the following.

Step 1

Assess the needs:

- of the individual (skills, knowledge, attitudes, both long and short term)
- of the job (competencies required)
- of the business (for example, culture, goals, standards, service levels).

Step 2

Determine the objectives of the training program for the business, job and individual. Management input and support at this stage is critical to a successful training program.

Step 3

Consider the internal and external influences. Internal influences include the attitude of employees to training, staffing, and financial and physical resources available to operate the program. External influences include any new research on relevant training issues and government programs or support available for training.

Step 4

Determine the process — that is:

- the content of the training program
- the learning principles to be applied, including participation, repetition, demonstration and feedback
- the learning methods to be applied, such as simulation training, lectures, online modules
- the location of the training program, whether on-site, off-site or online
- the participants involved — employees, supervisors, human resource manager, external consultants.

Step 5

Evaluate the training program. Strategies include tests and surveys, both prior to training and after training; performance appraisal; observation; benchmarking of key indicators, such as defects, customer complaints and accident rates. The training program can be evaluated over time in terms of the changes in key indicators, including cost of sales, sales volumes and labour turnover.

BizFACT

The development of soft skills (non-technical skills that apply in the workplace) is seen as the key to an employee's future career. These skills are often implied but many employers expect them to be displayed in various contexts. These soft skills include listening, emotional intelligence, adaptability, communication, teamwork, interaction, creativity, problem solving and critical thinking.

BizFACT

Training at the communications company Motorola is high on the agenda. Every Motorola employee must complete at least 40 hours of training a year.

19.3.4 Organisational development

Today, organisational structures are less hierarchical and flatter in structure. Team- and project-based structures, some even virtual, are widely used. Businesses with flatter structures benefit from employees' ability to develop shared ideas and solutions to problems. It can improve efficiency, effectiveness and response to customer needs.

Flatter structures may have improved employee autonomy and efficiency; however, they have also reduced promotional opportunities. Human resource managers, therefore, need to use strategies to help motivate and retain talented staff. Strategies can include:

- **job enlargement** — increasing the breadth of tasks in a job
- **job rotation** (multiskilling) — moving staff from one task to another over a period of time
- **job enrichment** — increasing the responsibilities of a staff member
- **job sharing** — where two people share the same job
- self-managing teams — teams in which roles and decisions are determined by their members
- mentoring and coaching — where a leader or more experienced member of staff provides advice and support to another person developing skills in the area.

job enlargement involves increasing the breadth of tasks in a job

job rotation involves moving staff from one task to another over a period of time in order to multiskill employees

job enrichment involves increasing the responsibilities of a staff member

job sharing when two people share the same job

19.3.5 Mentoring and coaching

Mentoring and coaching are increasingly used to motivate and develop staff with leadership potential. Mentoring is a mutually agreed role, which suits experienced staff keen to transfer knowledge and skills through succession planning. It is more focused on building a personal relationship that encompasses the life experience of both parties. Often those being mentored select their mentors and are free to accept or reject the advice offered.

Coaching is focused on improving skills and performance, and on helping individuals manage specific work roles more effectively. Coaches may be provided by the business, or may be sought by those seeking further development.

FIGURE 19.4 Mentoring is a more mutually rewarding personal relationship.



The major differences between mentoring and coaching are illustrated in table 19.1.

TABLE 19.1 Employee participation strategies

	Mentoring	Coaching
Focus	Individual life development, preparation for future roles	Performance enhancement by building skills and capabilities, overcoming weaknesses, resolving specific issues
Role	• Facilitator, guide, based on sharing advice and experience • Personal relationship, more like a friend	• Specific to employee's work function • Assists employee in setting goals and finding solutions
Function	Provide advice that may assist in improving the way someone manages issues and situations	Share skills, knowledge, styles and techniques that are relevant to employee needs
Time frame	No time frame	Specific time frame
Structure	Unstructured	More structured
Benefits	• Individual, through personal growth, potential improvement in performance • May also benefit business • Enhances morale	• Business, through improved teamwork, performance and productivity • May enhance morale

19.3.6 Performance appraisal

Performance appraisal is a systematic process of analysing and evaluating employee performance for strengths, weaknesses and opportunities for development. It is also used to assess an employee's suitability for promotion (future leader or manager) and their potential value to the business's success. A wide range of tools are available to evaluate employee performance, and many businesses use a mix of strategies for different circumstances and levels of seniority.

Common methods of appraisal

The following are some of the commonly used techniques for carrying out appraisals.

- **Essay method.** A manager keeps a journal on each employee being appraised. Notes may be restricted to specific aspects of job performance, such as customer service, sales, personal presentation and cash register use.
- **Critical incident method.** This is similar to the essay method except that the manager records only exceptionally good or bad aspects of work performance.
- **Comparison method.** Each employee is ranked according to a list of predetermined performance criteria. This method often incorporates statistical values as a means of measurement. For example, a rating scale of 1 to 5 may be employed (1 being poor and 5 being excellent). This scale may be used to assess knowledge, speed, accuracy, communication, interpersonal skills, oral and written skills, personal presentation and administration techniques

If most employees continually perform below expectations, the business's recruitment and selection process may need to be changed, or extra training and development may be required. Although many managers are uncomfortable with the idea of evaluating employees, effective performance appraisal is a crucial function of good management.

performance appraisal a process of assessing the performance of an employee, generally against a set of criteria or standards

No matter which appraisal technique is used, the results should be discussed with the employee as soon as possible. The manager should explain both the positive and the negative aspects of an employee's performance, encourage the employee to continue with his or her positive behaviour, and let the employee know what to do to be recognised as a more productive employee in the future. The manager will also be able to identify training needs for the employee so that he or she can improve in areas that may be lacking. Without this performance feedback, performance appraisals are a pointless exercise.

Performance appraisal facilitates communication and allows positive relationships to develop between management and employees. Feedback can help employees to improve their performance. However, the performance appraisal process can be time consuming, particularly if the cycle becomes shorter (such as monthly or weekly). Performance appraisal can be stressful for both managers and employees.

Employees are more likely to value a performance appraisal if they are given a chance to discuss their performance and to challenge their evaluation. When employees believe the process is constructive and fair, and will help them improve their future performance, it will be perceived as a more useful experience. This needs to be factored into the performance appraisal system.

FIGURE 19.5 Employees value the opportunity to challenge and discuss aspects of a performance appraisal.



KEY IDEAS

- Development involves enhancing the skills of the employee through training, mentoring, coaching and performance management so they develop a career with the business.
- Effective induction and training equips a new employee with the skills to carry out their job and work effectively with co-workers within the business and its culture.
- Ongoing training should be part of every workplace. Changes in the business environment, including new technology and global competition, are increasing the need for training.
- Businesses are using flatter structures to improve efficiency and competitiveness by creating more opportunities for employees to innovate and participate in solving business problems.
- Organisational development involves developing strategies such as job rotation to increase employee participation, motivation and retention.
- Performance appraisal is used to evaluate employee performance, and identify areas for mentoring, coaching, leadership development or performance management to enable the employee to contribute most effectively to a business's success.

19.3 Activities

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19.3 Quick quiz on | **19.3 Exercise** | **19.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 5, 6, 8	2, 4, 7, 10, 11, 12	9

19.3 Exercise

Revision

1. **Clarify** the benefits of training and development.
2. In small groups, **construct** a table listing all the forms of training and development a business can use and the advantages and disadvantages of each approach.
3. **Outline** the strategies a human resource manager can use to help motivate and retain talented staff.
4. **a.** Define the term 'performance appraisal'.
   b. How can performance appraisals assist in the development of employees?
   c. Why must this process be managed in a constructive manner?
   d. Why is performance review useful for employers in assessing the effectiveness of its management of human resources?
5. **Identify** and **describe** the forms of performance appraisal that you would prefer used on yourself in a workplace. Justify your choice.

Read the 'Telstra turns to TOBI' case study and answer questions 6 to 8.

6. **What** skills do the workers at Telstra retail stores need?
7. **How** did Telstra manage the induction process for its retail workers?
8. **Outline** the Telstra OnBoarding & Induction (TOBI) program and its use of a learning app.

Extension

9. Imagine you are an employee of a large restaurant, working at night while studying during the day. The essay method appraisal from an anonymous co-worker is critical of your work effort and skills, and states you lack interest in customer needs.
   a. **Evaluate** the value of an essay method feedback system and its likely impact on your performance.
   b. Justify an alternative method.
   c. Consider the value of your school report as an appraisal tool of your performance. Discuss your conclusions with a classmate.
10. **Construct** a speech that you would make as the human resources manager of Solar Structures Pty Ltd where you focus on the need to develop a stronger learning culture within the business.
11. You have been contracted to investigate the high rate of staff turnover at Solar Structures Pty Ltd. What process would you use to investigate this issue? **Recommend** some changes you would make to assist the firm in reducing staff turnover.
12. **Justify** the system you would implement in a hospital to ensure effective performance appraisals of the nursing staff.

19.3 Exam questions

Question 1 (1 mark)

Which of the following is a benefit of the development process in human resource management for employees?

A. Time consuming
B. Reduces staff turnover
C. Creates independence
D. Builds loyalty

Question 2 (1 mark)

Which of the following is a benefit of the development process in human resource management for employers?

A. Reduces staff turnover
B. Increases job satisfaction
C. Helps with promotion
D. Increases staff turnover

Question 3 (2 marks)

Outline the advantages and disadvantages of in-house training as a method for development of human resources.

Question 4 (4 marks)

Heats Discount Store has 21 permanent and 25 casual employees. The manager wishes to improve customer service and wants all staff to know about the products sold by Heats. The manager states that development of human resources is essential for Heats.

Explain the benefits of the processes of development for the employees and employer of Heats.

More exam questions are available in your learnON title.

19.4 Maintenance

SYLLABUS LINK In this subtopic you will learn about how the process of maintenance occurs in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

19.4.1 Introduction

In human resource management, maintenance focuses on the processes needed to retain staff and manage their wellbeing at work. Maintenance of staff involves looking after staff wellbeing, safety and health, managing communications effectively, and complying with industrial agreements and legal responsibilities.

FIGURE 19.6 Family-friendly programs such as telecommuting, part-time work and flexible working hours support the work–life balance of employees.



Staff wellbeing is maximised through encouraging staff to participate in decision making, and giving employees some control over their work lives. A range of employee participation strategies, including involvement in teams, collective bargaining, workplace surveys and activities, fosters involvement in decision making. Effective communication strategies support employee participation and a strong workplace culture. Employees also have the right to a healthy and safe work environment, where work-related stress and unproductive conflict are minimised.

Offering family-friendly programs that support work–life balance is critical in workplaces where staff are increasingly asked to do 'more with less'. These include flexible job roles such as job sharing, multiskilling, telecommuting, part-time work and flexible working hours to suit family needs. Employees also expect that industrial agreements, and payroll obligations and benefits are met.

BizFACT

Many larger workplaces also recognise the impact of personal problems on employee performance and wellbeing. Work-based programs, such as the Employee Assistance Program (EAP) schemes, are widely available to provide additional support for staff and their family members with problems such as conflicts with others at work, family or marital difficulties, substance abuse, gambling problems, anxiety or depression. Using this service is just a matter of a phone call, and it is confidential.

19.4.2 Communication and workplace culture

Effective workplace relationships depend heavily on the strength of a business's communications systems. Poor communication is often reflected in workplace conflict and high turnover rates.

Common methods of communication include regular team meetings between managers, or supervisors, and employees; staff bulletins and newsletters; staff seminars; social functions; suggestion boxes and staff surveys; and email and intranet.

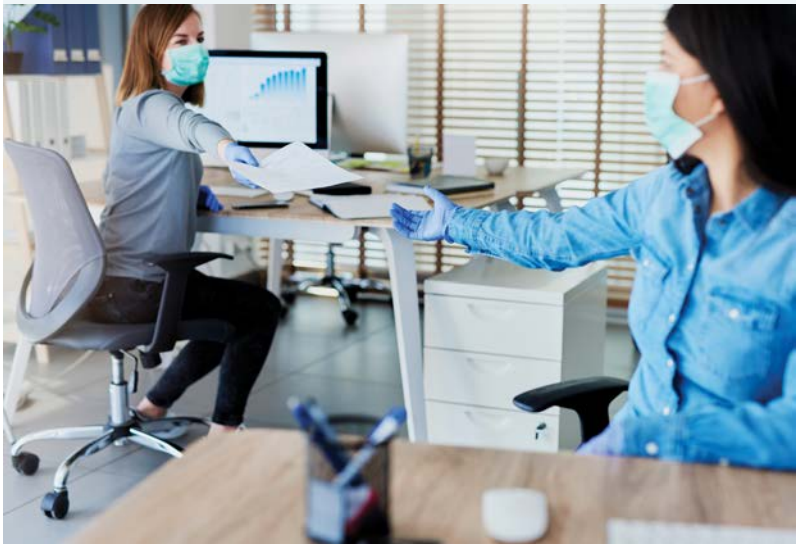
Email is often criticised for being a source of misunderstandings and tension if protocols are not established for constructive communications and timelines for feedback. Expectations that staff will attend to emails at home is a common source of workplace conflict, which needs to be managed carefully to avoid burnout of staff and grievances developing.

Strategies that focus on building trust and direct communication between people are critical in preventing conflict and escalating issues. As well, such strategies help in building a positive workplace culture. Recognition of staff achievements is critical in building a positive workplace culture. Communications with employees should always be constructive, even when there are problems with employees.

The need for social distancing in a post COVID-19 work environment has seen a shift in office layouts and the need to minimise risk. Workers are being encouraged to work from home where they can. If this is not possible, there are a number of strategies businesses can use, including:

- ensuring people with symptoms of COVID-19 do not come to work
- separating workers into dedicated teams and having them work the same shift or work in a particular area to limit interaction with others
- screening workers
- maintaining physical distancing by changing the physical office layout, modifying workflows so that people do not spend time in close proximity in kitchens and meeting rooms, staggering start and finish times, restricting access to essential visitors only
- practising good personal hygiene (including hand washing)
- engaging in routine cleaning and disinfection of surfaces
- providing personal protective equipment (PPE) where appropriate
- contact tracing
- signage and posters to remind workers of the effects of the virus
- minimising opportunities for large gatherings.

FIGURE 19.7 Office layouts can be designed to create spaces for people to socially isolate and reduce the opportunites for close contact and the risk of spreading COVID-19.



This will require management to be more creative in including workers in more traditional team meetings and thus encourage effective communication.

19.4.3 Employee participation

The nature of workplace communication is changing with the increasing use of email and increased opportunities for employee participation. Firms encourage employee participation to improve communication, empower employees and develop their commitment to improving quality and efficiency. Employees are being trained to make some decisions 'on the spot', either to solve problems or provide incentives to retain customers, as customers demand quicker and more efficient service.

FIGURE 19.8 Employee participation provides a constructive path to business success.



BizFACT

The death of the owner of C-Mac industries, a sheet metal fabricating firm in Sydney's western suburbs, resulted in employees facing the prospect of the business closing permanently. Staff kept the business operating by successfully undertaking to purchase it rather than facing the uncertainty of finding an outside buyer.

Source: Employee Ownership Australia and New Zealand

Businesses benefit from employee experience and knowledge on the job, and improvements they suggest are often critical to a business's competitiveness and success.

The value and effectiveness of employee participation depends on the training, knowledge and skills of the employees involved. The use of suggestion boxes is often included as an example of employee participation. However, more effective participation is fostered through regular team meetings/briefings to discuss customer feedback, company trends and issues — these build a sense of shared purpose and company identity.

A range of employee participation strategies are described in table 19.2.

TABLE 19.2 Employee participation strategies

Participation strategy	Explanation
Participation through membership of the board of directors	This strategy allows an employee or senior employee to represent staff on the board. This strategy presents conflicts of interest for the employee, who often becomes alienated from other employees.
Participation through ownership	Employees buy shares in their company, which may result in increased commitment. However, ownership and participation involve different objectives and may lead to a conflict of interest, particularly as ownership increases in scale.
Joint consultative committees	Also called works committees, these are formally established groups consisting of employees and management representatives, and may or may not include union representatives. Their original purpose was to provide management with the views of employees on a range of issues, enhance communication and improve efficiency and productivity. In NSW, these have been mandatory for larger workplaces for work health and safety (WHS).
Participation in collective bargaining	It is a requirement that a majority of employees be involved in developing an enterprise agreement. The advantage is that under good faith bargaining principles all parties are required to make an effort to resolve issues through negotiation and conciliation. This ensures that employees and employers have clear opportunities to learn from each other's experience and to negotiate outcomes beneficial for both groups.
Team briefings	Teams provide an excellent opportunity for employees to share knowledge, skills and experience; to find solutions to problems and develop innovations.
Employee surveys and feedback from performance interviews	Many businesses use a range of surveys and reports from staff to seek valued feedback on ways to improve business performance.

19.4.4 Benefits

Benefits are often a litmus test of the workplace culture as they are available to all staff. They may be monetary in value or non-monetary, and the extent of benefits available will reflect the resources of the business and the nature of its activities.

SNAPSHOT

Case study: Superannuation — money for later, but paid for now



Under the federal Superannuation Guarantee scheme, all employers must make a financial contribution to a fund for employees' superannuation (otherwise known as super) that employees can access when they retire. Employers are not required to provide superannuation for employees aged under 18 years (unless they work more than 30 hours a week), employees paid less than $450 per month and employees working outside Australia.The employer's main obligation is to make a financial contribution — from 1 July 2014, 9.5 per cent of an employee's earnings for their ordinary hours of work — to their employees' superannuation account. As with taxation, employers are required to keep records of all superannuation-related transactions, including payments contributed, payroll and employee records, and the level of entitlement of each employee.

All employers are also required to pay superannuation for employees who are aged 18 years or older, and who earn a minimum of $450 (before taxation) per month as a casual, part-time or full-time employee.

Typical benefits include flexible working arrangements, paid training opportunities, travel allowances, health insurance, subsidised gym membership, housing and company car.

Businesses carefully consider the value of these benefits in terms of retention of staff and workplace culture, as they are expensive and some attract an employer-paid **fringe benefits tax (FBT)**. Benefits that may be considered for FBT include airline transport, expense accounts, board and accommodation, housing loans, living-away-from-home allowance, car parking, property and entertainment allowance.

Some examples of workplace benefits are shown in table 19.3.

TABLE 19.3 Examples of workplace benefits in three Australian businesses

Rio Tinto's Iron Ore	Orica	Westfield Australia
• Residential allowances • Fly-in, fly-out commuting allowances • Additional superannuation investment choice and insurance benefits • Housing assistance • Salary packaging • Employee incentive scheme • Subsidised gym membership • Savings-related share option scheme • Relocation assistance • Remote area holiday travel allowance • Subsidised private medical insurance • Discount offers from key suppliers	• Flexible working arrangements • Attractive package for health insurance • Insurance discounts • Employee assistance program • Specialist leadership training and development support • Dulux staff card • Novated car leases • Mobile phone plan • Employee share plan • Paid family leave — up to six weeks, some paternity leave • 20 days unpaid leave • Ford car program • 'Dare to Share' charity program	• Regular training packages and programs • Career progression — domestic and international • Sponsor a friend recruitment program • Social club organises activities at a discount, including opera and theatre tickets, fun parks, dinners • Study assistance, online textbooks • Employee assistance program • Salary sacrifice program • Intranet product and service exchange • Business improvement awards

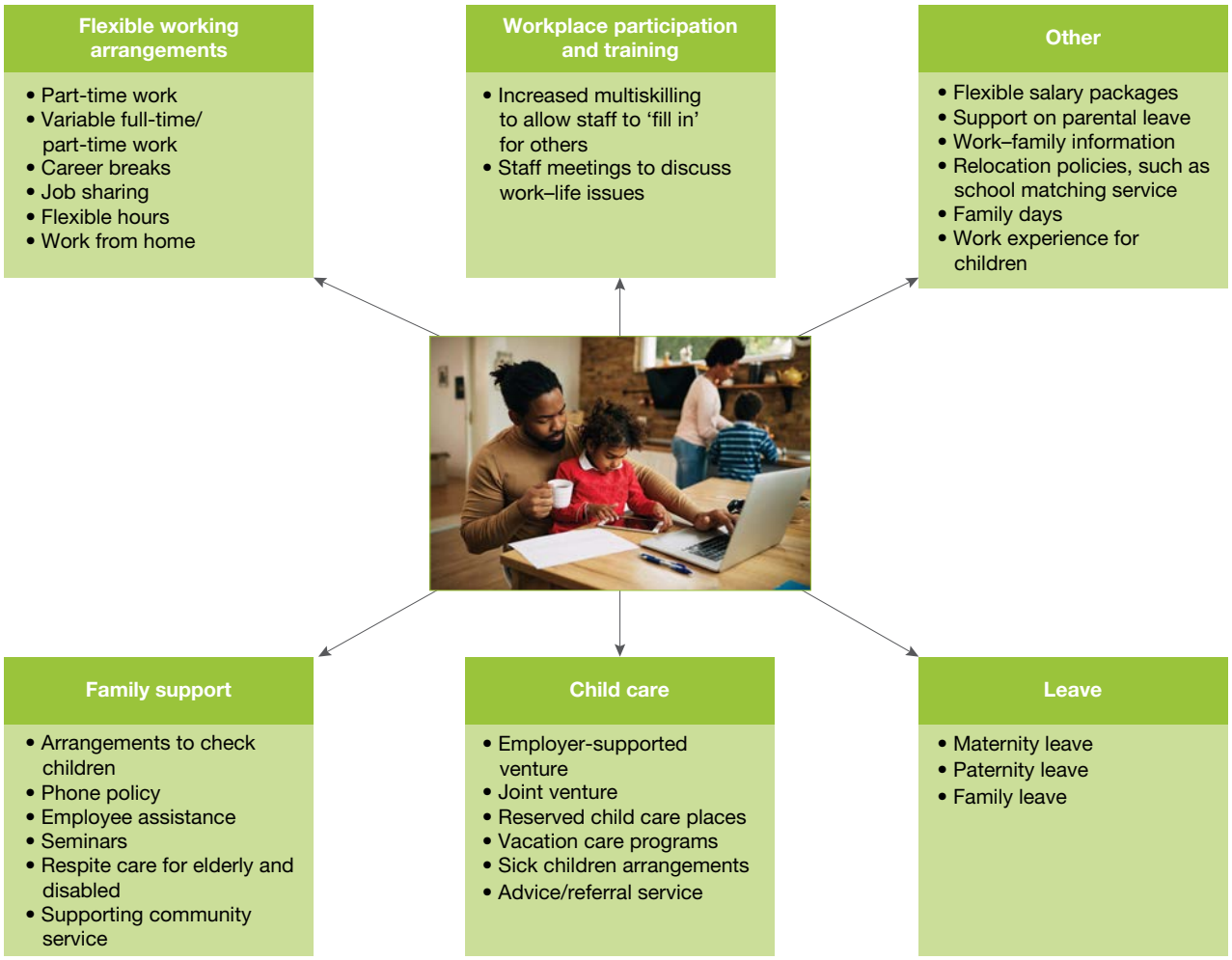
Flexible and family-friendly work arrangements

Around one-third of Australian employees cite a need for work–life balance as a major consideration in future work choices. Employers are responding with more flexible working arrangements to attract and retain talented staff. These arrangements are reflected in the New Employment Standards, and are also a key feature in many industrial agreements today. Typical features of a family-friendly workplace are shown in figure 19.9.

Flexible working conditions allow businesses to work more efficiently, or allowemployees to balance work and family responsibilities more effectively. For example, some employer–employee agreements allow opportunities for home-based work, which gives employees more flexibility during working hours. It is becoming more practical as the electronic methods of communication and technology improve.

fringe benefits tax (FBT) a tax employers must pay on certain benefits they provide to their employees or their employees' associates, such as a family member. It is based on the taxable value of the various fringe benefits provided.

FIGURE 19.9 Features of a family-friendly workplace. Opportunities for home-based work and family-friendly working hours allow employees to balance work and family responsibilities more effectively.



BizFACT

Flexible working hours are a common feature of enterprise agreements and individual contracts. Maxiflex allows employees to build up sufficient hours to take a day off. Employers are usually allowed to nominate the day off. Flexitime allows an employee to nominate start and finish times to suit their needs

Typical flexible working conditions include:

- flexible remuneration (reward) options
- flexible working hours
- flexible study/work arrangements
- career break schemes
- job sharing — involves two employees voluntarily sharing one permanent full-time job. This arrangement has been very popular with women returning to the workforce after having children, but requires commitment and communication to be effective
- work-from-home arrangements (rostered days off, telecommuting, a compressed work week)
- family leave
- part-year work arrangements (often suit competitive sportsmen and women).

Family-friendly programs are effective in retaining staff in the longer term as they recognise the interdependence of work and family life, and reduce problems involved in managing family responsibilities. Employees are able to leave and later re-enter the workforce, thus reducing separation, recruitment and training costs for new employees. Such programs also create a positive image of the firm within the community.

SNAPSHOT

Case study: Are work lives in balance?

It would appear that Australian workers have all of their expectations met, except for one. According to the OECD's *How's Life? 2020* report, Australia performed well in many of the 11 life dimensions that the OECD considers essential to a good life. But it lies below the OECD average in terms of work–life balance: in Australia, 13 per cent of employees work very long hours, above the OECD average of 11 per cent. The more people work, the less time they have to spend on other activities, such as personal care or leisure. In Australia, full-time workers devote 60 per cent of their day on average, or 14.4 hours, to personal care (eating, sleeping, etc.) and leisure (socialising with friends and family, hobbies, games, computer and television use, etc.) — less than the OECD average of 15 hours. Many studies have shown that Australians feel that work frequently interferes with other life activities.

Australia is well behind other countries when it comes to providing employees with work–life balance.



The consequences for workplaces with a low work–life balance include increased staff turnover and stress levels, decreased morale and job satisfaction, and deterioration in health and wellbeing. One way in which businesses can provide work–life balance is to offer flexible conditions. The Australian Public Service has been gradually increasing its workplace flexibility over the past 20 years. In 2017, 41 per cent of male employees and 52 per cent of female employees were accessing flexible work arrangements. The most common types of flexible work arrangements included:

- flexible hours of work — 60 per cent
- part-time work — 31 per cent
- working away from the office — 19 per cent.

It has been shown that flexible work arrangements help reduce unscheduled absences, such as personal leave. The 2020 Public Service employees' census indicated that employees who have access to flexible work arrangements are less likely to take unscheduled personal leave days.

19.4.5 Legal compliance and corporate social responsibility

All employers are required by law to ensure that human resource procedures and policies comply with existing legislation, including anti-discrimination and sex discrimination legislation, WHS taxation, social justice legislation, and industrial relations legislation and agreements.

BizFACT

A female employed by a New South Wales club was awarded $15 000 for sexual harassment she endured from her male supervisor. Despite the fact that the club had policies in place to deal with harassment, these were assessed to not be comprehensive enough to deal with such matters. The club was aware of previous incidents involving the manager, but had not acted upon them thoroughly enough. The club was also criticised for not training its staff in how to deal with issues of harassment and discrimination in the workplace.

Bullying and sexual harassment, along with conflict between employees and high workloads, are major causes of stress at work. These issues are behind high levels of staff stress, absenteeism, turnover, and low productivity and morale. Creating a workplace where staff treat each other in a respectful, professional, fair and considerate manner is essential for employee wellbeing and retention of productive staff.

A major focus of maintenance is for human resource managers to minimise the exposure of the business to risk by implementing a range of proactive and preventative strategies in health and safety, anti-discrimination and conflict resolution. Problems that arise over misconduct in employment relationships, particularly regarding sexual harassment, bullying and discrimination, can be very costly and damaging to the business and destroy individuals.

FIGURE 19.10 Human resource managers may be called on to mediate in employment relationships.



Bullying is common in industries where there are a high number of vulnerable employees such as apprentices, young staff or migrant workers. It can be minimised by:

- providing information about workplace bullying, which covers common forms such as verbal abuse, spreading rumours, exclusion, ignoring someone, physical intimidation or violence, or initiation
- inducting and training employees in company policy, procedures to deal with bullying, and consequences of bullying
- providing training to increase cultural awareness
- promoting a culture that is based on open communication, respect, fairness and trust
- ensuring management is committed to resolving bullying and grievances
- having mentoring or buddy systems for new and young employees
- having a member of staff, appointed by the staff, to handle complaints and grievances.

SNAPSHOT

Case study: Bullying in the workplace

We sometimes think of bullying as being confined to the school yard. Unfortunately, it can also be a serious issue in workplaces.

The more noticeable forms of workplace bullying are intimidation, humiliation, verbal abuse, slamming doors, pushing, touching or fondling, and threatened or actual violence against an employee — in short, any repeated actions likely to generate a risk to a person's health and safety. Australian businesses are paying dearly for bullying in the workplace. Recently, a company was ordered to pay $350 000 to an employee for his medical bills, loss of income, and pain and suffering. As a young apprentice the employee faced continual harassment, including being rolled around the factory inside a large drum, and having grease smeared on parts of his body. The judge found the business instilled a 'culture of intimidation'.

There are also subtle forms of bullying such as excluding or isolating employees, assigning meaningless tasks that are unrelated to the job, deliberately changing work rosters to inconvenience particular employees and intentionally withholding information that is vital for effective workplace performance.

Verbal abuse is the most common form of workplace bullying.



KEY IDEAS

- Maintenance focuses on the processes needed to retain staff and manage their wellbeing at work.
- Staff wellbeing is maximised through encouraging staff to participate in decision making, and giving employees some control over their work lives.
- Effective workplace relationships depend heavily on a business's communications systems. Poor communication is often reflected in workplace conflict and high turnover rates.
- Businesses benefit from employee experience and knowledge on the job, and improvements they suggest are often critical to a business's competitiveness and success.
- Benefits are an integral element in building workplace culture. They may be monetary in value or non-monetary.
- Employers are responding to employees' desire for a work–life balance with more flexible working arrangements.
- An important role of the human resource manager is ensuring the policies comply with legislation including anti-discrimination and sex discrimination legislation, WHS, taxation, social justice legislation and industrial relations legislation and agreements.

19.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. **A downloadable solutions** file is also available in the Resources tab.

19.4 Quick quiz on	19.4 Exercise	19.4 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 5, 11, 12, 14, 15, 16, 17, 21, 22	2, 4, 6, 7, 8, 9, 10, 13, 20, 23	3, 18, 19, 24, 25

19.4 Exercise

Revision

1. **Define** the term 'maintenance'.
2. a. **Propose** and **compare** a list of all the workplace elements that would be effective in maximising staff wellbeing.
   b. **Compare** your list with that of another student for similarities and differences.
3. What are the most common forms of communication used in a workplace? **Evaluate** the importance of each method for effective communication and for building a positive workplace culture.
4. **Discuss** and **justify** the role an intranet can play in improving workplace communications and culture. Identify elements that should be included in a high-quality workplace intranet. Justify your response.
5. **Describe** the benefits of employee participation and team structures for employers.
6. Study table 19.2. As an employee, select the two participation strategies you would like to be involved in. **Justify** your selection.
7. **Distinguish** between monetary and non-monetary benefits.
8. Study table 19.3. **Account** for why these three businesses provide an extensive range of workplace benefits. Share your answer with the class.
9. **Propose** likely benefits to the employer of a family-friendly workplace.
10. **How** do specific human resource strategies, such as employee participation, teamwork, flexible working conditions, training and rewards, benefit both the employee and employer? Present your answer in table format.
11. **Identify** the major legal areas of responsibility for a human resource manager.
12. **Describe** the costs of sexual harassment and bullying in the workplace.
13. In small groups, **propose** strategies businesses need to implement in order to minimise workplace bullying and sexual harassment.

Read the 'Superannuation — money for later, but paid for now' case study and answer questions 14 to 17.

14. **Outline** the requirement of the federal Superannuation Guarantee scheme.
15. **List** the people who are entitled to superannuation payments on their behalf.
16. **Identify** the employer's main obligation to employees.
17. **List** the types of records employers are expected to maintain.

Read the 'Are work lives in balance?' case study and answer questions 18 to 20.

18. **Analyse** whether Australian workers are having their work–life balance expectations met.
19. **Analyse** two consequences of a poor work–life balance for employees.
20. **Explain** how the Australian Public Service provides work arrangements that can contribute to a positive work–life balance.

Read the 'Bullying in the workplace' case study and answer questions 21 and 22.

21. **List** the most common forms of bullying in the workplace.
22. **Describe** the subtle forms of bullying common to some workplaces.

Extension

23. 'The critical issues for human resource managers today are raising productivity, improving customer satisfaction, providing quality products and services, and aligning human resource strategy to business goals.'

Human resource manager at Jack's Candles Ltd

Imagine you are the human resource manager at Jack's Candles Ltd, and **explain** how you would address these issues.

24. Use the internet to research employee share ownership plans (ESOP) in Australia. **Analyse** why ESOPs are less common in Australia than overseas. **Assess** the potential benefits to Australian firms of ESOPs.

25. As CEO of Pets Play, a manufacturer of pet accessories with turnover of $50 million and 150 employees, you are finding it hard to keep your young staff once they begin having families.

a. **Create** a list of family-friendly initiatives you may be able to afford to offer.

b. Explain how four of these initiatives may help you retain staff.

c. **Determine** the processes you would use to become a more family-friendly workplace.

d. Identify three policies a firm could implement to reduce absenteeism. Justify your answer.

e. Propose strategies you could implement to promote your family-friendly initiatives and become an employer of choice.

19.4 Exam questions

Question 1 (6 marks)

Source: HSC 2014 Business Studies Exam, Section II, Q23b

Maintenance is a process of human resource management.

By referring to a specific example, explain how maintenance could be used to improve business performance.

Question 2 (4 marks)

Compare the processes of development and maintenance in the management of human resources.

Question 3 (3 marks)

Assess the importance of maintenance as a part of human resource management

Question 4 (1 mark)

Steven has a well-educated and ambitious staff. Which of the following would be the most appropriate method to assist Steven in the maintenance process of human resource management?

A. Include staff in decision making and control responsibilities
B. Have two-way communication with little delegation
C. Share power and delegate responsibilities
D. Reduce conflicts and centralise responsibility

Question 5 (1 mark)

Helen is the human resource manager in a large business. She is concerned that staff turnover is high. Helen cites the old fashioned ways the business maintains its employees as a reason for the high turnover. Which of the following would be a feature of a more modern maintenance process?

A. Hold formal meetings
B. Use control as a feature of leadership
C. View employees as resources
D. View employees as individuals

More exam questions are available in your learnON title.

19.5 Separation

SYLLABUS LINK In this subtopic you will learn about how the process of separation occurs in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

19.5.1 Introduction

Separation, where an employee leaves a business, may be voluntary or involuntary. Voluntary separation may take the form of resignation, relocation, voluntary **redundancy** or retirement. Involuntary separation may take the form of contract expiry, **retrenchment** or dismissal. To avoid claims of discrimination and adverse effects on the morale and productivity of remaining staff, involuntary separation must be managed carefully and in compliance with legislation, awards and agreements.

Situations where redundancy occurs include closure of the workplace site, completion of the project on which the employee worked, lack of contracts or orders for work, a downturn in demand from customers or a need to reduce staff due to financial difficulties in the business. Documentary evidence would be required for these reasons, for example the company's financial statements.

It is important to consider a range of matters in determining who will be retrenched. These may include length of service, standard of performance, future potential and whether some staff may be willing to leave voluntarily.

FIGURE 19.11 Separation is the end of the employment contract. At this stage the human resource department needs to fulfil all the legal requirements and complete the necessary documentation accurately and speedily.



Notice and leave entitlements given must comply with legislation and industrial agreements. Managers should consult with staff prior to termination and support them with outplacement to ensure a smooth transition that does not adversely affect the remaining employees' morale. It is best to sever staff who are leaving immediately and pay out their notice. It is rare to see retrenched or redundant staff leave cheerfully, even when the separation is handled in a professional and caring manner.

redundancy occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition

retrenchment when a business dismisses an employee because there is not enough work to justify paying him or her

BizFACT

The closure of the car manufacturing industry in Australia resulted in 14 000 job losses nationally. Initial predictions of 27 500 job losses, many in local communities in Victoria and South Australia, did not materialise. An average of 84 per cent of employees gained employment, mostly full time (59 per cent) in manufacturing (35 per cent) and in some cases started their own businesses (6 per cent).

When an employee's employment is terminated, the employer must provide a written statement confirming the termination and date of determination.

Most awards and agreements have common provisions relating to termination, change and redundancy that cover matters including the procedures for retrenchment, amount of notice to be given or pay in lieu of notice and severance pay. These supplement and override legislation if conditions are more favourable.

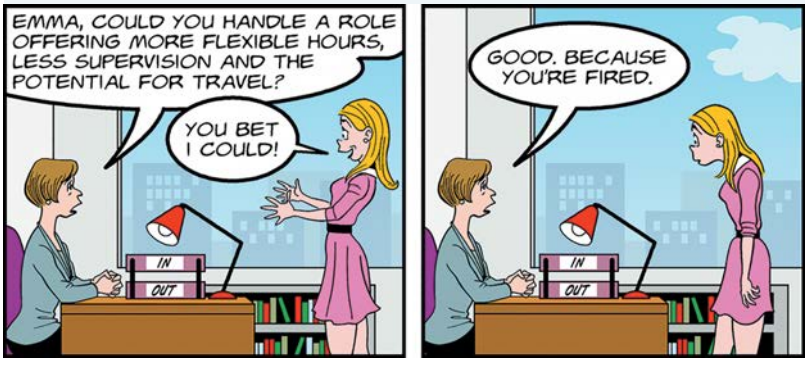
BizFACT

High-earning employees who earn over the threshold, under the Fair Work Act ($153 600 in 2020, annually indexed), do not have access to unfair dismissal laws unless they are covered by a modern award or enterprise agreement when they are dismissed; that is, in terms of undertaking the duties the award covers and their actual classification.

19.5.2 Dismissal

Staff may be dismissed for a number of reasons. Summary dismissal is an instant form of dismissal that applies to employees involved in gross or serious misconduct, such as theft. Termination for misconduct must meet the test of being fair and reasonable, given the circumstances. The Fair Work Commission will generally determine whether the reasons were sound and well founded, and whether the employer had made reasonable efforts to investigate the allegations and allowed the employee the right to respond. If there is any doubt, payment of notice in lieu will generally avoid an unfair dismissal claim for serious misconduct.

FIGURE 19.12 An employment contract is legally binding. Therefore, employers must terminate the contract in a legally compliant manner. Gone are the days when a boss can simply shout 'You're fired!' on a whim. Many colloquialisms are used to describe involuntary termination: 'given the bullet', 'shown the front door', 'fired', 'booted out', 'told to pick up my pay and go', 'no longer required' and 'given an offer I couldn't refuse'. They all have one feature in common: the business requests that the employee leaves the business.



Dismissal can also be based on poor performance or redundancy due to organisational restructuring, a downturn in business or technological change making a job redundant. In recent years, businesses have tried to reduce costs and improve productivity through reducing staff numbers, flattening management structures and making greater use of technology. Widespread restructuring and managerial policies are major factors contributing to industrial disputes and unfair dismissal claims.

BizFACT

Under National Employment Standards entitlements the notice of termination and redundancy pay states that up to 4 weeks' notice of termination (plus an extra week if the employee is over 45 and has been in the job for at least 2 years) and up to 16 weeks redundancy pay must be given

Employers need to prove that they have followed all the processes required before dismissing an employee.

In the case of poor performance, businesses are required to:

- give employees a written warning about their poor performance over a period of time
- give them advice and support so they have the opportunity to improve
- notify employees of the reason for the termination and an opportunity to respond.

In the case of redundancy, the employer may be asked to show that:

- the employee's job was no longer needed; that the redundancy is genuine
- no appropriate work was available elsewhere within the organisation
- the employee was consulted about alternative redeployment options within the business.

19.5.3 Unfair dismissal

Selecting staff for dismissal can be risky and requires awareness of legislation and industrial agreements. Documentation of processes undertaken is also required to avoid claims of **unfair dismissal**.

The Fair Work Commission provides these grounds for unfair dismissal claims for employees covered by the national system.

'An unfair dismissal occurs where an employee makes an unfair dismissal remedy application and Fair Work Commission finds that:

- the employee was dismissed, and
- the dismissal was harsh, unjust or unreasonable, and
- the dismissal was not a case of genuine redundancy.'

Employees are able to claim unfair dismissal if:

- the business has more than 15 employees, either full-time or the equivalent, who have been employed for more than six months. This includes casuals with six months service.
- the processes for dismissal have not been carried out correctly.

unfair dismissal occurs where an employee is dismissed by their employer and they believe the action is harsh, unreasonable or unjust

BizFACT

The Fair Work Commission will judge a claim on whether a termination/dismissal is lawful, harsh, unjust or unreasonable, and will take into account the procedures followed, whether the grounds were reasonable, the circumstances of the business, whether human resources expertise was available, whether the employee was provided opportunities to respond or have a support person, and any other matters the Fair Work Commission deems relevant.

The claim may be resolved through informal conferences, telephone conferences (the most common method) or by a formal hearing. Reinstatement will be the remedy for a claim that is upheld, unless it is not in the interests of either of the parties, in which case compensation may be ordered. A cap of six month pay is the maximum compensation, but most cases would not reach this level.

An employer has the right to object to a claim on the basis that it is vexatious or frivolous, not submitted in an appropriate time frame, not reasonably likely to succeed, not a case of unfair dismissal or that the person making the claim is not eligible.

Businesses can be badly hit by such claims. Many have found the need for a lengthy procedural approach frustrating, particularly the need to give employees time to improve their performance after a warning has been given.

Many businesses have preferred to avoid the risk by hiring casuals and contractors. Other businesses have tightened their employment contracts (often called 'corporate pre-nuptial agreements') and included job descriptions, probation periods and measurable targets to allow for dismissal of staff if required. They are keen to avoid unfair dismissal claims, which create adverse publicity for the business internally and externally, with the potential to lose customers. For many it has been regarded as cheaper and less time consuming to settle the claim, regardless of whether or not it is valid. Many have needed to consult specialists in the area of termination to avoid these problems.

KEY IDEAS

- Separation occurs when an employee either chooses to leave an employer voluntarily through resignation, voluntary redundancy or retirement, or involuntarily through retrenchment or dismissal.
- Dismissals may occur due to serious misconduct, poor performance or redundancy due to organisational restructuring.
- Employers need to take great care in following all the legal processes involved in dismissing an employee to avoid costly claims of unfair dismissal.
- Unfair dismissal occurs where an employee is dismissed by their employer and they believe the action is harsh, unreasonable or unjust.

19.5 Activities

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To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. **A downloadable solutions** file is also available in the Resources tab.

19.5 Quick quiz on	19.5 Exercise	19.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 4, 5, 6, 8	1, 2, 7, 11	9, 10, 12

19.5 Exercise

Revision

1. **Distinguish** between voluntary and involuntary termination, giving examples of each.
2. **Why** must involuntary separation be managed carefully?
3. **What** are the acceptable situations for redundancy?
4. **State** the matters that need to be considered when determining who will be retrenched.
5. **List** some of the entitlements of employees who are made redundant.
6. **Outline** the issues an HR manager must be aware of when dismissing an employee.

7. **Explain** the role of the Fair Work Commission in handling unfair dismissal cases.
8. **Outline** the ways in which businesses are responding to the risk of unfair dismissal claims.

Extension

9. **Evaluate** current dismissal laws from the perspectives of both employers and employees.
10. You are appointed human resource manager for a bank with a high level of turnover of female staff, and low rates of return from maternity leave. **Create** a speech for the executive team explaining the likely reasons and the best practice strategies needed to create a positive workplace culture that is free from bullying and is also family-friendly.
11. **Investigate** recent unfair dismissal claims and summarise the main reasons the claims have been upheld or dismissed.
12. Interview two employees in a business that you know about the methods used for communication with and between staff. **Evaluate** the strategies used and recommend additional or alternative methods that could improve communication or employee participation.

19.5 Exam questions

Question 1 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q4

Which of the following is an example of voluntary separation in the workplace?

A. Dismissal
B. Promotion
C. Reinstatement
D. Resignation

Question 2 (1 mark)

Source: HSC 2016 Business Studies Exam, Section I, Q2

Ruth observed that a work colleague was stealing and reported the theft to her supervisor. As a result, Ruth's employment was terminated.

What is this an example of?

A. Performance management
B. Redundancy
C. Retrenchment
D. Unfair dismissal

Question 3 (4 marks)

Buster's Total Building Pty Ltd has experienced steady falls in sales. As a result, management feels that the only way to survive is to cut back on its operations and to consolidate its debts. This will mean that 25 per cent of the staff will no longer be required. The 75 staff members include many who have worked with Buster for over 20 years. Quite a few are close to retirement age. Recommend strategies for separation for Buster's Total Building Pty Ltd.

Question 4 (2 marks)

Describe voluntary and involuntary separation.

Question 5 (1 mark)

For a long time, Carrie has been arriving late to her job at a restaurant. She finally loses her job. Which of the following statements best describes this separation?

A. Dismissal
B. Retrenchment
C. Redundancy
D. Retirement

More exam questions are available in your learn ON title.

19.6 Review

19.6.1 Summary

Acquisition

- The major elements of human resource management are: acquisition, development, maintenance and separation.
- A strategic approach to human resource management is proactive, considers the short- and long-term business needs, and uses a systematic approach that integrates all the human resource strategies to achieve the business goals.
- Acquisition involves analysing the internal and external environment of a business.
- An effective induction program is carefully planned to introduce a new employee to the job, their co-workers, the business and its culture.
- Recruitment involves locating and attracting the right quantity and quality of staff to apply for employment vacancies.
- Employee selection involves gathering information about each applicant and using that information to choose the most appropriate applicant.
- Placement involves locating the employee in a position that best utilises their skills to meet the needs of the business.

Development

- Development involves enhancing the skills of the employee through training, mentoring, coaching and performance management so they develop a career with the business.
- Effective induction and training equips a new employee with the skills to carry out their job and work effectively with co-workers within the business and its culture.
- Ongoing training should be part of every workplace. Changes in the business environment, including new technology and global competition, are increasing the need for training.
- Businesses are using flatter structures to improve efficiency and competitiveness by creating more opportunities for employees to innovate and participate in solving business problems.
- Organisational development involves developing strategies such as job rotation to increase employee participation, motivation and retention.
- Performance appraisal is used to evaluate employee performance, and identify areas for mentoring, coaching, leadership development or performance management to enable the employee to contribute most effectively to a business's success.

Maintenance

- Maintenance focuses on the processes needed to retain staff and manage their wellbeing at work.
- Staff wellbeing is maximised through encouraging staff to participate in decision making, and giving employees some control over their work lives.
- Effective workplace relationships depend heavily on a business's communications systems. Poor communication is often reflected in workplace conflict and high turnover rates.
- Businesses benefit from employee experience and knowledge on the job, and improvements they suggest are often critical to a business's competitiveness and success.
- Benefits are an integral element in building workplace culture. They may be monetary in value or non-monetary.
- Employers are responding to employees' desire for a work–life balance with more flexible working arrangements.
- An important role of the human resource manager is ensuring the policies comply with legislation including anti-discrimination and sex discrimination legislation, WHS, taxation, social justice legislation and industrial relations legislation and agreements.

Separation

- Separation occurs when an employee either chooses to leave an employer voluntarily through resignation, voluntary redundancy or retirement, or involuntarily through retrenchment or dismissal.
- Dismissals may occur due to serious misconduct, poor performance or redundancy due to organisational restructuring.
- Employers need to take great care in following all the legal processes involved in dismissing an employee to avoid costly claims of unfair dismissal.
- Unfair dismissal occurs where an employee is dismissed by their employer and they believe the action is harsh, unreasonable or unjust.

19.6.2 Key terms

acquisition the process of attracting and recruiting the right staff for roles in a business
development refers to enhancing the skills of the employee in line with the changing and future needs of the organisation
employee selection involves gathering information about each applicant for a position, then using that information to choose the most appropriate applicant
fringe benefits tax (FBT) a tax employers must pay on certain benefits they provide to their employees or their employees' associates, such as a family member. It is based on the taxable value of the various fringe benefits provided.
job enlargement involves increasing the breadth of tasks in a job
job enrichment involves increasing the responsibilities of a staff member
job rotation involves moving staff from one task to another over a period of time in order to multiskill employees
job sharing when two people share the same job
maintenance the process of managing the needs of staff for health and safety, industrial relations and legal responsibilities, including compensation and benefits, of all staff
performance appraisal a process of assessing the performance of an employee, generally against a set of criteria or standards
placement involves locating the employee in a position that best utilises the skills of the individual to meet the needs of the business
recruitment the process of finding and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost
redundancy occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition
retrenchment when a business dismisses an employee because there is not enough work to justify paying him or her
separation the process of employees leaving voluntarily or through dismissal or retrenchment processes
unfair dismissal occurs where an employee is dismissed by their employer and they believe the action is harsh, unreasonable or unjust

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Digital documents	Key terms glossary (doc-35674) Chapter crossword (doc-36224)
Interactivity	Chapter crossword (int-7177)
Exam question booklet	Chapter 19 Exam question booklet (eqb-0041)

19.6 Activities

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Exercise 1: Multiple choice questions

1. Which of the following would not lead to a need for staff acquisition in a berry farm?
   - **A.** The beginning of the harvest season
   - **B.** A significant increase in the award wage
   - **C.** An increase in demand for berries
   - **D.** A higher than expected berry harvest

2. If a business faces a staffing shortage in the next few months, which of the following should they consider?
   - **A.** Use of casual workers
   - **B.** Reducing overtime
   - **C.** Retrenchment packages
   - **D.** Closing the business

3. Effective recruitment and selection does not include which of the following?
   - **A.** Providing a range of monetary benefits only
   - **B.** A fair, non-discriminatory selection process is applied
   - **C.** Evaluating and attracting qualified applicants whose values align with the business and its culture
   - **D.** Giving applicants a realistic understanding of their job requirements

4. Which of the following plays a major role of the human resource manager in development of staff?
   - **A.** Establishing effective training programs and evaluating them
   - **B.** Establishing good working relationships with co-workers and supervisors
   - **C.** Building new employee confidence in the job
   - **D.** Removing restrictive work practices

5. Training and development is most useful when it results in which of the following?
   - **A.** Reduced business competitiveness
   - **B.** Increased levels of communication, teamwork, opportunities for problem solving and financial analysis
   - **C.** Focused on high turnover rates
   - **D.** Higher staff turnover

6. Which of the following is an internal influence on training?
   - **A.** Attitude of employees to training
   - **B.** New research on training
   - **C.** Support available for training from government programs
   - **D.** Learning methods to be applied

7. Which of the following is a difference between mentoring and coaching?
   - **A.** Mentoring includes a specific time frame, coaching does not.
   - **B.** Mentoring is structured, coaching is not.
   - **C.** Coaching is specific to an employee's work function and mentoring focuses on preparation for future roles.
   - **D.** A coach acts as a facilitator, providing advice, while a mentor provides support with goal setting.

8. Which of the following describes the reason for the use of flexible work arrangements?
   - **A.** They are rarely valued by staff.
   - **B.** Many are costly to administer.
   - **C.** They are often useful in retaining staff.
   - **D.** They are not a legal requirement of federal awards.

9. Which of the following are not strategies that assist in retaining staff?
   - **A.** Family-friendly programs; for example, job sharing
   - **B.** Protocols for constructive communications including email
   - **C.** Team briefings
   - **D.** Inducting and training staff in workplace benefits

10. When may an employee contest a dismissal?
   - **A.** They believe the action is harsh, unreasonable or unjust.
   - **B.** They believe their dismissal is vexatious or frivolous.
   - **C.** They believe the reason their job was made redundant was because of reduced sales.
   - **D.** Workers cannot contest their dismissal.

Exercise 2: Exam practice questions

Question 1 (3 marks)
Describe the processes of human resource management.

Question 2 (4 marks)
Distinguish between acquisition and separation and their role in managing human resources.

Question 3 (6 marks)
a. **Outline** the importance of maintenance in human resource management. **(2 marks)**
b. **Recommend** TWO strategies to reduce staff turnover in a business. **(4 marks)**

Question 4 (5 marks)
Analyse the importance of induction in the acquisition process of human resource management.

Question 5 (2 marks)
Outline ONE feature of an effective training program.

Question 6 (5 marks)
Analyse employee participation strategies used in the process of maintenance in human resource management.

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Teacher-led video Chapter 19 Exam practice solutions (tlvd-1882)

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20 Strategies in human resource management

20.1 Overview

LEARNING SEQUENCE

20.1 Overview
20.2 Leadership styles
20.3 Job design
20.4 Recruitment and selection process
20.5 Training and development
20.6 Performance management
20.7 Rewards
20.8 Global strategies
20.9 Workplace disputes
20.10 Review

20.1.1 Introduction

Human resource management strategies are the plans implemented by a business to manage staff and align them with the strategic goals of the business. They are the means by which the business implements the different processes of human resource management (i.e. acquisition, development, maintenance and separation). For instance, human resource managers need to develop and implement strategies that will attract potential employees to the business and develop their skills so they can add value, motivate and reward staff, as well as create a culture that retains staff and reduces employee dissatisfaction.

FIGURE 20.1 Effective human resource management requires the management of staff to be aligned with the strategic goals of the business.



Most human resource management strategies will involve managers making choices; for instance, which leadership style to adopt, which recruitment strategies to use, what training strategies to provide or what rewards should be given. There are no 'right' or 'wrong' choices; however, the strategies chosen should be appropriate and guided by the overall strategic goals of the business. The strategies should therefore provide a roadmap for the organisation on how it can leverage its employees to achieve the business's objectives.

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Digital document Key terms glossary (doc-35676)
Exam question booklet Chapter 20 Exam question booklet (eqb-0042)

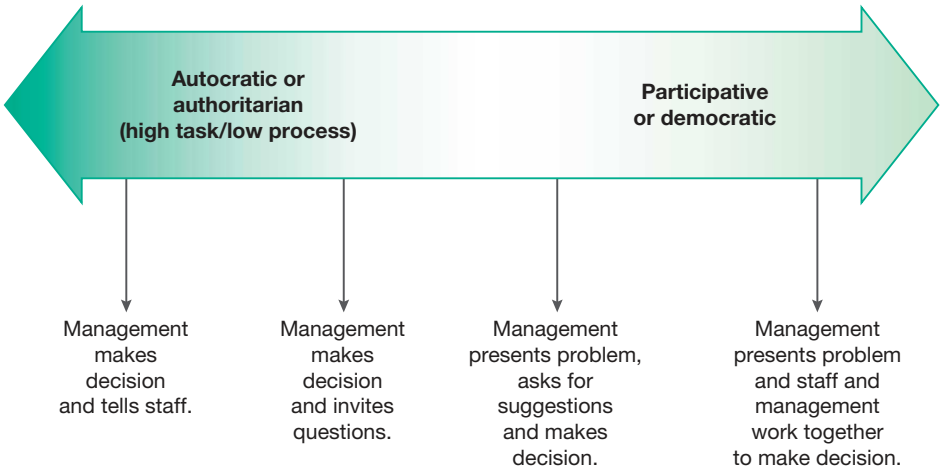
20.2 Leadership styles

SYLLABUS LINK In this subtopic you will learn about leadership style as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Leadership style refers to ways that managers communicate with their employees to inspire and motivate them to work together to achieve an organisation's goals. Rarely does a 'one size fits all' approach to leadership work so it is necessary to consider a number of different styles. The leadership styles can be considered through a continuum as illustrated in figure 20.2.

FIGURE 20.2 One theory of leadership styles — the continuum



Autocratic (authoritarian) leadership style

Managers who make decisions quickly and in many cases without input from staff characterise an autocratic leadership style. This leadership style works well with unskilled and/or inexperienced workers where the work is highly organised and controlled. This inflexibility can, however, lead to problems such as higher levels of absenteeism and staff turnover. It does work well in situations such as in the defence forces where leaders are expected to make difficult decisions without the need for consultation or discussion.

The autocratic leadership style is sometimes aligned with a transactional management style where workers' compliance is recognised through financial reward that is often linked to meeting organisational goals. It suits those driven by financial reward, but is often linked to lower levels of job satisfaction.

The autocratic leadership style has its origins in the Classical school of management where employees' work could be more scientifically measured and the most efficient and productive methods applied.

While the autocratic leadership style was historically used in the mass production of goods in the early 20th century, it is still used in some businesses today; for example, in the fast food industry. The autocratic leadership style can be effective in times of crisis when immediate compliance with rules or procedure is needed, in situations that require fast and immediate decision-making or where there are a lot of inexperienced staff. This style is most appropriate when the nature of work requires strong centralised control.

leadership style refers to ways that managers communicate with their employees to inspire and motivate them to work together to achieve an organisation's goals

BizFACT

Studies of Australian leaders stated that they traditionally value egalitarianism, mateship and a fair go, but have a history of discrimination and value individual, rather than group rewards. They are seen as decisive, of high integrity, performance orientated, and demonstrating humanity. In international studies, however, they do not want to stand out from their peers.

Participative (democratic) leadership style

At the other end of the continuum is the participative or democratic style. This leadership style is characterised by a more consultative approach between managers and workers that encourages them to be more engaged in the decision-making process. This style of leadership is linked to transformational leadership where managers have higher expectations of workers and this leads to higher levels of engagement.

This higher level of involvement in the decision-making process gives workers a greater sense of ownership of the final decision and also results in higher levels of job satisfaction and productivity.

This approach works well when the emphasis is on higher quality output rather than efficiency. It may lead to a longer decision-making process as time is given over when management consults with staff. Further, where workers are inexperienced or disaffected their lack of engagement may be of little assistance to the decision-making process and this too can be considered as problematic.

The participative or democratic approach also encompasses a more behavioural approach to the management of workers. It therefore addresses the role of motivation, conflict and relationships. Workers are seen as a resource that can be developed over time.

Appropriate uses for different leadership styles

Australians tend to appreciate a leadership style that encourages management and staff to work together in achieving goals, rather than be led from the front. Australian workers respond better to higher levels of expertise and leaders who have gained other workers' respect are far more likely to achieve business goals. Most managers will use a variety of management styles depending on the situation. Effective leaders are flexible and adept at analysing situations and then using the most appropriate leadership style for the given circumstances.

The most appropriate uses for these styles are shown in table 20.1.

TABLE 20.1 Leadership styles

Leadership style	Example phrases	When the style works best
Directive • Emphasis on immediate compliance from employees • Other labels: autocratic, dictatorial, coercive	Do it the way I tell you. I believe that people should do what I tell them.	In a crisis, to kick start a turnaround or with problem employees
Visionary • Emphasis on long-term vision and leadership • Other labels: big picture, authoritative	I enjoy mobilising people towards a bigger picture. I believe I am firm but fair, giving employees clear direction, motivating by persuasion and giving feedback on task performance.	When changes require a new vision, or when a clear direction is needed
Affiliative • Emphasis on the creation of harmony • Other labels: harmoniser	I believe in people before tasks — emotional bonding.	To build buy-in or consensus or to get input from valuable employees

(continued)

TABLE 20.1 Leadership styles *(continued)*

Leadership style	Example phrases	When the style works best
Participative/democratic • Emphasis on group consensus and generating new ideas • Other labels: democratic	I believe in building support and commitment.	To build buy-in or consensus or to get input from valuable employees
Pacesetting • Emphasis on accomplishment of tasks to high standards	I expect self-direction and excellence.	To get quick results from a highly motivated and competent team
Coaching • Emphasis on the professional growth of employees • Other labels: developmental	I develop others for the future.	To help an employee improve performance or to develop long-term strengths

Source: Workforce Planning and Policy Directorate, South Australia, Department of Further Education, Employment, Science and Technology, 2010

BizFACT

For managers who really want to be constructive the advice is to:

- seek advice from others about your style. Listen to your employees' feedback.
- think about the behaviours you want to develop
- be a good role model
- support your employees.

SNAPSHOT

Case study: Leadership versus management — is there a difference?

There are a number of accepted characteristics that are considered essential for all leaders. It may be true that not all leaders will have all these traits but a good leader is able to compensate for this by being capable of identifying such qualities in their staff and being able to use their skills for the benefit of the organisation.

The characteristics of effective leaders include:	
Self-awareness	the ability to identify your own strengths and weaknesses
Decisiveness	the ability to make decisions quickly
Fairness	treating workers equally
Enthusiasm	motivating your team with a positive outlook
Integrity	earning respect from staff
Knowledge	the ability to understand your job including changes that take place and that change requires a response
Creativity and imagination	generating new and innovative ideas
Endurance	persevering with a task or difficult situation until it is resolved

Some of the qualities observed in less effective leaders include:	
Poor communication	may lead to misunderstandings
Reluctance to delegate	can result in resentment and low productivity
Nepotism	favouring certain staff, which can lead to poor morale

Often there is a view that management and leadership are the same. It is increasingly the case rather that the roles are viewed as being quite separate. A leader inspires, motivates and encourages their team to strive to achieve the business's vision; a manager is more involved in the day-to-day operational activities required to run the business. To this end the manager will:

- ensure that products meet customer expectations
- evaluate existing operations processes
- address work health and safety requirements
- plan, implement and monitor budgets.

That is not to say a manager and leader cannot be the same person, however, the roles should be viewed separately. A leader can only implement the business's vision if there is an effective and efficient management structure in place; the leader is then free to be effective without getting tied down in more operational matters.

Recently, indications in the Australian corporate environment are that many employees are dissatisfied with the leadership provided by many managers. The main issue for many workers is that managers seem to lack strategic planning initiatives and, in particular, fail to anticipate the rise of disruptive changes in markets such as the emergence of the 'share economy'. Moreover, management often appears unable to identify opportunities and how to adapt to the dynamic business environment. If these challenges are to be met, leadership and management skills must be developed sooner rather than later.



KEY IDEAS

- A range of strategies are used to align the management of staff with the goals of the firm, including leadership styles.
- Leadership styles can be considered across a spectrum from an autocratic approach to a participative or democratic approach.
- Leadership styles which are most effective in Australia are more egalitarian and empowering and less directive than in other countries.
- Australian employees tend to be critical of the quality of Australian leadership and are seeking constructive workplace cultures where employers are supportive and focused on developing the skills and talents of employees in challenging and meaningful tasks and projects.

20.2 Activities

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20.2 Quick quiz on	20.2 Exercise	20.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
6, 7, 11, 14	1, 2, 3, 4, 5, 9, 10	8, 12, 13

20.2 Exercise

Revision

1. **Distinguish** between an autocratic and democratic/participative leadership style.
2. Select two leadership styles you believe are most effective in creating a positive workplace culture. **Justify** your choice.
3. **Discuss** the use of a directive leadership style in business.
4. **How** does culture influence leadership style in Australia today?
5. **Discuss** the major challenges faced by leaders and human resources managers in assisting in the implementation of change today.

Read the 'Leadership versus management— is there a difference?' case study and answer questions 6 to 11.

6. **Identify** some of the less effective qualities observed in leaders.
7. **List** some of the positive character traits found in effective leaders.
8. **Analyse** the characteristics of leaders you have observed at the school, community, politics or business level. List the positive qualities you identified in them.
9. **Distinguish** between a leader and a manager.
10. Is it possible for a manager and a leader to be the same person? **Discuss**.
11. **What** challenges are faced by leaders and managers in the Australian corporate environment?

Extension

12. **Evaluate** the significance of 'leadership styles' on employee performance.
13. **Analyse** how an Australian leader may need to adapt to managing staff overseas.
14. Interview a manager about their day's activities. Construct a table listing these activities and **describe** the most appropriate leadership style for each of these activities.

20.2 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q3

A business in crisis needs to make immediate and timely decisions in order to survive.

Which leadership style does a manager of this business need to adopt?

A. Autocratic
B. Bureaucratic
C. Democratic
D. Laissez-faire

Question 2 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q13

What is a reason for a business to use a democratic leadership style?

A. It has a project with a tight deadline.
B. It has experienced, highly skilled employees.
C. There is a need for more standardised products.
D. There is a potentially dangerous work situation.

Question 3 (6 marks)

Source: HSC 2012 Business Studies Exam, Section II, Q24b

TextMore is a global communications business that is facing increased competition. Management has decided to reduce the size of its factory workforce by 25% but also employ more information technology (IT) specialists.

Explain how TWO human resource strategies could be used to effectively manage downsizing TextMore's factory workforce.

Question 4 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q12

A manager builds relationships with individual employees and encourages their contribution to decision-making in the workplace.

What leadership style is this?

A. Autocratic
B. Democratic
C. Laissez-faire
D. Political

Question 5 (1 mark)

Source: HSC 2004 Business Studies Exam, Section I, Q7

The new CEO of Red Flash Sports Clothing Pty Ltd is determined to consult with stakeholders to achieve specific production targets.

What is her leadership style?

A. Autocratic
B. Contingency
C. Hierarchical
D. Participative

More exam questions are available in your learnON title.

20.3 Job design

SYLLABUS LINK In this subtopic you will learn about job design (general or specific tasks) as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Job design is the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job.

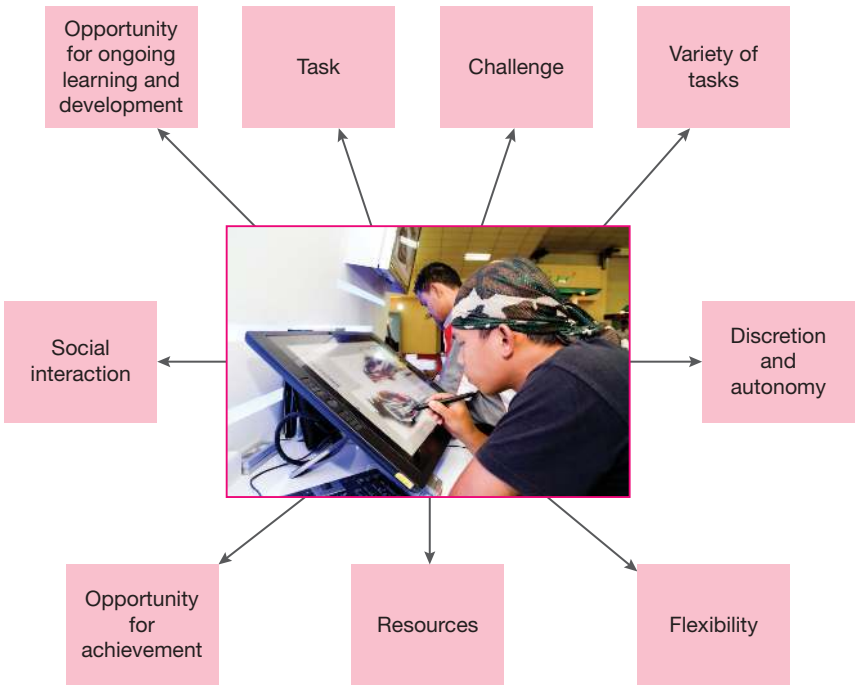
Tasks are often routine, repetitive and inflexible and reflect a relatively simple approach. Specific tasks in job design are best represented through the Scientific management approach developed by Frederick Taylor who identified that there was one best way of doing a job and that worker skills should be matched to the job requirements. It is based on specialisation and is an efficient process that often uses low-skilled, cheap labour.

In recent times, however, job design has been expanded to incorporate a more general approach with a greater variety of tasks to be performed by workers. This is sometimes referred to as job enlargement; that is, the horizontal expansion of the job by adding similar level responsibilities. The main objective of the provision of a wider variety of tasks is to improve worker engagement, satisfaction and ultimately productivity. Managers must, however, avoid simply adding tasks for the sake of it and should recognise that there is some benefit from a specialised approach.

The common elements of a well designed job are shown in figure 20.3. It is known that employees are more motivated and likely to share ideas if they have autonomy, have clear task identity (know what they have to do), are well trained and feel competent, and receive feedback that allows them to be recognised and develop further. Feedback is demotivating when it is controlling, although feedback that is informative and constructive is motivating. Employees are also more motivated when they are able to plan, schedule and determine how to do a job.

job design the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job

FIGURE 20.3 The core elements of a well-designed job



SNAPSHOT

Case study: Job design — intrinsic rewards

In the past, job specialisation — where production was broken down into distinct tasks that were performed by individual employees — often resulted in employee boredom and dissatisfaction. To counter this effect, three job design approaches have been used based on intrinsic rewards — the good feeling that one gets from doing something well.



Job design approach	Explanation
1. Job rotation	Employees switch, for a period of time, from one job to another. This provides variety and gives employees a more comprehensive view of the organisation or the production process.
2. Job enlargement	Employees are given more things to do within the same job. This provides job variety and a greater challenge for employees.
3. Job enrichment	Employees are given more control and independence over how they do their work. This makes the job more interesting and challenging and provides motivating opportunities for self-satisfaction.

BizFACT

- Common methods used in job design today are developing broader, more generalised and flexible jobs, so that businesses can attract, motivate, retain and use labour more flexibly and efficiently.
- Research indicates that it can take employees 50 per cent longer to complete tasks when they are required to multitask and it is also a major cause of work-related stress.

KEY IDEAS

- Job design is the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job.
- Job design (specific tasks) is best represented through the Scientific management approach developed by Frederick Taylor that identified one best way of doing a job and that worker skills should be matched to job requirements.
- Job design (general tasks) refers to a greater variety of tasks to be performed by workers. The main objective of the provision of a wider variety of tasks is to improve worker satisfaction and productivity.

20.3 Activities

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20.3 Quick quiz on | **20.3 Exercise** | **20.3 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 4, 6, 7, 8	3, 5	9, 10, 11, 12

20.3 Exercise

Revision

1. **What** is the purpose of job design in human resource management?
2. **Identify** the steps involved in effective job design.
3. **Discuss** the different approaches to job design.
4. **Outline** examples of how three methods of job design could be applied in (a) a school administrative office, (b) a theatre and (c) a football club in order to meet the needs of the employees or business.
5. **Explain** why specialised job design often reduces job satisfaction.

Read the 'Job design — intrinsic rewards' case study and answer questions 6 to 8.

6. **What** is job specialisation?
7. **Define** intrinsic rewards.
8. **Identify** one of the three job design approaches and explain what you understand by it.

Extension

9. **Evaluate** the use of team structures in job design today.
10. **Determine** the issues associated with designing specialist jobs.
11. Interview someone you know about their job. **Assess** the quality of their job design.
12. **a. Create** a job design for someone within a business you know.
    b. Evaluate the process of job design you used.

20.3 Exam questions

Question 1 (1 mark)

Which of the following is a benefit for an employee of appropriate job design?

A. Increased job satisfaction
B. Increased productivity
C. Reduced costs and waste
D. Increased teamwork

Question 2 (1 mark)

A large manufacturing business has a leader who uses a very traditional approach to human resource management. Which of the following would best describe his approach to job design?

A. General job design
B. Team-oriented job design
C. Little emphasis on job design
D. Specific tasks in job design

Question 3 (2 marks)

Distinguish between general and specific tasks as strategies of job design in human resource management.

Question 4 (4 marks)

Explain job design as a strategy of successful human resource management.

More exam questions are available in your learnON title.

20.4 Recruitment and selection process

SYLLABUS LINK In this subtopic you will learn about recruitment (internal or external, general or specific skills) as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

20.4.1 What is recruitment?

Recruitment is the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost. Effective recruitment and selection allows the most appropriate applicant to be selected. The most visible aspect of the recruitment process is the job advertisement.

recruitment the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost

SNAPSHOT

Case study: Outback trackers — seeking a General Manager

Position: General Manager

Location: Head office located in Darwin, with teams located throughout the Northern Territory

Salary: $100 000 + accommodation + superannuation



Outback Trackers provides guided tours, including walking, camping and canoeing expeditions and scenic flights, through the breathtaking Northern Territory. Outback Trackers is wholly owned and operated by Indigenous Australians, who share their extensive knowledge of the terrain and history of the region while expertly guiding you through the stunning scenery.

Outback Trackers is seeking a General Manager to be part of this exciting company. The primary responsibility of this role is to oversee the everyday management of Outback Trackers, including staff and operational management, budgeting and management reporting, and ensuring the highest product quality and service standards. Excellent interpersonal and communication skills are essential to build upon and enhance effective working relationships. You'll be able to multitask and work under pressure while maintaining stringent attention to detail. You will have excellent oral and written communication skills, as well as the ability to work closely with all teams, including Operations and Marketing, to build the success of the company and drive it forward into the next decade and beyond.

BizFACT

Attracting the right candidates to the job is an ongoing process. Many organisations actively seek to build their 'employer brand', creating an image of their company as a great place to work for both current and prospective employees. Among the preferred employers identified in a recent survey conducted by LinkedIn were IAG (insurance), AGL Energy (utilities), Qantas (aviation), Wesfarmers (retail) and KPMG Australia (management consulting).

The sources and methods of recruitment that a company uses will depend on:

- the recruitment goals and policies of the business (e.g. preference for internal recruitment)
- the conditions of the labour market
- the location of the business
- the financial or other resources of the business
- the specifications of the job to be filled (e.g. whether general skills or specific skills are needed).

For example, internal recruitment may be used as a strategy to motivate and reward employees. Most businesses use a mix of internal and external recruitment, and require a mix of general and specific skills.

A poor selection process leads to increased costs and lower productivity by increasing (among other things):

- training costs (if poorly qualified staff are selected)
- job dissatisfaction, lower performance, industrial unrest/labour turnover if the business or the job does not meet the expectations of candidates selected
- the absenteeism rate if staff feel inadequate for the job/business or feel excessive work pressure
- accident or defect rates, fines if inappropriate/untrained staff are selected
- claims of discrimination if the process is not undertaken appropriately.

20.4.2 Internal or external recruitment

Internal recruitment sources include employees, former applicants and former employees, and they may be invited to apply through intranet postings, staff records, promotion lists, word of mouth, email and other methods. Employee referrals are popular, when accompanied by an employee bonus, and useful for bringing in staff with the right 'cultural fit'.

External recruitment employees may be obtained through traditional methods such as newspaper advertisements, online advertisements and referrals through recruitment agencies, company websites, trade unions, trade shows, management networks, professional associations, schools, radio and television.

The fastest growing recruitment methods today are social networking sites, such as Facebook, Twitter, LinkedIn and niche blogs; and virtual reality sites, such as Second Life. Some firms cite online company videos as having response rates of up to 18 per cent, far exceeding that of other recruiting strategies. They are very successful when used on smart phones, with videos often going 'viral'. This is important for businesses that need to be constantly recruiting, such as technology, mining and hospitality companies.

FIGURE 20.4 Social networking sites and company videos viewed on mobile phones are the fastest growing recruitment methods today.



internal recruitment involves filling job vacancies with people from within the business

external recruitment involves filling job vacancies with people from outside the business

The advantages and disadvantages of internal and external recruitment are shown in table 20.2 and table 20.3.

TABLE 20.2 Advantages and disadvantages of internal recruitment

Internal recruitment	
Advantages	**Disadvantages**
• Motivational for staff, see development opportunity • Builds commitment and loyalty • Business only needs to hire at base level • Employees know the culture, operations — productivity maintained • Can lead to a succession of promotion opportunities in line with succession planning • Recognises and rewards staff for effort and achievement • Cheaper than external recruitment, less chance of a failure as staff are observed in operation, strengths and weaknesses are known	• Can reinforce negative culture • Can lead to rivalry for positions • Need established framework for training and merit-based appraisal system • Often attracts a significant number of internal applicants; need to manage unsuccessful applicants who will be demotivated, can lead to poor working relationships • Little value added, no new skills

TABLE 20.3 Advantages and disadvantages of external recruitment

External recruitment	
Advantages	**Disadvantages**
• Wider applicant pool • New ideas, perspectives and skills may produce better solutions to business issues • Get specific skills needed, save on training • Dilutes internal politics • More diversity in employment — equal employment opportunity • Builds organisational 'brand' through publicity • Can shape new employee to business	• Risk of unknown staff • Lost productivity in initial phases of orientation and induction • New employee may not fit culture, and may not be accepted by internal rivals • Takes a lot of effort and time • Risk of legal claims

Many firms consider internal potential candidates first and move to external recruitment when appropriate internal staff are not available. Some positions, such as sales staff, need to be filled immediately and will require a significant campaign, although others can be managed over a longer period at a lower cost.

The recruitment process needs to be managed very carefully and applicants given a realistic job preview during the process, using videos, samples or descriptions of the actual work to avoid expensive acceptance errors, where new employees find the work does not match their expectations and leave the position. Background checking and contact with referees is critical to verify qualifications and experience provided.

BizFACT

Most firms still use résumés, applications and interviews as their major tools in the recruitment process. Interviews prove most useful for determining behaviour and cultural fit. The internet is the most common method used to advertise positions vacant.

SNAPSHOT

Case study: Outsourcing the search for the most suitable candidate

Many business owners use external recruitment agencies as a way of decreasing the time involved in searching for a new employee. They pay an agency to interview applicants and recommend a short list of potential employees or an employee suitable for the available position.



There are a number of reasons for this trend, including the:

- growing demands on businesses to comply with increasingly complex employment legislation. Business owners find it beneficial to access specialist advice rather than risk breaching employment law
- availability of online recruiters. Recent statistics show that employers have widely embraced e-recruitment agencies
- desire by business owners to concentrate on their core business
- difficulty in attracting candidates due to the low level of unemployment
- ready databases of possible employees and the skill to sort candidates that external recruiters generally have.

However, the principal reason for using an external recruitment agency is related to the cost of a poor recruitment decision, which is generally believed to be around two or three times the annual salary of the person recruited. A poor recruitment and selection process leads to increased costs and lower productivity by increasing (among other things):

- training costs if poorly qualified staff are selected
- job dissatisfaction, lower performance, industrial unrest or labour turnover if the business or the job does not meet the expectations of candidates selected
- the absenteeism rate if staff feel inadequate for the job or feel under excessive work pressure
- accident or defect rates if untrained or inappropriate staff are selected.

20.4.3 General or specific skills

General skills

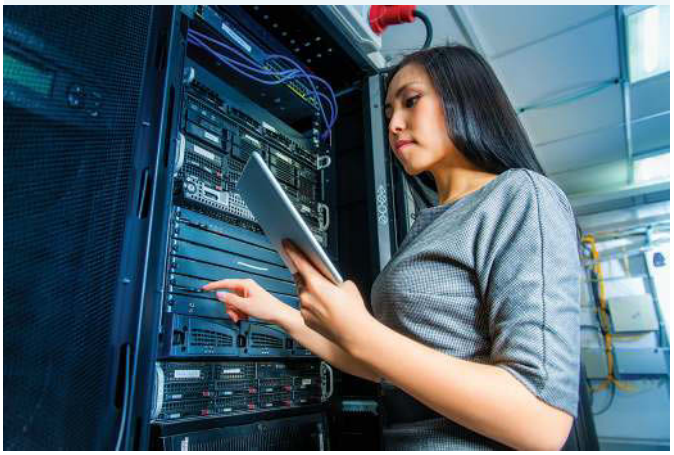
Many businesses focus on attracting staff with general skills, attitudes and behaviours that are a good cultural fit for their business. The job can then be customised to suit the recruits who can be trained and developed according to the business's needs. Key **general skills** include flexibility and versatility, social confidence, a positive attitude, motivation, ability to work as a team or independently, leadership and decision-making styles, willingness to learn, and ability to work under pressure. These behavioural 'soft' skills, are often critical in building a successful workforce, and are not really 'learned', whereas specific skills can be taught.

general skills include flexibility and versatility, social confidence, positive attitude, motivation, and the ability to work as a team and/or independently

General skills are important because many jobs today require individuals to work independently and undertake many different tasks. General skills, therefore, are not as narrowly defined as in the past and they are generally more service oriented, making social and information skills increasingly important. Such skills are necessary not only to gain employment but also to progress within a business. Human resource managers value these skills within individuals because they generally indicate that the employee has a capacity and willingness to learn.

Increasingly, as online recruiting grows, businesses use their websites to promote their 'brand', the values and culture of their business. They also post generic position statements for positions that regularly come up, and for which many potentially attractive recruits exist. This strategy widens the pool of potential talent available to a business, particularly when coupled with online innovative strategies, such as employee resources.

FIGURE 20.5 Australia tends to suffer from a skills shortage, so employers are more likely to consider hiring for general skills, such as flexibility and versatility, and upskilling internally.



Specific skills

Most businesses are concerned about skill shortages and still need to target employees with **specific skills** to fill gaps in their business.

Sophisticated software is available to support workforce and recruitment planning. Both short- and long-term strategies need to operate parallel to ensure that businesses have staff with the required skills.

Many businesses are recruiting overseas or using outsourcing and overseas recruitment to overcome skill gaps in their businesses, particularly through skilled migration programs such as the Temporary Skill Shortage visa (formerly 457 visa).

While the need for chefs, skilled tradespersons, building professionals and engineers is well known, there is a significant shortage developing in more highly skilled and professional areas including specialist project management skills.

Industry sources have been critical of Australian firms for not investing in training their staff for developing workforce needs and changing organisational structures. They believe a greater part of the load needs to be shouldered by the very companies complaining about not having enough skilled workers. **Employee poaching** is frequently used.

specific skills highly specialised skills that are required for some jobs within science, technology and engineering sectors

employee poaching the practice of enticing employees to work for another business

SNAPSHOT

Case study: Jobs are changing, and fast. Here's what the VET sector (and employers) need to do to keep up

Technological developments are expected to majorly, and rapidly, disrupt or change the nature of employment. The multiplier effect of these disruptions interacting with each other has led to what has been termed the fourth industrial revolution (i4.0).

The first industrial revolution took us from agrarian to industrial economies and the second used resources like electricity and steel to create mass production. The third refers to technology advancing from analog and mechanical devices to the digital technology available today.

The fourth industrial revolution represents ways technology has become embedded in societies by the fusion of technologies, or what is known as cyber-physical systems. For example, 3D printing needs advanced materials with printers linked to the internet, which are increasingly intelligent and autonomous.

The consensus among experts is that our training providers and employers aren't adapting fast enough to meet the skill needs of the fourth industrial revolution. This is reflected in a growing technological and digital skills gap. But there are some things the sector can do to catch up.

Doom or opportunity?

Commentators have polarising views on the possible effects of the fourth industrial revolution. Some see technologies offering limitless new opportunities while others see major economic disruptions — the so-called dark side of technological change.

The pessimistic perspective is provided in an often cited 2013 study by labour researchers Carl Benedikt Frey and Michael A. Osborne, who argue 47 per cent of total employment in developed economies is at risk of automation. This figure also underlies eye-catching headline such as:

- Could a robot do your job?
- Artificial intelligence and automation are coming, so what will we all do for work?

In Australia, the Productivity Commission estimates 40 per cent of employment is at risk of being digitally disrupted by automation over the next 10 to 15 years. The Australian Industrial Transformation Institute estimates the level of disruption to be between 5 and 10 per cent.

But an important point often overlooked in these and related studies based on Frey and Osborne's modelling, is that they investigate the potential for existing jobs to be automated. They don't take into account the net effect of automation on jobs and that new jobs may be created as a consequence of automation.

More recent reports address this issue and point to a less pessimistic future. The World Economic Forum recently projected that while 75 million jobs will likely be displaced by robots, 133 million new jobs will be created. This means a net gain of more than 50 million jobs globally.

This suggests by 2022, some established roles such as data analysts and software developers — as well as so-called emerging roles such as machine learning specialists and robotics engineers, together with existing roles based on distinctively human traits such as customer service workers and people and culture specialists — will rise from 16 per cent of the labour force to 27 per cent.

On the flip side, as algorithms replace workers, declining roles such as accountants and telemarketers, currently representing around one third of the labour force, will fall to one in five workers.

In Australia, Deloitte Access Economics estimates more than 80 per cent of jobs will be created between now and 2030 for knowledge workers.

Should we be worried?

The suggested net employment gains are not a foregone conclusion. There is growing consensus developed economies like Australia must take urgent steps to mitigate the negative effects of technological disruption and take advantage of opportunities.

The fourth industrial revolution is predicted to be as, if not more, disruptive than the preceding three, in part as a consequence of the pace of change and magnitude of skill shifts. Australian workers are growing increasingly worried they will be displaced by technology because of irrelevant skills.

More than half expect they will need skills they currently lack within five years and that they will need to upskill, reskill and retrain.

Skills are a Darwinian, survival issue, not only for workers, but for the organisations that employ them. Two-thirds of employers say technology-related skills shortages are impacting them now (not in five years) and have noted their biggest challenge is to re-skill employees.

Recent research shows that while disruptive technology has reduced the need for some jobs, the main issue facing Australian employers is the changing nature of existing jobs.

This is particularly the case for the expanded range of tasks workers are expected to do. Employers seeking external training report difficulties finding vocational education and training (VET) providers delivering training in disruptive technologies.

Accordingly, larger firms will likely resort to in-house training, while smaller firms with fewer resources look to hire skilled workers.

Employers also often view university graduates with technology-related skills as more valuable than employees with VET qualifications. The result is a decline in confidence in the ability of the VET sector to deliver training that meets the challenges of technological disruption.

What kind of skills will future jobs need?

Much of the recent debate related to digital disruption has focused on the dichotomy between the importance of hard or technical skills (such as industry 4.0 programming, software engineering and data science) and soft or non-technical skills (such as creativity, design and teamwork).

For example, about half of Chief Information Officers favour hard skills while the other half prefer soft skills among future employees.

What needs to be done?

The VET sector requires increased collaboration between industry, educators and governments. It also needs responsiveness and flexibility in delivering skills, from formal qualifications to micro-credentials or non-formal education to reflect the needs of rapidly changing technologies.

A good example of this is the first nationally recognised qualification in automation, launched in Perth earlier this month. This came out of a collaboration led by Rio Tinto, South Metropolitan TAFE and the WA government.

Employers should also take a lead with experimenting and testing new methods to meet future skill needs. A South Australian electronics firm, REDARC, is preparing employees to become ready for the fourth industrial revolution by engaging experts to run dedicated sessions on the application of an overarching i4.0 lens across the core competencies of mechanical, chemical and electronic engineering.

The VET sector can play a complementary and reinforcing role. Besides catering for current students and apprentices, VET providers need to work with industry to build systems to facilitate continual learning (such as through flexible micro-courses) to ensure the skills of VET graduates or alumni are upgraded responsively.

Federal and state governments need to work to restore the confidence of employers and students in the VET sector. An important first step is to implement the early recommendations of the Joyce Review on VET.

Recent initiatives indicate the VET sector, industry and government have recognised these issues. They will need to pick up the pace to ensure vocational education provides students — and businesses that employ them — with the future-ready skills needed to succeed in the fourth industrial revolution.

Source: Pi-Shen Seet, Ann-louise Hordacre, Janice Jones & John Spoehr, 'Jobs are changing, and fast. Here's what the VET sector (and employers) need to do to keep up', *The Conversation*, 25 June 2019.

KEY IDEAS

- Recruitment is the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost.
- Most businesses use a mix of internal and external recruitment to maximise opportunities for new ideas and use of existing expertise in the business.
- Australia has long experienced a skills shortage, leading employers to increasingly recruit staff with general skills and upskilling internally.
- Many businesses recruit overseas and poach staff from other businesses to overcome shortages of skilled staff.

20.4 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

20.4 Quick quiz on | **20.4 Exercise** | **20.4 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
3, 4, 6, 7, 11, 13, 14, 16, 17, 18, 20, 21, 23	1, 2, 5, 8, 12, 15, 22	9, 10, 19

20.4 Exercise

Revision

1. Beth Gaikwad, manager at HRFirst, said: 'A poor recruitment and selection process has negative consequences for the business as well as the individual'. **Discuss**.
2. **Distinguish** between internal and external recruitment.
3. Using tables 20.2 and 20.3 as a guide, **clarify** when it is appropriate for a business to use:
   a. internal recruitment
   b. external recruitment.
4. **Identify** the set of general skills employees need to possess.
5. **How** do human resource managers choose whether to recruit for general or specific skills?

Read the 'Outback Trackers — seeking a General Manager' case study and answer questions 6 to 10.

6. **Identify** all the tasks involved in this job.
7. **Identify** and justify the major characteristics you would be looking for in an applicant for this position.
8. **Explain** how job analysis may have been undertaken for this job.
9. **Evaluate** this job in terms of the criteria for a well-designed job.
10. **Assess** the reward package for this job.

Read the 'Outsourcing the search for the most suitable candidate' case study and answer questions 11 to 15.

11. **What** is outsourcing?
12. **How** do businesses use external recruitment agencies to search for new employees?
13. **Outline** reasons for the use of external agencies in the recruitment process.
14. **What** is the likely outcome of a poor recruitment decision?
15. **How** does the selection of the wrong employee increase costs and reduce productivity?

Read the 'Jobs are changing, and fast' case study and answer questions 16 to 23.

16. **What** is the fourth industrial revolution (i4.0)?
17. **Identify** the previous industrial revolutions.
18. **How** is Australia placed to meet the skills requirements for i4.0?
19. **Assess** whether i4.0 poses a threat or an opportunity to Australia's workers.
20. **How** did the World Economic Forum view the increased trend towards automation?
21. **What** is the main issue facing Australian employers and how are they likely to respond?
22. **Distinguish** between hard and soft skills.
23. **Outline** the action that needs to be taken by industry, educators and governments to 'future-proof' Australian workers.

20.4 Exam questions

Question 1 (1 mark)

Source: HSC 2017 Business Studies Exam, Section I, Q1

A recruitment officer is employed by a business.

In which specific business function are they most likely to be engaged?

A. Finance
B. Human resources
C. Marketing
D. Operations

Question 2 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q3

A business places a job vacancy advertisement on its website.

Which aspect of human resource management is this an example of?

A. Development
B. Maintenance
C. Recruitment
D. Selection

Question 3 (1 mark)

Which of the following is an advantage of internal recruitment?

A. Ensures the best person for the job
B. Reduces the chance of conflicts
C. Requires no orientation
D. Brings new ideas

Question 4 (1 mark)

Which of the following is an advantage of external recruitment?

A. Ensures the best person for the job
B. Reduces the chance of conflicts
C. Requires no orientation
D. Brings new ideas

Question 5 (1 mark)

The human resource department of a large transnational corporation wishes to recruit a manager for its South-East Asian operations. The job will require excellent people skills, and the ability to work in different countries and deal with a variety cultures and work practices. The business is looking to recruit a person from one of its competitors because she is a team player and motivator.

Which of the following best describes the criteria for this recruitment strategy?

A. Internal and general skills
B. External and general skills
C. External and specific skills
D. Internal and specific skills

More exam questions are available in your learnON title.

20.5 Training and development

SYLLABUS LINK In this subtopic you will learn about training and development (current or future skills) as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Training aims to develop skills, knowledge and attitudes that lead to superior work performance. Training is critical in Australia today, as businesses report significant labour market problems, including a shortage of skilled labour, and a mismatch between what skills are needed and what is available. These problems act as a brake on investment, but can be overcome by business commitment to ongoing training.

Development is focused on enhancing the skills of the employee in line with the changing and future needs of the business. It also encourages employees to take advantage of opportunities to develop a career with the business. The business benefits by retaining the employee's experience and knowledge of the business, and by helping it maintain competitiveness.

training to develop skills, knowledge and attitudes that lead to superior work performance

development refers to enhancing the skills of the employee in line with the changing and future needs of the organisation

SNAPSHOT

Case study: BDO Australia — career planning

Peter O'Sullivan is Head of People and Culture at BDO Australia.

In reality, careers often develop with little in the way of planning. For example, in professions or organisations where there are well-established career paths, people may progress through the ranks without understanding or considering the range of career options available to them. In other contexts where career paths are less clear, they may move from one role to the next in a reactive or haphazard fashion, without considering how each role helps equip them for a long-term career goal. This tendency to let careers just happen is reinforced when organisations see career planning and development as the sole responsibility of the employee.



At BDO, we recognise that the best outcomes are achieved for both parties when the organisation supports the employee's career planning. At the beginning of an accountant's career, this usually involves participation in a structured graduate program and supporting the employee through their studies towards their professional qualification. These are formative career years, and the investment by BDO and employee alike is significant.

Like most organisations, BDO has a formal process for performance appraisal and professional development planning, and our process involves six-monthly discussions and the documentation of short-term and long-term developmental and career goals. These discussions are significant signposts in the employee's career, providing the opportunity to reflect on achievements and progress, obtain feedback and seek guidance about future goals and next steps, and discuss ideas and options. In addition, on-the-job appraisal, coaching and mentoring are all important aspects of BDO's approach to career planning and development.

BDO also has a learning and development curriculum that encompasses a comprehensive suite of programs tailored to staff at various stages of their career. One of the more innovative programs is our Career Development Workshop. This program is targeted at accountants who have already completed their professional qualification and is largely focused on career planning. Participants reflect on their career progress to date; are provided with detailed information and multiple perspectives on the range of career options available to them both within and outside BDO; and given tools, frameworks and tangible support to develop their own individual career plan.

The program recognises that not all of our staff will follow the traditional path to partner, and equips them to make more informed career decisions.

While it will always be up to our employees to take responsibility for driving their career, BDO encourages an approach to career planning and development in which the employee's supervising partner or other direct manager plays an active role. Other stakeholders such as senior partners, mentors, and human resources and learning and development team members also have important roles to play. Our approach is ultimately about providing as many opportunities as possible for reflection, meaningful discussion, learning, goal setting and planning. We want to make sure our people have a sense of control of their career and do not just 'let it happen'.

In choosing the nature of training and development, businesses need to use a systematic process to evaluate the needs of the business, the supply of these skills in the economy, the demand for these skills, and the changing nature of work and the general pattern of employment.

The shift to a largely service-based economy has seen many traditional skills, particularly those in manufacturing, become obsolete. Businesses need to consider the mix of skills they can develop internally and those for which they need to recruit.

Businesses will need to consider these options:

- invest in further in-house training and development
- recruit staff for specific skills
- retain experts who retire on a part-time basis
- retain women through flexible work structures such as part-time work
- share staff with other firms, or do work for other firms (**insourcing**)
- outsource functions to specialist firms or agencies, even overseas
- sponsor overseas migrants for areas of major shortages
- build networks or alliances with other firms with specialist skills or skills needed in the future.

insourcing delegating a job to someone within the business, as opposed to someone outside the business

BizFACT

Countries with similar economies to Australia, such as Canada, have identified the following work trends for the future:

- the complete transition to a service-based economy with primary sector jobs being fully automated
- growth in social professions such as teachers, nurses and homecare workers
- virtual work undertaken away from traditional workplaces that removes the need for commuting.

FIGURE 20.6 Children born today will work in jobs that have not yet been invented. Coming soon are these new areas of job growth.



BizFACT

A recent report states key skills sought by employers of university graduates are both verbal and written skills required in communication, the ability to work in teams and influence others — so called 'soft skills'. However, other skills such as critical thinking, problem-solving, attention to detail and writing were also highly sought and were common across all jobs and industries.

KEY IDEAS

- Training aims to develop skills, knowledge and attitudes that lead to superior work performance.
- Development is focused on enhancing the skills of the employee to upgrade their skills in line with the changing and future needs of the business.

20.5 Activities

learnON

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20.5 Quick quiz on	20.5 Exercise	20.5 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 4	1, 3, 5, 7	6

20.5 Exercise

Revision

1. 'Training improves current skills while development provides for future skills.' **Explain**.

Read the 'BDO Australia — career planning' case study and answer questions 2 to 5.

2. **What** role does career planning usually play in people's professional lives?
3. **How** does BDO assist people at the start of their career?
4. **Outline** the role of performance appraisal and professional development at BDO.
5. **Explain** the features of the learning and development curriculum that assist staff at BDO.

Extension

6. **Evaluate** the benefits of developing a training strategy which is focused on future skills in addition to current skills.
7. **Discuss** the benefits and costs of poaching staff from other businesses to overcome skills shortages.

20.5 Exam questions

Question 1 (1 mark)

Source: HSC 2020 Business Studies Exam, Section I, Q1

Which row of the table shows benefits of both staff training and staff development?

	Staff training	*Staff development*
A.	Increase staff skills	Increased staff turnover
B.	Increase staff skills	Retain experienced staff
C.	Decrease in workplace accidents	Increased staff turnover
D.	Decrease in workplace redundancies	Retain experienced staff

Question 2 (1 mark)

Which of the following best describes a feature of a successful training and development strategy?

A. Increases job turnover
B. Reduces teamwork
C. Helps business to change
D. Helps employees find new jobs

Question 3 (4 marks)

Freya Foods Pty Ltd wishes to implement a strategy to develop future skills in its human resources. Describe future skills as a training and development strategy and recommend a way to achieve this aim.

Question 4 (1 mark)

Barnaby works in the accounts department of a large retail business. The business wishes to use a different software program.

Barnaby is to attend a two day training course in the program's applications. Which of the following best describes the focus of the training and development strategy in which Barnaby is participating?

A. Current and specific skills
B. Future skills for long-term change
C. Current and general skills
D. Future and general skills

Question 5 (4 marks)

Analyse training and development as a strategy in human resource management.

More exam questions are available in your learnON title.

20.6 Performance management

SYLLABUS LINK In this subtopic you will learn about performance management – developmental or administrative – as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

20.6.1 Purposes of performance management

Performance management addresses both individual and business performance. Successful individual performance will often translate into the business's strategic objectives being met.

Job design, recruiting the best staff, training and development and rewards are all features of performance management.

The world's most admired businesses all view performance measures for human resources as equal to financial performance measures, and regularly evaluate such reports at board level, clearly indicating that managing people effectively is critical to business success. Figure 20.7 summarises the value of performance management.

Performance appraisal and management systems can be designed to meet two purposes for a business: developmental and administrative.

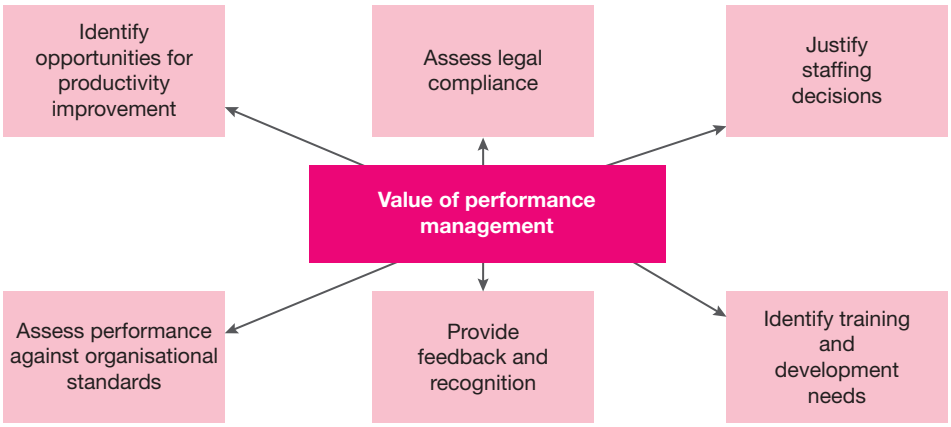
performance management addresses both individual and business performance. Successful individual performance will often translate into the business's strategic objectives being met.

performance management (developmental) this model improves individual performance through establishing objectives such as reaching sales targets that are consistent with achieving the organisation's goals

Developmental

The **performance management (developmental)** model is focused on using data to develop the individual skills and abilities of employees, so they improve their effectiveness in their roles, overcome weaknesses and are prepared for promotion. This is best achieved through year round periodic feedback and shared discussion that is both empathetic and goal focused.

FIGURE 20.7 The value of performance management



Administrative

The **performance management (administrative)** model provides information, often following an annual appraisal, which can be used by management for planning in human resource functions such as training, development, rewards, pay levels, benefits and performance improvement. The focus is on collecting data to manage the HRM function more efficiently and ensure that individual and business goals are aligned and strategic goals are met.

performance management (administrative) this model assesses the progress of the business in meeting its strategic goals and where necessary identifying the areas for improvement, such as establishing new goals or employee performance

SNAPSHOT

Case study: Regular feedback equals successful performance appraisal



While the end of the financial year provides businesses with an opportunity to do a 'stocktake' on their financial performance, equally important, but often overlooked, are regular reviews of the team's performance.

It is often said employees are the most important asset. If this is accepted, it would also stand to reason that people leaders would also review the performance of their employees.

. . .

Performance reviews [or appraisals] are a key aspect of keeping your team engaged and 'buying in' to what the business is trying to achieve. However, for some — both people leaders and employees — performance appraisals can be seen as a tiresome and difficult process, but it need not be.

When both parties know what is expected of them, a performance review should not contain any nasty surprises. However, lack of clear expectations is often where problems begin.

Most employees have a strong work ethic and want to do well . . . Notwithstanding, feedback from peers and people leaders is an important gauge for what an employee is doing well and what areas need development.

It is important to remember that feedback should not happen only at the end of the year in the form of an official performance appraisal. Feedback should happen regularly to ensure all parties are on the same page and any issues can be addressed quickly.

This four step process of performance management has traditionally worked well for setting employees up to achieve the best possible results.

Step 1. Ensure expectations are clear, for no other reason than employees are typically more productive when they know what is expected of them and when. These expectations may be set on a weekly basis but also typically cover a longer term, say half yearly or yearly. Some employers fall into the trap of assuming that their staff know what is expected of them. As a people leader, it is your responsibility to be clear.

Step 2. Assess performance regularly. Some people leaders complete an annual performance review and think their job as a people leader is done. Of course, an annual performance review is important to discuss what has been achieved over the year, but performance should be assessed on a regular basis to make sure projects are on track, milestones are being met and any queries resolved. A monthly catch up is a good starting point, to review . . . not only what is being achieved, but also . . . how it is being achieved.

Step 3. Provide feedback on a regular basis. Ideally, you should not need a formal catch up to provide feedback, but it is imperative that feedback is provided when performance is assessed. Feedback should include recognition of the effort, improvements and achievements throughout the past month, quarter or year, which is an excellent motivator for many employees. This is also the time to provide constructive feedback for development areas. Providing constructive feedback to highlight and bridge performance gaps, if delivered in the right way, can be equally motivating, as most employees want to continually improve their knowledge and skills.

Step 4. Continuous development will keep employees engaged and will ultimately result in increased productivity. Development planning looks not only at what the employee needs to do to complete their current role, but also helps to up-skill them for their next role. Development means different things to different people, but typically encompasses learning new skills on the job, mentoring, new responsibilities or stretch targets and formal courses.

Source: Extracts from 'The benefits of performance reviews', 12 June 2014, https://probonoaustralia.com.au

20.6.2 Benefits of effective performance management

The benefits of effective performance management from a developmental and administrative perspective are identified in table 20.4.

Establishing a link between performance evaluation and employee development will ensure that staff remain motivated and both they and the organisation benefit.

The key elements of performance management are the creation of a shared vision of the strategic direction of the business between employees and employers, the establishment of review process.

FIGURE 20.8 To be valued by employees, performance management requires active listening, regular feedback by all parties involved, and mutually agreed and beneficial action plans.



TABLE 20.4 Benefits of performance management

Developmental benefits	Administrative benefits
• Assists with human resource planning • Can plan to overcome gaps or weaknesses found in performance • Shows the effectiveness of current selection processes and whether staff recruited match the cultural fit and skills required for the organisation • Identifies training and development or legal compliance needs • Evaluates rewards and benefits programs • Communicates expectations, helps build trust, promotes long-term organisational development. • Helps identify, motivate and retain talented staff for leadership succession • Identifies and documents poor performance, and links it with training and improvement strategies • Helps build best practice culture	• Higher productivity • Better financial performance • Comparison of contribution to organisation and performance against agreed standards • Helps assess rewards and benefits linked to performance • Builds self-efficacy as contributions recognised — important in motivation and retention • Identifies strengths and weaknesses, creating opportunities for training and development, coaching or mentoring • Creates opportunity for employee to provide feedback • Initiative recognised and rewarded • Fosters promotion on merit • Employee focus is aligned with organisational strategy

BizFACT

Under the *Fair Work Act (2011)* all employees can bring an action for unfair dismissal. It is important for employers to be able to provide documented evidence of poor performance and how this has been communicated to the employee.

KEY IDEAS

- Performance management is a systematic process of evaluating and managing employee performance in order to achieve the best outcomes for a business.
- Feedback from performance appraisal and management provides many benefits to the business and the individual.

20.6 Activities

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20.6 Quick quiz on	20.6 Exercise	20.6 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 4, 5, 7	6	

20.6 Exercise

Revision

1. **Outline** the purpose of performance management systems.
2. **Describe** the benefits to employers of using both developmental and administrative approaches to performance management.
3. **Describe** four benefits of an effective performance management system.

Read the 'Regular feedback equals successful performance appraisal' case study and answer questions 4 to 7.

4. **What** is performance management?
5. **List** the advantages of an informal and frequent discussion with employees.
6. **How** can performance appraisal contribute to an employee's professional development?
7. Use an appropriate graphic template to design a document that **summarises** the four-step process of performance management.

20.6 Exam questions

Question 1 (1 mark)

Source: HSC 2013 Business Studies Exam, Section I, Q20

Which of the following is an example of developmental performance management?

A. Reviewing the reward system for all employees
B. Evaluating an online payroll system for employees
C. Improving an individual employee's leadership skills
D. Collecting data to manage the human resources function more effectively

Question 2 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q10

Sam's job is to set goals for employees and give them feedback on the achievement of their goals.

What best describes this process?

A. Dispute resolution
B. Job design
C. Performance management
D. Recruitment

Question 3 (3 marks)

Lohan Sports Shoes has several factories in South-East Asia. Recommend a performance management strategy as a part of human resource strategies to be used in the factories.

Question 4 (6 marks)

Analyse the advantages and disadvantages of developmental and administrative performance management strategies.

More exam questions are available in your learnON title.

20.7 Rewards

SYLLABUS LINK In this subtopic you will learn about rewards (monetary and non-monetary, individual or group, performance pay) as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

A well-planned reward system is a key strategy in attracting, motivating and retaining employees. A rewards system can reinforce strategies to facilitate change or support desirable corporate values, such as a focus on the customer.

monetary rewards those rewards reflected in pay or having financial value

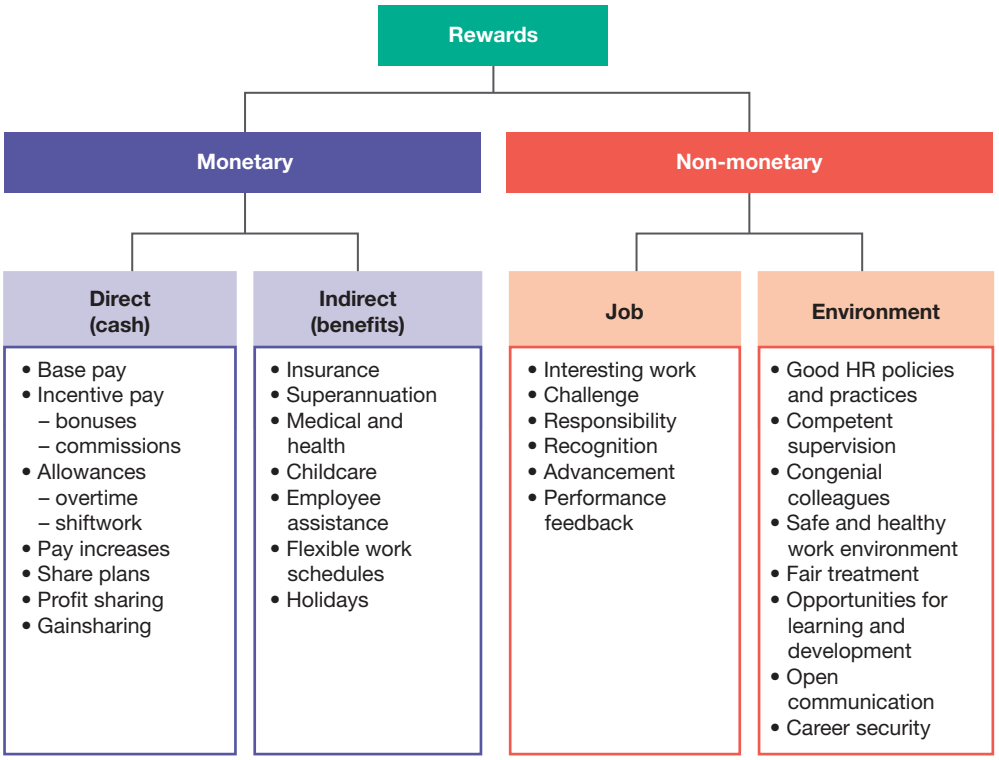
non-monetary rewards those rewards that do not have a financial value, such as social activities or retirement planning

remuneration the financial (e.g. pay) and non-financial (e.g. career security) benefits that employees receive in return for their work effort

20.7.1 Monetary and non-monetary rewards

Rewards can be **monetary** or **non-monetary**, as shown in figure 20.9, and evidence suggests a business's reward policies assist to reinforce its culture and values, and achieve strategic objectives. A business's sustainable competitive advantage is also linked to a **remuneration** system that seeks to encourage and reward employees. Rewards are seen as a significant tool in motivating staff to higher levels of performance.

FIGURE 20.9 Types of employee rewards



BizFACT

Employers need to analyse both financial and non-financial rewards to maximise employee engagement and performance. The demographic characteristics of a diversified workforce (gender, age, ethnicity, occupation) all have an impact upon selecting the most appropriate form of remuneration.

SNAPSHOT

Case study: Motivating employees at Fonda Mexican Restaurant



The word 'Fonda' is used in Mexico to describe a house with an open kitchen, where visitors are always welcome. The Fonda restaurant chain was founded in Melbourne by David Youl and Tim McDonald in 2011, and aims to carry on this tradition of a relaxed and welcoming dining experience. Although the restaurant now operates at seven different sites in Melbourne and one in Sydney, David and Tim have chosen not to make use of a franchise model, as they wish to maintain a consistent management culture across each of the restaurants. This culture encompasses the following features:

- Alignment between the business objectives and employee objectives is given highest priority. This means that employees have a direct interest in improving the profits of the business through a system of profit sharing.
- Each branch of the business is managed by a Restaurant Business Leader (RBL). This person is paid a base salary, which is augmented monthly by a 7 per cent share of the profit of that restaurant. The higher the profit, the larger the amount paid to the RBL. Base salaries are kept relatively low (and in line with legal minimums), but the share in the profits has meant that the actual take home pay is generally higher than the industry average.
- Assisting the RBL in each restaurant is a Senior Assistant Business Leader, who is paid 3 per cent of the profits, and two or three Assistant Business Leaders who are each paid 2 per cent. While base salaries for each of the members of the leadership team is also relatively low, their share of profit inevitably means they actually take home salaries that are higher than comparable employees in other restaurants.
- The leadership teams meet together monthly with the business owners, when profit share payments are made and ideas for improving productivity are shared. Leaders are encouraged to learn from each other and to celebrate the achievement of business goals.
- Every three months, all staff meet for a 'Buzz Breakfast', at which a wide variety of staff achievements are reported and celebrated.
- An annual awards dinner is held each year for all employees, and this is seen as the company's equivalent to a Brownlow Medal celebration (the AFL best and fairest award).

- Each May, the leadership teams meet to set the objectives for the next financial year. These objectives are broken down into monthly, weekly and even daily goals, and these goals are made measurable and communicated to all staff. It is not unusual for customers in one of the restaurants to see staff stop for 20 seconds and break out into cheering and applause when a daily sales goal or a food preparation time goal has been achieved.
- Staff are known as 'Fondarians', and are encouraged to see themselves as important team members. Ideas and suggestions for improvement from all staff is strongly encouraged, acknowledged regularly and celebrated.

In 2015, Fonda was recognised by the *Business Review Weekly* as the 22nd fastest growing company in Australia, up from 39th the previous year. Aligning staff motivation with business objectives has proved a recipe for success for Fonda in the very crowded and competitive hospitality industry.

20.7.2 Individual or group reward

Rewards are often related to individual performance; however, this can lead to conflict and rivalry if not managed effectively. All individuals are dependent on others and on efficient workplace systems to achieve high-quality performance. Increasing use of group- and team-based structures have increased the need for cooperation and made it difficult to distinguish performance of individuals within teams.

Many tools can be used by the human resource manager in developing a reward system. For example, a grid or matrix could be drawn up to assess the objectives of each reward and the overall effectiveness of the system (an example is shown in table 20.5).

TABLE 20.5 A rewards matrix for a business

	Reward objectives					
Reward component	**Attract**	**Retain**	**Productivity**	**Individual contribution**	**Employee security**	**Company performance**
Base salary	✓	✓				
Gain-sharing plan			✓			
Performance incentive		✓		✓		
Corporate profit share	✓					✓
Superannuation	✓	✓				
Other benefits		✓			✓	
Career planning		✓	✓		✓	

FIGURE 20.10 A team-based reward system encourages cooperation between the employees in the business. However, it can result in the 'free-rider' phenomenon: the team member who contributes little to overall performance but receives the reward nevertheless.



BizFACT

Wages growth for Australia's workers is among the lowest in the industrialised world and for more than one-third of workers, wages aren't growing at all.

Reasons given include workers not changing jobs, caps on public service salaries and the loss of worker power due to the decline in trade unionism.

Key issues to consider in designing a reward and benefits system in terms of the business include:

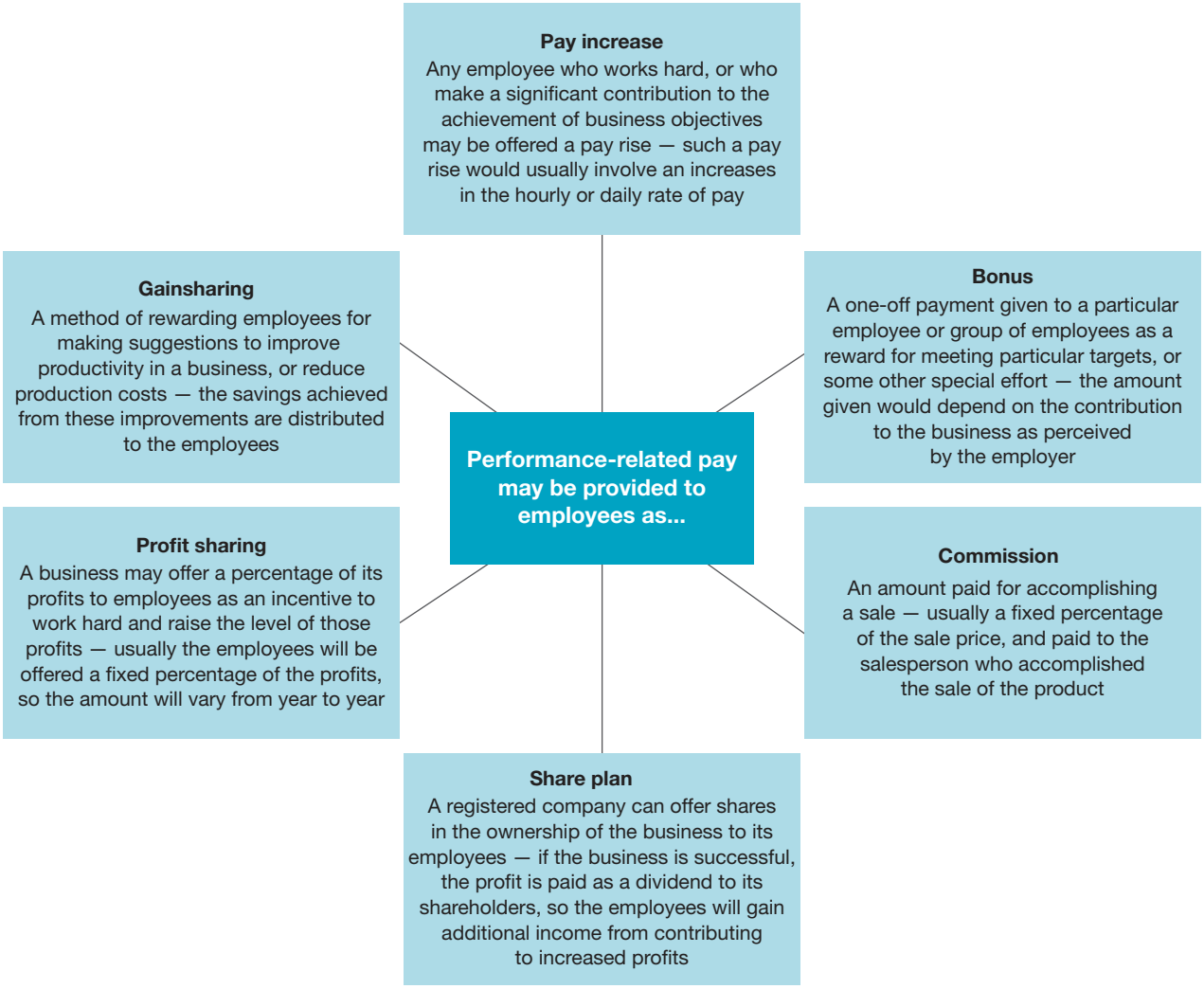
- business strategy
- economic conditions — supply and demand for labour and skills shortages
- organisational objectives of rewards
- rewards and benefits of competitors
- relevant awards and agreements, minimum employment standards
- union power
- profitability/viability of the business.

Performance-related pay is a means of rewarding employees through monetary compensation when they perform their duties in a manner that equals or exceeds a set of pre-determined goals or criteria. It is usually designed as a means of motivating employees. An employer can provide motivation with direct payments to employees, such as pay increases, bonuses and commissions, as well as other methods including share plans, profit sharing and gainsharing (see figure 20.11). Employees who achieve the set standards, or reach above the standards, will be motivated to work hard at their job and perform well in order to receive the financial incentive.

Reward systems that are not clear or fair, or where employees believe there has been favouritism or bias, can lead to internal politicking and conflict, loss of trust and motivation, and higher levels of labour turnover.

The reward system should aim to motivate staff and be equitable, clearly communicated, defensible, relevant, cost effective and integrated with the corporate strategy. It must also be simple to understand and administer, and consistently applied to all employees.

FIGURE 20.11 There are a number of ways in which a business may provide performance-related pay to employees.



SNAPSHOT

Case study: Red Star Fashions — the debate around bonuses

Maureen Brady, CEO of Red Star Fashions, pushed the thin pile of papers away and sighed. 'It seems that we have a serious problem. Employee productivity is in decline. We are losing our competitiveness. At this rate, we will make a financial loss by year end. Does anyone have anything to say?'

'Yes', snapped Carolyn Simon, Finance Director. 'The problem is our people are not motivated. Everyone gets paid the same irrespective of their performance. The best people became demotivated — everyone sinks to the lowest common denominator.'



'I agree', interjected Nick Dalmaris, Marketing Manager. 'We don't reward performance. We ignore it. It is no wonder that our people aren't motivated. Why should they be? What do they get for doing a good job? Nothing. This place has become a safe haven for non-performers. They get paid regardless and they know they can't or won't be sacked. It should come as no surprise that we are losing our competitiveness.'

'What do you suggest then?' asked Maureen.

'Pay people on the basis of their performance, not on how long they have been with the company', replied Nick.

'Nick is right', Carolyn said enthusiastically. 'We need to get away from seniority and switch to a system of performance-based rewards. We need a bonus system. People should get a bonus for outstanding performance.'

'Stephanie, you have been silent so far, what are your thoughts?'

Stephanie Magolis, HR manager paused, then said, 'The culture of this company is built around teamwork — working together, sharing our knowledge and experiences. Individual performance rewards will destroy the collegiality that exists. Individual rewards promote competition. They will trash our cooperative culture. The present system is fair. Seniority-based rewards recognise loyalty and promote harmony. Individual performance payments do not. All that will happen is that people will spend all their time manoeuvring themselves to gain favour with their bosses. I am opposed to any change. I believe that the introduction of individual performance bonuses would have a most negative effect on the moral fibre of this company.'

'For heaven's sake, Stephanie, you must understand that if we wish to attract and retain talented people, we have to reward them appropriately. Why would a top performer come here?'

'We want a champion team, not a team of champions', Stephanie shot back. 'Performance pay is not about performance, it is about competition and the destruction of a cooperative corporate culture.'

KEY IDEAS

- Rewards management is a system of monetary and non-monetary, and intrinsic and extrinsic rewards to attract, motivate and retain employees for their effort and performance.
- An effective reward system is equitable, clearly communicated, relevant, cost effective, simple to administer and aligned with the business's goals.

20.7 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

20.7 Quick quiz on | **20.7 Exercise** | **20.7 Exam questions**

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 6	1, 3, 4, 5, 7, 8	9

20.7 Exercise

Revision

1. **Distinguish** between monetary and non-monetary rewards, and explain why a mix is best.
2. **Outline** the main features of a well-designed rewards system.

Read the 'Motivating employees at Fonda Mexican restaurant' case study and answer questions 3 to 5.

3. **How** do the owners of Fonda Mexican Restaurants make use of both monetary and non-monetary strategies to motivate staff?
4. **How** are the business objectives of Fonda Mexican Restaurants aligned with the objectives of employees in those restaurants?
5. **Explain** why customers at a Fonda restaurant may occasionally see employees breaking out into cheers and applause, and congratulating each other.

Read the 'Red Star Fashions — the debate around bonuses' case study and answer questions 6 to 8.

6. **Outline** the opposing arguments presented. Justify your own position.
7. **Discuss** the effect of a reward system on the culture of an organisation.
8. Project into the role of HR manager, and **propose** recommendations that you would make to improve the productivity and competitiveness of Red Star Fashions.

Extension

9. In groups, **create** a rewards system either for staff in a university or for journalists at a large metropolitan newspaper. Justify your strategy.

20.7 Exam questions

Question 1 (2 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q23a

A business has been rapidly expanding and requires additional staff.

a. Describe ONE monetary reward that could be offered during the recruitment process. **(2 marks)**
b. Describe ONE non-monetary reward that could be offered during the recruitment process. **(2 marks)**

Question 2 (1 mark)

Source: HSC 2015 Business Studies Exam, Section I, Q11

Which of the following is an example of a business using performance pay?

A. Emily is paid penalty rates for working on a public holiday.
B. Mike receives a gift voucher from his supervisor for Christmas.
C. Jamie is paid 5% above the level set in his enterprise agreement.
D. Sally's department receives a bonus for meeting its sales target.

Question 3 (4 marks)

Source: HSC 2013 Business Studies Exam, Section II, Q21a

How can employee rewards be used to improve business performance? Use an example of a specific reward to support your answer.

Question 4 (1 mark)

Source: Adapted from HSC 2009 Business Studies Exam, Section I, Q13

Which strategy may achieve effective human resource management for both employers and employees?

A. Outsourcing product manufacture
B. Determining levels of staff turnover
C. Offering share options to employees
D. Estimating the cost of retrenchment packages

Question 5 (2 marks)

Source: HSC 2002 Business Studies Exam, Section II, Q23a

Sandra owns a computer software business selling a range of games and small-business packages. She employs two full-time and three part-time sales staff.

Describe ONE example of a financial reward and ONE example of a non-financial reward that Sandra could use to motivate her staff.

More exam questions are available in your learnON title.

20.8 Global strategies

SYLLABUS LINK In this subtopic you will learn about global costs, skills and supply as a strategy in human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Globalisation of business, as well as technological developments in the internet, human resource applications and telecommunications, has significantly increased the competition faced by any business. These advances have also increased the complexity of managing human resources.

Issues such as high domestic labour costs, a skills shortage, especially apparent in some industries, and a relatively small labour pool have made businesses re-think the management of human resources.

The globalisation that has affected a number of Australian businesses has brought with it the need for change. Increasing competition, shareholder demands for higher returns, privatisation, outsourcing and restructuring have all forced businesses to analyse their strategic direction. Most of these strategic decisions have at their core matters relating to labour costs, skills and supply.

Australia's higher living standards bring with it the expectation of better wages and salaries for workers. Employers are also faced with on-costs such as superannuation that add to the expense of remunerating local staff.

Some businesses have found that these higher labour costs reduce competitiveness and as a result have made the decision to restructure their workforce, including outsourcing some functions to lower labour cost countries. Others have established **subsidiaries** off-shore to take advantage of the opportunity to reduce production costs and gain access to new markets.

Countries such as China have factories able to produce goods at very competitive prices. This has attracted the attention of Australian businesses, which have moved production to China because it is cheaper, causing Australian factories to close.

For example, the Australian company Pacific Brands, known for its Bonds and Holeproof products (among others), relocated its manufacturing to China at a cost of some 1800 Australian jobs as it was no longer sustainable to keep its Australian factories open.

The airline Qantas also faced scrutiny for its ongoing restructuring of its domestic maintenance facilities that have resulted in a loss of 1550 jobs since 2014. Much of the work previously done in regional centres such as Avalon, Victoria, was relocated to lower labour cost countries such as Singapore and Hong Kong.

Other activities such as basic accounting and legal work, including the processing of insurance policies, are being outsourced to countries such as India. India has a large pool of English-speaking, highly literate and tertiary-educated workers able to provide the type of services desired by Australian businesses at a much lower rate than if the work was done in Australia.

The issue of labour force skills has also been significant for many Australian businesses. For some time now local managers have expressed their concern that there is a major issue relating to matching the skills possessed by Australian workers and those needed by business. It is a belief widely held by many of these managers that the Australian education system has not produced workers with the necessary numeracy and literacy skills.

Estimates are that Australian businesses will need in the vicinity of 2 million workers in the next few years and more than 5 million by the start of the next decade. Moreover, this shortage is seen as a major impediment to improving productivity in the workplace. This skills shortage is often blamed on the education system and on some employers who are more intent on importing cheaper labour, outsourcing or recruiting overseas. Australia will have a shortfall of 500 000 workers by the end of the decade and the skills shortage remains an issue as Australia continues to pursue opportunities for economic growth.

subsidiary a company that is owned by another company (referred to as the parent) and it is often located in another country

Short-term initiatives have been used to overcome the shortage of workers. The Temporary Skill Shortage (TSS) visa was introduced in March 2018. It replaced the temporary work (skilled) visa — the 457 visa. The TSS visa program comprises a short-term (up to two years) visa or a medium-term (up to four years) visa and will support businesses in addressing genuine skill shortages in their workforce. It aims to align with the skill needs of the Australian labour market and tightens eligibility requirements for employer sponsored permanent skilled visas.

Temporary visas serve the economy well in times of skills shortages in the short term; for example, in periods of economic growth. They are especially useful in attracting skilled workers to remote areas where Australian workers are reluctant to go especially in the medical services, engineering and skilled trades. A solid commitment to training Australia's workers is, however, the long-term solution.

The ongoing economic problems in Europe, with a number of long-term unemployed but highly skilled workers, is attracting the interest of some Australian businesses in search of workers. Europe, South Africa, the United States and the United Kingdom are also providing some Australian businesses with highly experienced senior management.

The supply of workers continues to be a problem for a country of 25 million people. China and India with their huge populations have an abundance of workers keen to find well-paid employment overseas. Australia is allowing skilled workers from these countries to migrate and work here, especially in difficult-to-fill occupations such as IT, and to replace the 100 000 workers Australia loses to business migration each year.

Businesses are sometimes attracted by the lower labour costs on offer in some countries; however, this needs to be more fully explored. Countries like China have a huge supply of labour but much of it is ageing and poorly qualified with low literacy levels. This is compounded by a shortage of younger workers and the limited availability of quality managers. Qualified staff tend to be concentrated in the major cities such as Beijing or Shanghai. Consequently, companies looking to China as a destination for expansion often face higher human resource costs and any benefits derived from such relocation decisions need to be considered in light of these factors.

It is often said that in China nothing is ever black and white — everything is negotiable. Worker rights are often ignored. The right to strike does not exist in law but there is no current law that expressly prohibits it. In addition, independent trade unions are not permitted (the government controls all unions via the All China Federation of Trade Unions) but instead are seen as an instrument of government policy where worker entitlements are secondary to the promotion of government interests.

Further, the change to a more market-based economy in China means there are inconsistencies in workplace laws that can appear to support unscrupulous management practices. This has given rise to criticism of some multinational businesses that have sought to benefit from this lack of structure and taken advantage of China's supply of low-cost labour in situations where the required skill level is relatively low.

Recently there is growing concern that global supply chains are profiting from low cost, plentiful labour supplies in countries such as China. Moreover, some of these vulnerable workers are providing cheap clothes for Australians in conditions that can only be described as modern-day slavery.

SNAPSHOT

Case study: *Four Corners'* forced labour exposé shows why you might be wearing slave-made clothes

With China's western-most province of Xinjiang being turned into a mass internment camp, last night's ABC *Four Corners* program reported on the Chinese Communist Party's alleged plans to put up to a million detained Uyghurs to work.

The Uyghurs are Turkic-speaking Muslims from the Central Asian region. The largest population live in China's autonomous Xinjiang region, in the country's north-west.

Muslim minorities are being arbitrarily arrested and imprisoned. It's estimated around one million Uyghurs have been detained in what China calls 'vocational training centres'.

These are purpose-built detention centres, some of which resemble high-security jails. A recent ABC investigation found 28 detention camps had expanded across Xinjiang as part of China's program of subjugation.

There is growing evidence of human rights violations inside the centres as well as reports of deaths in custody and forced labour.

The exposé highlights how global supply chains make it possible for the clothes you're wearing, and many other things you own, to have been made using slavery.

The program featured the cases of several women who say they have been forced to work in textile factories. According to China scholar Adrian Zenz, government documents reveal plans for 're-education' through labour. Satellite photos show what look like large warehouses close to detention camps.

Target, Cotton On, Jeanswest, Dangerfield, IKEA and H&M are among the brands in Australia sourcing cotton from Xinjiang, according to *Four Corners*. In response to questions from the ABC, Target and Cotton On declared they would investigate their relationships with suppliers.

Modern slavery: a snapshot

For many of us it is hard to believe modern slavery is now more prevalent than at any time in history.

But the ubiquity and lack of accountability in global supply chains mean an estimated 25 million people around the world are in forced labour. A further 15 million are in forced marriage.

About two-thirds of the total number of people in modern slavery are in the Asia-Pacific region, where most Australian companies source their materials and products.

The problem is so widespread it's unlikely any companies' operations or supply chains are completely free of modern slavery.

Yet many businesses are unaware of what modern slavery is and what it might look like in their operations and supply chains. And some companies — and their customers — may be complicit in creating a 'race to bottom' by demanding cheaper goods and services without checks on social (and environmental) credentials.

Australia's legal reforms

This problem was recognised with Australia passing modern slavery legislation last year. The *Modern Slavery Act 2018* requires businesses of a certain size to report their efforts to keep their supply chains slavery-free. The requirements came into effect this month.

Modelled on the UK *Modern Slavery Act 2015*, Australia's law requires businesses with a consolidated annual revenue of more than $100 million a year to publish an annual modern slavery statement.

The statement must address seven mandatory criteria (including risks in the business' operations and supply chains and the actions taken to address those risks).

The government has the power to publicly name those that fail to comply, but not to fine or penalise them in other ways. It is hoped fear of shaming will be enough incentive to avoid the reputational, financial and other risks that might arise from public scrutiny.

Without penalties, civil, shareholder and consumer activism will be crucial to motivate businesses.

If nothing else, as shoppers we can become better informed about the risks in business supply chains and challenge companies and governments to do better through social media and other avenues. Each purchase of a good or service can be an ethical choice.

Source: Yvette Salim, 'Four Corners' forced labour exposé shows why you might be wearing slave-made clothes', *The Conversation*, 16 July 2019.

KEY IDEAS

- Globalisation brings issues related to managing human resources. Access to sufficient numbers of skilled workers affects business decision making.
- The rapid growth of global outsourcing illustrates the potential for firms to develop creative strategies that access lower labour cost, while complying with regulations and pay scales in overseas countries.

20.8 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

20.8 Quick quiz on	20.8 Exercise	20.8 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
2, 3, 4, 5	1	6

20.8 Exercise

Revision

Read the *'Four Corners'* forced labour exposé shows why you might be wearing slave-made clothes' case study and answer questions 1 to 4.

1. **Explain** the relationship between the Uyghurs in western China and retailers Target, Cotton On and Jeanswest in Australia.
2. **Outline** the extent of modern slavery throughout the world.
3. **Describe** Australia's legal reforms in the area of modern slavery.
4. **Identify** the benefits of the closer scrutiny of global supply chains and the issue of slavery.

Extension

5. **Outline** the 'push' factors that may lead business managers to consider a shift to global rather than local production.
6. The global pandemic has interrupted the supply of 'backpackers' who are usually required by many businesses in Australia. **Evaluate** how this has been addressed.

20.8 Exam questions

Question 1 (2 marks)

Source: HSC 2003 Business Studies Exam, Section II, Q23a

Watermelon Electronics is considering setting up a subsidiary in a developing country to manufacture some of its components. It could benefit from tax advantages and lower production costs, yet faces potential problems of a shortage of skilled labour and differences in labour law.

Outline ONE human resources strategy that Watermelon Electronics could use to overcome the problem of a shortage of skilled labour.

Question 2 (4 marks)

Eagles Enterprises is considering relocating the manufacturing part of its operations to a developing country. Cost is not a concern.

Describe TWO other issues that the human resource management of Eagles Enterprises should consider before relocating.

Question 3 (1 mark)

Ella Ltd is spending a lot of time and money to recruit the best person to manage its latest mining project in Africa. Which issue of global human resource management is of most concern to Ella Ltd in this case?

A. Skills
B. Supply
C. Cost
D. Relocation

Question 4 (2 marks)

Explain how cost is an issue in global human resource management.

More exam questions are available in your learnON title.

20.9 Workplace disputes

SYLLABUS LINK In this subtopic you will learn about workplace disputes (resolution, including negotiation, mediation, grievance procedures, involvement of courts and tribunals) as a strategy in human resource management and learn to analyse the causes of two workplace disputes and the strategies used to resolve them.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

20.9.1 Different types of disputes

Disputes are conflicts, disagreements or dissatisfaction between individuals and/or groups. Conflict between stakeholders is inevitable in workplaces. Stakeholders often have conflicting interests, particularly over the degree to which employees should share in the profits.

Workplace conflict can lead to problems such as higher levels of absenteeism, low productivity, legal claims and high staff turnover, which may be even more costly in the long run.

The Australian Bureau of Statistics (ABS) maintains statistics about official, or overt, disputes. An **industrial dispute** is a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work.

Strikes refer to situations in which workers withdraw their labour. They are the most overt form of industrial action and aim to attract publicity and support for the employees' case. Strike action is more common in public sector organisations and in the mining sector.

Lockouts occur when employers close the entrance to a workplace and refuse admission to the workers. In some lockouts, management has been brought in by helicopter to avoid a **picket** line of workers. Lockouts have been used frequently in long disputes in manufacturing to promote concession bargaining, to push employees to sign individual agreements, and in response to strike action.

Each withdrawal or refusal is made to enforce a demand, to resist a demand or to express a grievance. Legal claims for matters such as discrimination, harassment and bullying are not included in these disputes.

The level of disputes varies within and between industries and businesses. Some employers seek to minimise conflict, others stifle it through tough tactics, while others manage more collaboratively through negotiation with staff and unions.

industrial dispute a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work

strikes situations in which workers withdraw their labour

lockouts when employers close the entrance to a workplace and refuse admission to the workers

pickets protests that take place outside the workplace, generally associated with a strike. Unionists stop the delivery of goods and try to stop the entry of non-union labour into the workplace.

FIGURE 20.12 Strikes can attract publicity and support for the employees' case.



BizFACT

The types of strikes include the following:

- Sympathy strikes are those called in support of a group of workers already on strike.
- Rolling strikes occur over a period of time, in between working periods.
- Rotating and revolving strikes occur where workers at different locations take turns to strike.
- Political strikes involve employees taking strike action over political issues, against government policy or actions.
- Wildcat strikes are those that take place without union approval.
- Lightning strikes occur without an employer being notified.
- General strikes involve a large number of workers in different industries going on strike simultaneously.
- Stop-work meetings involve employees stopping work to hold a meeting on an industrial issue during work time.

Causes of workplace disputes

The major causes of disputes recognised by the ABS are disputes relating to negotiation of awards and enterprise agreements. These issues typically include disputes about:

- remuneration. This includes matters such as wages, allowances, entitlements and superannuation.
- employment conditions. These include matters such as working hours, leave, benefits and other general employment conditions.
- job security issues. These include retrenchment of employees, downsizing, restructuring, use of contractors, outsourcing, re-classification of the workforce, and other industry-related matters (see the following case study).

FIGURE 20.13 A picket line is formed by striking workers to prevent vehicles and non-striking workers from entering the workplace.



Matters outside agreements also cause disputes, for example:

- health and safety. These matters typically relate to physical working conditions, including safety matters, and workers' compensation provisions, protective clothing and equipment, uncomfortable working conditions, employee amenities, equipment condition, and overly strenuous physical tasks.
- managerial policy. These issues include decisions and policies of line managers, such as disciplinary matters, suspensions, discrimination, decisions that impact upon work and family issues, production limits or quotas, principles of promotion, and other work practices.
- union issues. These matters relate to employer approaches to the union, inter-union and intra-union disputes (e.g. demarcation disputes), sympathy stoppages in support of employees in another industry, and recognition of union activities.
- political or social protests.

BizFACT

Managerial policy is one of the most common causes of disputes. Disputes arising from managerial policy may be related to award restructuring, terms and conditions of employment, enterprise bargaining, production limits or quotas, promotion, discipline, personal disagreements and changing work practices.

SNAPSHOT

Case study: Analysing the causes of two workplace disputes and the strategies used to resolve them

Workplace dispute 1 — Hutchinson Ports Australia and the Maritime Union of Australia

Hutchinson Ports Australia used an unusual procedure for advising nearly 100 workers in both its Sydney and Brisbane terminals that their services were no longer required.

In a text message and email sent to workers late at night they were informed that:

> . . . your position will not be retained. There are no redeployment opportunities. The intended last day of your employment will be Friday 14 August 2015. Accordingly you are [sic] will not be required to attend work effective immediately. We will of course pay you your normal salary to your last date of employment.

Disbelieving (and now sacked) workers were locked out of the business the next day and although they and 100 supporters formed on-site pickets in both Sydney and Brisbane, management was adamant that the workers would not be recalled. Workers across the sites responded with a four-hour stop work meeting to give them an opportunity to consider their next step in support of sacked colleagues.



The Maritime Union of Australia was called in on behalf of its members at the business and it immediately lodged the matter with the Fair Work Commission and the Federal Court of Australia, arguing Hutchison Ports breached the enterprise agreement by failing to properly consult workers and caring little about a dispute resolution clause before announcing the redundancies.

A court-ordered injunction was issued to stop the dismissals and the on-site pickets were subsequently suspended. Management was able to meet with the union to articulate its concerns (believed to be about workplace inefficiencies) and a satisfactory settlement to the dispute sought.

The company eventually decided that it would accept voluntary redundancies in lieu of the sackings and about 25 per cent of the workers took this option. A further incentive for redundant employees came in the form of an additional payment of $20 000 above their legal entitlements.

In return the company would now be able to employ workers on a casual basis; however, the redundant workers could apply for these positions.

Workers had a slight increase in the length of the working week to 32 hours and they were also expected to offer some flexibility around rostering.

Hutchinson Ports Australia stated that it would benefit by being able to be more competitive through effective cost management and indicated that as the opportunity presented itself workers would be allowed to return to full-time work should they choose to do so.

Workplace dispute 2 — Bathurst Hospital and the Health Services Union

Some 150 workers supported by the Health Services Union (HSU) recently staged a four-hour strike to raise awareness of an alleged culture of bullying, harassment and intimidation at Bathurst Hospital. Catering, security, cleaners and health professionals employed at the hospital intended their demonstration to be a two-hour stop-work meeting but due to a perceived lack of interest by management it was extended. Further, if a satisfactory outcome was not achieved the HSU and its members were prepared to call a 24-hour strike if necessary.

The HSU called for an investigation into claims of a poor work culture at Bathurst Hospital, which they argued had developed over the previous seven years, rife with low morale, bullying and intimidation, unfavourable roster changes, health and safety concerns and poor pay rates.

As the stop-work meeting entered its fourth hour, a spokeswoman for Bathurst Hospital indicated that the workers' claims were being taken seriously and that an independent consultant would be employed to investigate the staff grievances.

At the same time Bathurst Hospital had to deal with a long-running dispute over other staffing issues including unreasonable workloads. Claims that staffing numbers were inadequate and that this placed additional pressure on workers were made before the Industrial Relations Commission.

A spokesman on behalf of the hospital said that meaningful discussions were being had and that progress was being made.

BizFACT

Most workplaces have never experienced industrial disputes such as strikes or lockouts. Many firms now try to develop a work environment in which disputes are minimised through collaborative working relationships and by training staff in procedures, policies and guidelines for managing disputes. Effective human resources requires prompt and equitable settlement of disputes.

20.9.2 Resolution of disputes

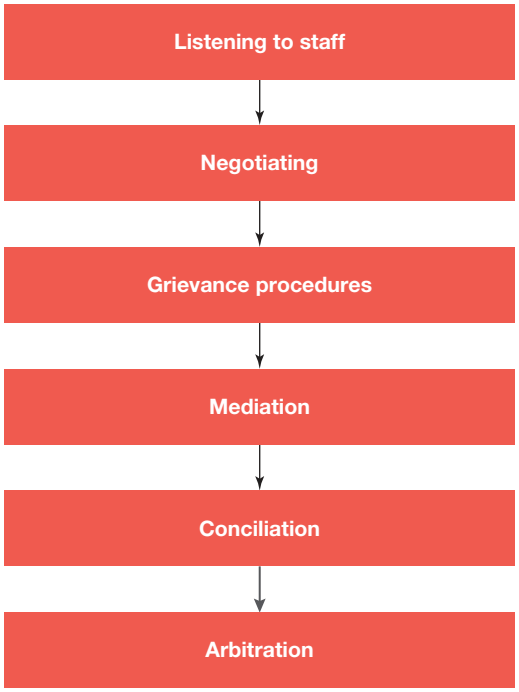
The key stakeholders involved in resolving disputes include employees, employers, governments, trade unions, employer associations, courts and industrial tribunals (see figure 20.15). The Fair Work Commission describes dispute resolution as the processes whereby disputes are brought to an end. The three processes are:

1. a negotiated outcome — the parties work out the solution for themselves
2. a mediated outcome — an independent mediator assists with the development of an agreement
3. an arbitrated/adjudicated agreement — an independent arbitrator or court determines how the matter will be resolved and makes a legally binding order.

Before either party may take protected industrial action, there must also be proof that both parties have attempted to bargain **in good faith**. For cases where collective or enterprise bargaining does not resolve disputes in the workplace, conciliation is still available through the Fair Work Commission.

When disputes develop, a number of methods can be used to try to resolve them.

FIGURE 20.14 A typical dispute resolution process



Negotiation

Negotiation is a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement. This process can benefit the parties involved by increasing their knowledge of company policy, business's objectives, workers' concerns and issues involved in implementing change.

Most Australian industrial disputes are resolved by resumption of work, without negotiation, such as following a stop-work meeting. This may later lead to an agreement change. Most other disputes are resolved by negotiation without the intervention of a third party. In such cases, employees return to work following industrial action for a pre-determined period (such as after a 24-hour strike). Options available to the parties involved may be determined by the nature of the industrial agreement covering employees (federal/state) and the goals of the parties.

Mediation

Mediation is the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party. The third party may be independent and agreed on by key parties in a dispute, or a representative from a business, tribunal or government agency, such as the Fair Work Commission, the Australian Human Rights Commission (AHRC) or the Anti-Discrimination Board (in New South Wales).

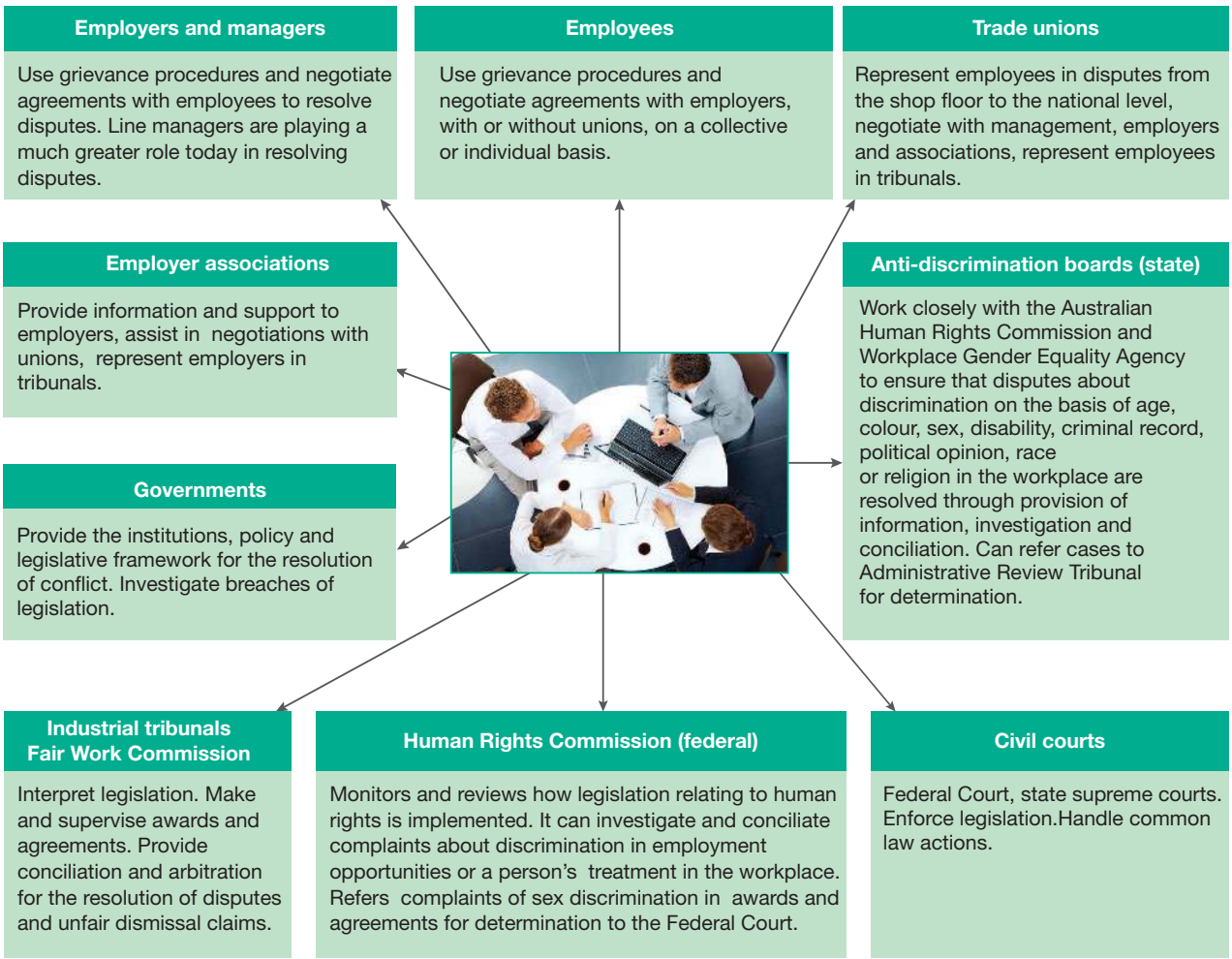
Mediation as an alternative dispute resolution technique is increasingly popular in Australia. It allows the parties to become empowered by resolving their own disputes, and it reduces the risk of disputes escalating and leading to expensive legal costs or industrial action. It is often required as the fist step in the resolution of a dispute.

in good faith means the parties meet with a willingness to reach an agreement

negotiation a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement

mediation the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party

FIGURE 20.15 Key stakeholders and their role in resolving workplace disputes



Grievance procedures

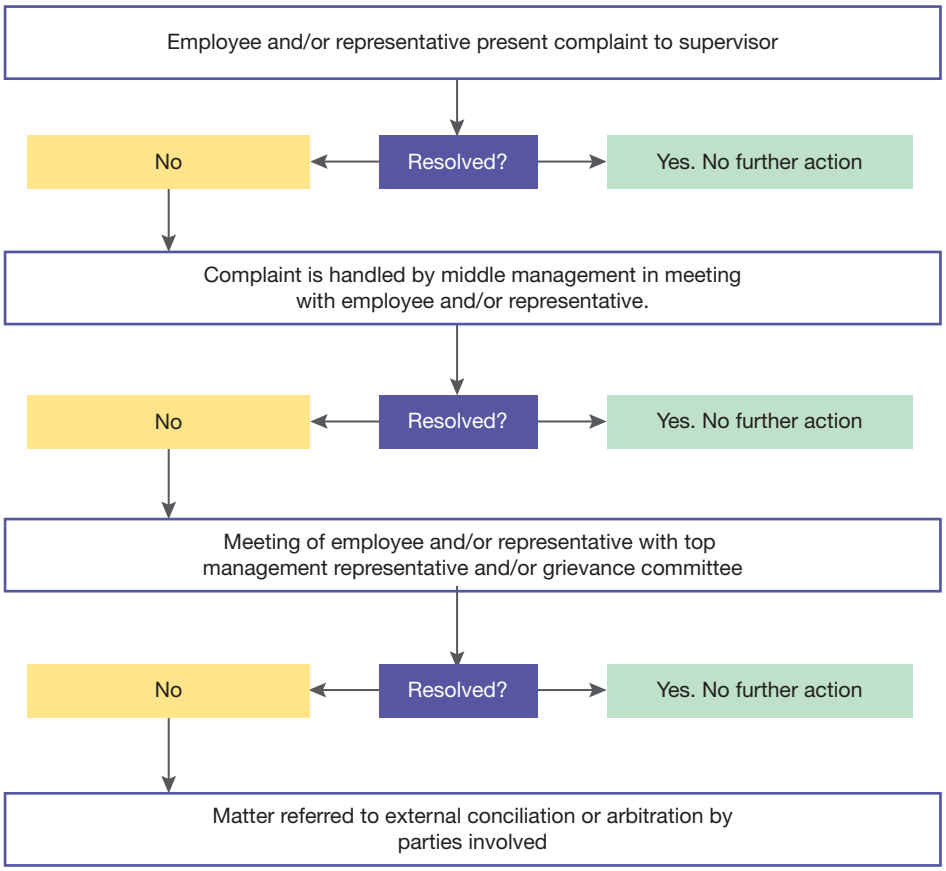
Grievance procedures are formal procedures, generally written into an award or agreement, that state agreed processes to resolve disputes in the workplace. Grievance procedures are useful in reducing the risk of an issue rapidly becoming a serious dispute. Most businesses have established a formal process, now required in modern awards and other agreements, by which issues can be handled. The steps in a typical grievance procedure are shown in figure 20.16.

grievance procedures formal procedures, generally written into an award or agreement, that state agreed processes to resolve disputes in the workplace

BizFACT

Around 70 per cent of managers are involved in grievance handling, and cite the most common issues as personality conflicts, allowances and pay, and discipline.

FIGURE 20.16 Steps in a formalised grievance procedure. Complaints may be resolved at any of the stages indicated.



SNAPSHOT

Case study: Workplace disputes — how to extinguish the flame and avoid a fire



When an employee has a grievance it means they have a complaint about a situation in the workplace they perceive as unfair. It may be a situation where the employee feels they are working in an unsafe environment. For example, an employee grievance was soon referred to the union when management ignored the complaints made by employees who constantly tore their clothing on the old wooden furniture in the office. This issue finally came to a head when an employee suffered from a splinter in their knee. The frustrated employee went to their union and that was the catalyst for management to agree to purchase new furniture.

Research has shown that a manager's skill in averting the escalation of such workplace disputes is critical. According to a senior human resource management executive at ANZ, encouraging communication and listening to staff is one way to avert potential problems in the workplace. He says: 'What we have done quite consciously is to build better communications with our staff — direct relationships face to face with our staff for matters that

affect them in the workplace and there is no substitute for that'. Supervisors and human resource managers are recommended to approach grievances in the first instance at the workplace level in the following ways:

- Treat the grievance seriously and in private.
- Listen to what the employee is saying.
- Establish exactly what the problem is.
- Identify the source or sources of dissatisfaction.
- Remain calm. Lost tempers and accusations can onlyescalate bad feeling.



After the manager has heard the grievance, some time should be set aside for establishing the facts. This could mean visiting the workplace to see firsthand what the problem is and talking to witnesses that the employee has identified. Lengthy delays in responding to the employee grievance should be avoided and a decision, once made, must be communicated. The reason behind the decision should be clearly articulated. It is considered unhelpful to just pass off the decision by saying to the employee that it is 'management policy'.

The procedure described is based on the concept of natural justice, which means that employees must be given a fair hearing and that decisions should be made without bias.

Effective grievance procedures require a full description of the complaint to be made by the employee(s) with the complaint. The person the grievance is made against should be given details of the allegation and an opportunity to provide their views. The process may deal with individual or collective issues, and matters such as changes being implemented in the workplace that will affect or cause conflict between staff. It is a useful strategy for resolving issues before they escalate. The Fair Work Commission recommends that issues be quickly resolved, handled sensitively and professionally, and in a manner that is fair, so that employees have confidence in the process.

Involvement of courts and tribunals

Industrial disputes that escalate to the level of courts and tribunals are most likely to occur when disputes have passed their nominal expiry date, bargaining has commenced towards a new agreement, and negotiations have failed. Employees and employers then enter a period where industrial action may be protected until a new agreement is developed.

Conciliation and arbitration

When a dispute has not been resolved through negotiation at the workplace, it may be referred to the Fair Work Commission (see the next case study), who will appoint a conciliation member to hear both sides of the dispute. Conciliation is a process where a third party is involved in helping two other parties reach an agreement. The conciliation member calls a conference and attempts to help both sides reach an agreement. The member may require all parties to continue negotiations, reduce the ambit of the dispute or develop other strategies to resolve the dispute, then report back for another conference.

If conciliation fails, the matter may be referred to arbitration, if it is in the award or agreement, or if the parties agree. Arbitration is a process where a third party hears both sides of a dispute and makes a legally binding decision to resolve the dispute.

In this situation, a member or a panel of members hears both sides of the dispute in a more formal, court-like setting. A judgement, for example an **order**, is handed down based on the merits of the evidence that becomes legally binding on all parties. Orders may end a restrictive work practice or behaviour, such as a lockout, or require a secret ballot of union members if strike action is proposed. The Fair Work Commission may also order that staff be reinstated or that the parties return to the tribunal at a later date for further negotiations.

orders decisions that require employees or employers to carry out a direction from the tribunal. They may be inserted in awards or agreements.

SNAPSHOT

Case study: The Fair Work Commission — dispute resolution

When a dispute is not resolved in the workplace, it may be referred to a third party, such as the Fair Work Commission, to assist with the resolution. The role of the Fair Work Commission is to ensure that the parties play by the rules of the *Fair Work Act 2009*. Clear rules provide certainty and consistency for all stakeholders. The Fair Work Commission's role in resolving disputes includes:

- providing conciliation, mediation, recommendations and opinions to parties in disputes
- hearing and authorising applications for protected industrial action. For industrial action to be lawful it must be protected industrial action
- hearing, conciliating and making determinations on unfair dismissal claims
- suspension or termination of bargaining periods or protected action or unprotected action. This may occur where substantial harm may be done, or is imminent, to the parties involved or to a third party, the community or the economy. This is enforceable through orders in the courts.



The Fair Work Commission is empowered to deal with disputes relating to:

- disputes under the terms of an award or a collective or enterprise agreement
- bargaining disputes
- disputes arising under the general protections provisions.

Under the Fair Work Act, protection has been provided against adverse actions that may cause discrimination or disadvantage in the workplace. The aim of the act is to protect workplace rights, including the right to bargain freely and not to suffer from discrimination.

FIGURE 20.17 During arbitration, an independent third party is brought in to hear submissions from parties who are in dispute.



BizFACT

Conciliation usually means that the solution is owned by the parties to the dispute, whereas arbitration means that the decision is imposed upon the parties.

A conciliated outcome will mean that both parties are committed to making the decision successful, whereas an arbitrated result will more than likely mean a winner and a loser and some resentment.

Common law action

Common law action is open to any party involved in or affected by industrial action. Parties may make direct claims for damages caused by the parties taking the action, or for breach of contract resulting from such action. An employer may ask a state or territory supreme court or the Federal Court for an injunction or stop order to prevent unlawful interference with the employer's trade or business, for example where a nuisance is created by a picket line. This option is not available if the action is a protected action during a bargaining period. Such action is costly and generally considered a 'last resort'. Common law action in civil courts is also available to those on individual common law contracts of employment disputing matters not covered in legislation or relevant awards.

FIGURE 20.18 One of the benefits of the successful resolution of industrial conflict is improved working relationships.



BizFACT

The *Fair Work Act 2009* provides protections of rights, including:

- workplace rights
- the right to engage in industrial activities
- the right to be free from unlawful discrimination
- the right to be free from undue influence or pressure in negotiating individual arrangements.

Industrial action will not be protected if it:

- is taken while a bargaining period has been suspended
- relates significantly to a demarcation dispute
- is in support of claims for a multi-enterprise or greenfields agreement
- covers matters not considered lawful in the dispute
- contravenes any Fair Work Australia orders.

on Resources

Weblink Fair Work Online

KEY IDEAS

- An industrial dispute is a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work.
- The level of disputes varies within and between industries and businesses. Some employers seek to minimise conflict, others stifle it through tough tactics, while others manage more collaboratively through negotiation with staff and unions.
- The major causes of disputes recognised by the ABS are disputes relating to negotiation of awards and enterprise agreements. These issues typically include disputes about remuneration, employment conditions and job security issues.
- The key stakeholders involved in resolving disputes include employees, employers, governments, trade unions, employer associations, courts and industrial tribunals.
- Negotiation is a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement.
- Mediation is the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party.
- Costs of industrial disputes include the cost of lost production and wages, loss of customer support, disruption to trade and social conflict.
- The Fair Work Commission has the power to resolve industrial disputes through conciliation or arbitration.
- Common law action is open to any party involved in or affected by industrial action.
- Benefits of industrial action include improvements in relationships and conditions.

20.9 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

20.9 Quick quiz on	20.9 Exercise	20.9 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 3, 5, 6, 8, 10, 11, 12, 15, 16, 17, 18, 19, 20	4, 7, 9, 14, 23	13, 21, 22

20.9 Exercise

Revision

1. **What** are the circumstances where a lockout or a picket would be used during an industrial dispute?
2. **Summarise** each of the methods available to resolve industrial disputes.
3. **Identify** the method used to describe the way the following disputes have been resolved.
   - **a.** Garth Enterprises makes an enterprise agreement with a majority of its employees, represented by the Australian Workers' Union.
   - **b.** Anna Baber and her employer PX Media ask the Australian Human Rights Commission to help them settle their dispute.
   - **c.** The Fair Work Commission orders Scali Ltd to reinstate 12 workers sacked last month.
   - **d.** Chow Machines finally reaches agreement with the CFMEU after regular meetings with the Fair Work Commission and the union.
   - **e.** Ramstine is fed up with his workmates playing practical jokes on him. He complains to Kevin Ly, his supervisor, who records the complaint and, as it is serious, takes it to the firm's group specifically established to help deal with such problems.
4. **Why** do many businesses not experience industrial disputes such as strikes?
5. **Identify** the criteria a party must prove to the Fair Work Commission before being permitted to take industrial action.
6. **Describe** how the focus on conflict resolution has changed over the last few years.
7. Recent legislation has forced employers and employees to increasingly resolve issues in the workplace. **Discuss** the advantages and disadvantages of this approach.
8. **Describe** common law action. Why it is generally considered a 'last resort'?
9. **Explain** how disputes can be costly to a business and the economy.

Read the 'Analysing the causes of two workplace disputes and the strategies used to resolve them' case studies and answer questions 10 to 13.

10. **List** the parties to the dispute.
11. **What** was the cause/s of the dispute?
12. **Identify** the types of industrial action taken both by employees and their employer.
13. **Analyse** the strategies used to resolve the dispute.

Read the 'Workplace disputes — how to extinguish the flame and avoid a fire' case study and answer questions 14 to 17.

14. **Why** is the manager's skill so important in avoiding an escalation of an industrial dispute?
15. **What** is a grievance procedure?
16. **List** the steps that a manager could take when dealing with a grievance in the first instance.
17. **Describe** the manager's role in making a decision after hearing an employee's grievance.

Read the 'Fair Work Commission — dispute resolution' case study and answer questions 18 to 20.

18. **Outline** the situations in which the Fair Work Commission assists in resolving issues.
19. **Clarify** the roles the Fair Work Commission can play in resolving disputes.
20. **Identify** the possible outcomes of disputes that are referred to the Fair Work Commission.

Extension

21. **Analyse** the issues in the following situation and propose a solution for Marie. Use information available from the **Fair Work Online** website to assist you in considering this situation.

    Marie's employer tells her she will not be paid for the next week because her employer intends to lock out Marie and three other workmates during a bargaining period leading up to the negotiation of a new enterprise agreement. He states that, if she does not agree to his new conditions after the lockout, she will be dismissed.
22. 'Sometimes an open dispute in the workplace can be beneficial.' **Evaluate** this statement.
23. In groups, use newspapers and the internet to **investigate** a range of industrial disputes. Create a PowerPoint presentation or video clip to report to the class on the costs of the disputes.

20.9 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q10

What is the common sequence for resolving workplace disputes?

A. Mediation, negotiation, involvement of courts and tribunals
B. Negotiation, mediation, involvement of courts and tribunals
C. Involvement of courts and tribunals, negotiation, mediation
D. Negotiation, involvement of courts and tribunals, mediation

Question 2 (1 mark)

Source: HSC 2018 Business Studies Exam, Section I, Q8

The Fair Work Commission has finalised a dispute between a large business and a union.

Which strategy has been used to resolve this workplace dispute?

A. Mediation
B. Arbitration
C. Negotiation
D. Common law action

Question 3 (20 marks)

Source: HSC 2016 Business Studies Exam, Section IV, Q28

Evaluate the response of human resource management to legal and ethical influences.

Question 4 (20 marks)

Source: HSC 2014 Business Studies Exam, Section IV, Q26

Analyse both the causes of workplace disputes and the strategies used to resolve them.

Question 5 (1 mark)

Source: HSC 2014 Business Studies Exam, Section I, Q4

Grievance procedures are used when

A. employees are ill.
B. employees have complaints.
C. employees are being appraised.
D. employers want to increase prices.

Question 6 (4 marks)

Source: HSC 2013 Business Studies Exam, Section II, Q21b

Discuss ONE dispute resolution method a business could use to resolve workplace conflict.

More exam questions are available in your learnON title.

20.10 Review

20.10.1 Summary

Leadership styles

- A range of strategies are used to align the management of staff with the goals of the firm, including leadership styles.
- Leadership styles can be considered across a spectrum from an autocratic approach to a participative or democratic approach.
- Leadership styles which are most effective in Australia are more egalitarian and empowering and less directive than in other countries.
- Australian employees tend to be critical of the quality of Australian leadership and are seeking constructive workplace cultures where employers are supportive and focused on developing the skills and talents of employees in challenging and meaningful tasks and projects.

Job design

- Job design is the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job.
- Job design (specific tasks) is best represented through the Scientific management approach developed by Frederick Taylor that identified one best way of doing a job and that worker skills should be matched to job requirements.
- Job design (general tasks) refers to a greater variety of tasks to be performed by workers. The main objective of the provision of a wider variety of tasks is to improve worker satisfaction and productivity.

Recruitment and selection process

- Recruitment is the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost.
- Most businesses use a mix of internal and external recruitment to maximise opportunities for new ideas and use of existing expertise in the business.
- Australia has long experienced a skills shortage, leading employers to increasingly recruit staff with general skills and upskilling internally.
- Many businesses recruit overseas and poach staff from other businesses to overcome shortages of skilled staff.

Training and development

- Training aims to develop skills, knowledge and attitudes that lead to superior work performance.
- Development is focused on enhancing the skills of the employee to upgrade their skills in line with the changing and future needs of the business.

Performance management

- Performance management is a systematic process of evaluating and managing employee performance in order to achieve the best outcomes for a business.
- Feedback from performance appraisal and management provides many benefits to the business and the individual.

Rewards

- Rewards management is a system of monetary and non-monetary, and intrinsic and extrinsic rewards to attract, motivate and retain employees for their effort and performance.
- An effective reward system is equitable, clearly communicated, relevant, cost effective, simple to administer and aligned with the business's goals.

Global strategies

- Globalisation brings issues related to managing human resources. Access to sufficient numbers of skilled workers affects business decision making.

- The rapid growth of global outsourcing illustrates the potential for firms to develop creative strategies that access lower labour cost, while complying with regulations and pay scales in overseas countries.

Workplace disputes

- An industrial dispute is a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work.
- The level of disputes varies within and between industries and businesses. Some employers seek to minimise conflict, others stifle it through tough tactics, while others manage more collaboratively through negotiation with staff and unions.
- The major causes of disputes recognised by the ABS are disputes relating to negotiation of awards and enterprise agreements. These issues typically include disputes about remuneration, employment conditions and job security issues.
- The key stakeholders involved in resolving disputes include employees, employers, governments, trade unions, employer associations, courts and industrial tribunals.
- Negotiation is a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement.
- Mediation is the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party.
- Costs of industrial disputes include the cost of lost production and wages, loss of customer support, disruption to trade and social conflict.
- The Fair Work Commission has the power to resolve industrial disputes through conciliation or arbitration.
- Common law action is open to any party involved in or affected by industrial action.
- Benefits of industrial action include improvements in relationships and conditions.

20.10.2 Key terms

development refers to enhancing the skills of the employee in line with the changing and future needs of the organisation
employee poaching the practice of enticing employees to work for another business
external recruitment involves filling job vacancies with people from outside the business
general skills include flexibility and versatility, social confidence, positive attitude, motivation, and the ability to work as a team and/or independently
grievance procedures formal procedures, generally written into an award or agreement, that state agreed processes to resolve disputes in the workplace
in good faith means the parties meet with a willingness to reach an agreement
industrial dispute a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work
insourcing delegating a job to someone within the business, as opposed to someone outside the business
internal recruitment involves filling job vacancies with people from within the business
job design the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job
leadership style refers to ways that managers communicate with their employees to inspire and motivate them to work together to achieve an organisation's goals
lockouts when employers close the entrance to a workplace and refuse admission to the workers
mediation the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party
monetary rewards those rewards reflected in pay or having financial value
negotiation a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement
non-monetary rewards those rewards that do not have a financial value, such as social activities or retirement planning
orders decisions that require employees or employers to carry out a direction from the tribunal. They may be inserted in awards or agreements.

performance management addresses both individual and business performance. Successful individual performance will often translate into the business's strategic objectives being met.
performance management (administrative) this model assesses the progress of the business in meeting its strategic goals and where necessary identifying the areas for improvement, such as establishing new goals or employee performance
performance management (developmental) this model improves individual performance through establishing objectives such as reaching sales targets that are consistent with achieving the organisation's goals
pickets protests that take place outside the workplace, generally associated with a strike. Unionists stop the delivery of goods and try to stop the entry of non-union labour into the workplace.
recruitment the process of locating and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost
remuneration the financial (e.g. pay) and non-financial (e.g. career security) benefits that employees receive in return for their work effort
specific skills highly specialised skills that are required for some jobs within science, technology and engineering sectors
strikes situations in which workers withdraw their labour
subsidiary a company that is owned by another company (referred to as the parent) and it is often located in another country
training to develop skills, knowledge and attitudes that lead to superior work performance

Resources

Digital documents	Key terms glossary (doc-35676) Chapter crossword (doc-36225)
Interactivity	Chapter crossword (int-7179)
Exam question booklet	Chapter 20 Exam question booklet (eqb-0042)

20.10 Activities

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Exercise 1: Multiple choice questions

1. Australian business leaders are generally seen as which of the following?
   - **A.** Autocratic and valuing mateship
   - **B.** Performance orientated and valuing egalitarianism
   - **C.** Efficiency focused and discriminatory
   - **D.** Participative and valuing group rewards

2. A café manager uses a democratic leadership approach. What does this mean?
   - **A.** She expects self direction and excellence.
   - **B.** She hugs all the customers and is kind to all staff.
   - **C.** She builds consensus for decision making.
   - **D.** She develops staff only for the business's current needs.

3. Well-designed jobs are most likely to do which of the following?
   - **A.** Have some clear task identity and provide feedback to employers
   - **B.** Provide employee recognition and constructive autonomy
   - **C.** Have resources and job specifications
   - **D.** Have some job autonomy and clear task identity

4. Which of the following are the major advantages of external recruitment for a large animation firm?
   - **A.** New ideas, skills and competition for internal staff
   - **B.** Reduced costs of outsourcing
   - **C.** Cheaper than internal recruitment
   - **D.** New ideas and less chance for ongoing internal politics

5. While employers are keen to hire more staff with general skills, specific skills are also in high demand, particularly from which of the following?
   - **A.** Skilled tradespersons
   - **B.** Employee poachers
   - **C.** Builders, engineers and administrators
   - **D.** Specialist educators

6. In choosing the appropriate training and development approach for their business, businesses must do which of the following?
   - **A.** Ignore the needs of the business.
   - **B.** Evaluate the supply of, and demand for, the skills needed by workers.
   - **C.** Shape the changing nature of work to suit only its business.
   - **D.** Reduce expenditure to ensure that the business loses fewer workers.

7. Performance management adds value to a business, including through which of the following?
   - **A.** Assessment of legal compliance and feedback
   - **B.** Identifying opportunities for productivity improvement
   - **C.** Identifying opportunities for new technology
   - **D.** A and B

8. Why do many firms use a rewards matrix?
   - **A.** To assess the objectives of each reward
   - **B.** To assess the overall effectiveness of the rewards system
   - **C.** To identify costs of monetary rewards and benefits
   - **D.** A and B

9. Which of the following are key factors underpinning strategic human resource management decisions of a global nature?
   - **A.** Restructuring of Australian businesses
   - **B.** Temporary work visas and outsourcing
   - **C.** Costs, skills and supply of labour
   - **D.** Costs, skills and demand for labour overseas

10. When does a lockout occur?
    - **A.** Employees refuse admission to employers in a workplace.
    - **B.** Employers refuse to let employees leave the workplace.
    - **C.** Employers refuse admission to workers at the workplace.
    - **D.** Employers fly in picket workers.

Exercise 2: Exam practice questions

Question 1 (7 marks)

a. **Assess** the range of leadership styles identified in business managers. **(3 marks)**

b. **Recommend** the most suitable leadership style for a business with inexperienced workers using heavy machinery in a factory. **(4 marks)**

Question 2 (7 marks)

a. **Describe** the role of internal and external recruitment as a strategy in human resource management. **(3 marks)**

b. **Justify** the decision to recruit employees for specific skills. **(4 marks)**

Question 3 (2 marks)

Identify TWO future skills needed for a student about to enter the workforce.

Question 4 (4 marks)

List TWO advantages and TWO disadvantages of performance pay in human resource management.

Question 5 (5 marks)

Discuss the costs, skills and supply of labour associated with global outsourcing.

Question 6 (6 marks)

Analyse TWO workplace disputes and the strategies used to resolve them.

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21 Effectiveness of human resource management

21.1 Overview

LEARNING SEQUENCE

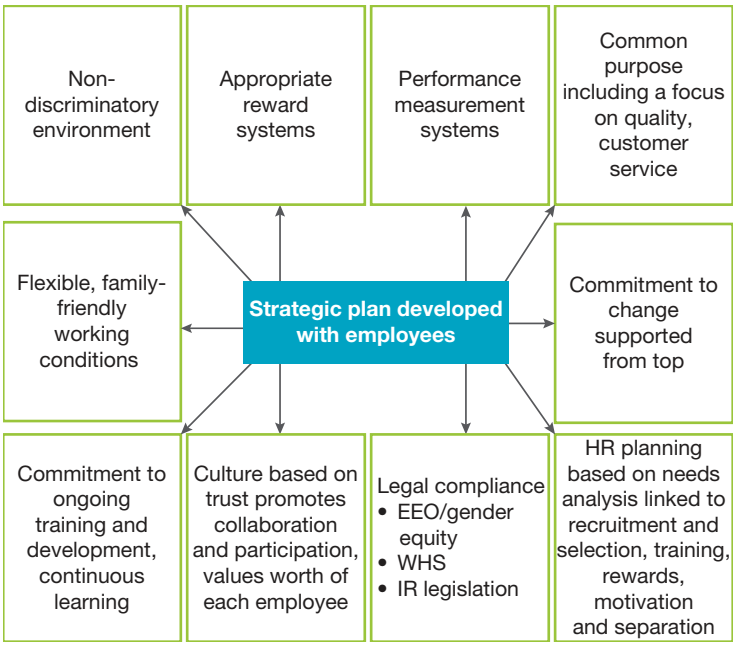
21.1 Overview
21.2 Corporate culture, benchmarking key variables and changes in staff turnover
21.3 Absenteeism, accidents, levels of disputation and worker satisfaction
21.4 Review

21.1.1 Introduction

The role of the human resource manager, working with the management team, is to decide how the employment relationship will be best managed so that it is cost-effective, achieves the business's goals and contributes to the 'bottom line'. These are important considerations, with managers reporting that labour costs are around 60 per cent of operating costs, and that 'people management issues' take up most of their managerial time.

In best practice businesses, a strategic, holistic view is taken of the importance of building a workplace culture that attracts and retains the 'best' employees and fosters the success of the enterprise. The role of the human resource function is to effectively link individual performance with corporate strategy. The business can then modify processes and strategies, if they are not successful, through performance management. As previously explained, performance management is a strategic approach to improving organisational effectiveness and success, through improving the performance of the business, teams and individual employees. Once all these elements have been implemented, the final aspect of human resource management is to evaluate their effectiveness.

FIGURE 21.1 Key elements of effective human resource management. These elements have been discussed in the preceding four chapters.



on Resources

Digital document Key terms glossary (doc-35678)
Exam question booklet Chapter 21 Exam question booklet (eqb-0043)

21.2 Corporate culture, benchmarking key variables and changes in staff turnover

SYLLABUS LINK In this subtopic you will learn about corporate culture, benchmarking key variables and changes in staff turnover as indicators in assessing the effectiveness of human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

Many businesses use a range of **indicators** to reflect on the effectiveness of the human resource functions. Indicators are performance measures used to evaluate the effectiveness of the business, team or individual, such as dollar sales achieved per employee per year.

Indicators can be compared to those of best practice businesses or internal divisions to determine strengths and weaknesses. This process is called **benchmarking**. Benchmarking is a process in which indicators (key variables) are used to compare business performance between internal sections of a business or between businesses. This is then used as a basis for improvement.

Indicators are gathered and collated in **human resource audits**. The major control tool is the annual strategic planning process, where performance is evaluated and strategies modified for further organisational development.

indicators performance measures that are used to evaluate organisational or individual effectiveness

benchmarking a process in which indicators are used to compare business performance between internal sections of a business or between businesses

human resource audit a diagnostic tool used to evaluate HR policies and practices in order to identify problems and develop solutions in an attempt to rectify problems

Typical indicators used to evaluate the effectiveness of the human resource function are shown in table 21.1.

TABLE 21.1 Human resources effectiveness indicators

Functional area	Indicators (/ means 'as a proportion of')
Human resources planning	Number of staff/budgeted staff
Recruitment and selection	Applicant rejections Acceptance rates for job offers Recruitment costs Vacancies filled within target time
Training and development	Training days/hours per employee Training time/budgeted time Cost of training Test outcomes — changes in skills, quality accidents, output, productivity Succession planning rate Promotion rate
Employee rewards and benefits	Costs of rewards and benefits Labour turnover rates Absence rates/total hours worked Rewards and benefits compared with other businesses
Industrial relations	Grievance records Industrial disputes, work stoppages Time lost through disputes
Work health and safety	Accident rates Lost time injury incidence rates Workers' compensation costs/payroll

(continued)

TABLE 21.1 Human resources effectiveness indicators *(continued)*

Functional area	Indicators (/ means 'as a proportion of')
Performance appraisal	Appraisals undertaken Goals achieved/not achieved Disciplinary interviews/people employed Improvements in quality and productivity (turnover rate)
Separation/termination	Separation rate Dismissal rate Resignation rate Average retirement rate Unfair dismissal claims
General HRM effectiveness	Labour costs/sales and gross profit per employee Growth in market share

The most commonly used key performance indicators benchmarked for the effectiveness of human resource management are:

- financial indicators for each member of staff, including sales per employee
- contribution to production, for example, output per employee
- changes in staff turnover
- absenteeism
- accidents
- levels of disputation — workplace conflict and industrial disputes
- worker satisfaction, as seen in surveys, feedback and exit interviews.

FIGURE 21.2 A cooperative workplace culture is common in the most popular workplaces. It is usually based around positive working relationships between employees.



Clearly, for indicators to be of value, results must be communicated and acted upon by management in improvement plans. The role of the human resource manager in using these indicators is focused on fostering continuous improvement by:

- communicating and educating employees about company vision, strategy and expectations at an operational level
- planning and setting goals for employees that are translated into meaningful tasks, and ensuring staff know how to achieve them
- developing employees effectively to improve performance
- evaluating performance, providing coaching and feedback in formal reviews
- linking rewards to performance measures
- providing organisational feedback for ongoing planning purposes.

21.2.1 Corporate culture

Reflect on either a part-time job you enjoyed doing, or a class you liked attending. What made these experiences so worthwhile? Your enjoyment was probably due to a combination of factors:

- You believed you were treated fairly and honestly, and were trusted.
- Your work was appreciated.
- Positive reinforcement, in the form of praise, was given for a job well done.
- Your involvement gave you a feeling of self-worth as you felt respected.
- Criticism, when given, was constructive.
- Conflicts, when they arose, were dealt with sensitively and appropriately.
- There was a harmonious atmosphere in the workplace/classroom, with positive work relationships between the staff.
- You felt part of a team working together to achieve a specific goal.

When you think about it, a sporting or debating team, emergency workers at the scene of an accident, the crew of an aircraft or sales assistants serving at the checkout all have one thing in common: they are part of a team that requires the interaction of a large number of individuals to achieve a common objective.

Most businesses that are successful in the long term maintain a balance between concern for success (expansion or profit) and regard for their employees. Better work and employment relationships begin with an understanding of how to develop a positive **corporate culture**.

People are a business's most valuable resource or asset. It makes sense, therefore, to develop a cooperative and effective corporate culture and positive working relationships. Without dedicated, trained and motivated employees, the best organised plans will never be achieved. In its broadest sense, human resources covers all types of interaction among people: conflicts, cooperative efforts, and interpersonal and group relationships.

The indicators that reveal a workplace has a poor corporate culture include:

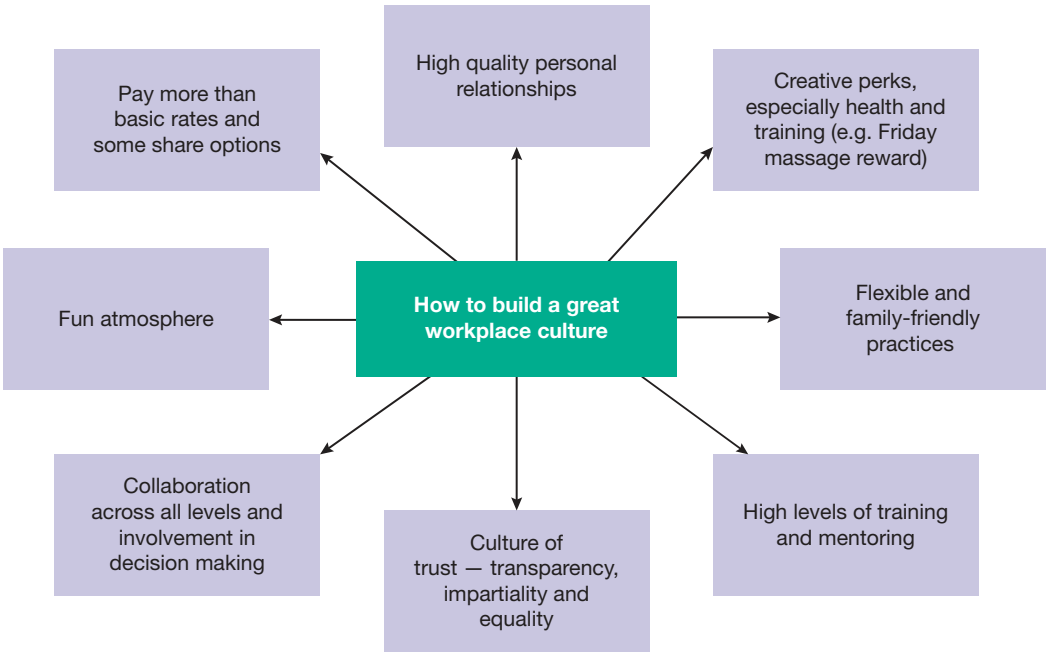
- high staff turnover
- poor customer service
- high levels of absenteeism
- accidents
- disputes and internal conflict.

These problems are reflected in poor business performance, lower sales, lower profits than competitors and ultimately the 'bottom line'.

corporate culture the values, ideas, expectations and beliefs shared by members of a business

Effective workplace relationships depend heavily on the quality of a business's communications systems and participation of employees in decision making, as discussed in chapter 20. Strategies that focus on building trust and direct communication between people, and value their ideas, are critical in building a positive workplace culture. Common features of the workplaces rated the best in Australia are shown in figure 21.3.

FIGURE 21.3 How to build a great workplace culture — features of workplaces rated the best in Australia



SNAPSHOT

Case study: Healthy management



City Health is a private healthcare provider serving a population of 500 000 people and operating with a budget of $500 million. It employs 3000 staff and has grown steadily over the last five years due to the merging of several major city hospitals. The chief executive of City Health, Dr Jan Dvorak, recently called a meeting of the executive team to discuss a strategic plan. These discussions explored the objectives of:

- developing a culture of quality and innovation
- working in partnership with all stakeholders to enhance the health of the community
- providing an environment that values and supports staff
- achieving a financially sustainable health service.

Up until now, Dr Dvorak has managed and guided City Health through its period of high growth. She has led the business to where it is today by listening to her employees, the hospital's patients and the community. She includes staff unconditionally in the decision-making process of the business. She is considered to be a great leader by her staff.

Dr Dvorak considers that the change to a new corporate culture will be her greatest challenge so far, but believes that the hospital is well on its way to achieving this goal.

21.2.2 Benchmarking key variables

Effectively performing benchmarking may involve coordination with line management, the human resource manager and even external specialist consultants. Each may share in evaluating the practices shown in figure 21.1. Benchmarking may follow a more comprehensive human resources audit or may be undertaken using basic indicators. The purpose is to compare a business's performance in specific areas against other similar businesses or divisions, or against 'best practice' businesses. The aim is then to initiate changes to foster improvement. Many businesses report they improve their process performance after undertaking benchmarking.

Benchmarking is commonly undertaken in a number of ways.

- **Informal benchmarking** includes any strategies such as networking through informal discussions with colleagues in other businesses, undertaking visits to other businesses, researching best practice online and attending conferences.
- **Performance benchmarking** involves comparing the performance levels of a process/activity with other businesses.
- **Best practice benchmarking** involves comparing performance levels with those of another best practice business in specific areas using a structured process to gain skills and knowledge, and to modify organisational processes.
- **Balanced scorecard benchmarking** is used for measuring whether the activities of a business are meeting its objectives established in the strategic plan. It benchmarks key performance variables with targets aligned with the strategic plan.

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The approach used for benchmarking needs to be chosen for its suitability to the business's needs and resources as it can be a very costly and time-consuming process. Most businesses do not rely solely on quantitative variables or sales per employee, but also consider qualitative information such as feedback from staff and customers. The impact on the 'bottom line' (i.e. valued in terms of profits/costs) does nevertheless remain a major consideration, with the cost of human resources being the largest single contributor to most organisational costs.

BizFACT

In 2021, the Workplace Gender Equality Agency (WGEA) introduced benchmark data that allows a business to compare its performance both within the industry and with other organisations of the same size in other industries with respect to specific human resources issues such as gender composition of its workforce, remuneration, flexible work arrangements and sex-based harassment and discrimination.

Care needs to be taken in benchmarking. It may provide useful information about the business's human resources, but may focus excessively on costs rather than what is actually being achieved or may be achieved. The most important information is the long-term performance of those recruited and the development needs of talented staff with future potential in the business.

SNAPSHOT

Case study: Evaluating human resource management effectiveness at the Woolworths Group

Increasingly businesses in Australia are making reference to a number of key human resource variables to assess performance in the 'people' aspects of the business.

Programs and performance in such areas as gender equity, diversity, support of Aboriginal and Torres Strait Islander employment and creating a safe environment are being assessed across years.

This assessment is often reported in the *Sustainability* component of the company's annual report.

The Woolworths Group has recently renewed the focus of its engagement and the effectiveness of its human resource strategies with stakeholders including its team members, as identified in the three pillars of People, Planet and Prosperity.

While successful, the company seeks to increase the number of executive and senior manager positions held by women (currently 41 per cent, up from 29 per cent in 2017), minimise the wage gap between male and female employees holding similar positions (currently less than 1 per cent), develop increasingly inclusive environments for all team members, encourage cultural diversity that better reflects the local community, provide ongoing career development opportunities for Aboriginal and Torres Strait Islander team members, focus on maintaining a workplace that safeguards health and wellbeing of team members including COVIDsafe and COVIDcare measures (19 per cent reduction in the total recordable injury frequency rate — TRIFR) and inclusion of LGBTQ+ communities.



Many of these indicators are addressed by other public companies, including those competing in the same retail sector. Woolworths' re-focus on these key indicators is proving relatively successful but with more than 215 000 team members, the 2025 Sustainability Strategy will continue to build upon these strengths.

Woolworths seeks to improve their performance in the following areas:

- engaging with female staff through strategies such as ensuring further opportunities to become managers
- resourcing cultural diversity initiatives, such as the *Proud* network that supports members of the team who identify as LGBTQ+
- continuing to increase employment opportunities for Aboriginal and Torres Strait Islander workers through the Woolworths–Federal Government partnership, *Diversity Demons*
- ensuring safer working environments for staff by working co-operatively with the community to reduce opportunities for the transmission of COVID-19.

Human resource audits

A human resource audit can be used to systematically analyse and evaluate human resource activities and their effectiveness. This audit can be performed in a number of ways:

- Performance of one division or the business itself against another is benchmarked and compared to industry 'best practice' to determine areas of weakness and for improvement.
- An outside consultant conducts research to analyse problems and suggest solutions.
- Key performance variables are evaluated by management.

FIGURE 21.4 Businesses should regularly evaluate human resource management strategies, the quality of workplace relationships and the corporate culture.



- A legal compliance analysis may be undertaken to determine areas of variance from laws and company policies. High levels of fines, workers' compensation claims and unfair dismissal claims would indicate this type of audit was required.
- A management by objectives (MBO) approach can be used to determine areas of poor performance against targets established.

Quantitative measures

Quantitative measures to be analysed are shown in table 21.1 and in the following case study. These should be able to demonstrate the actual effect of indicators in economic terms — that is, in terms of costs and profits. Key variables often include:

- variances in labour budgets. Significant increases in the size of labour budgets represent a major increase in the costs of business, and are most likely due to poor planning of staffing needs, higher unscheduled absenteeism, overtime or staff turnover rates, or increases in wage rates.
- time lost/costs of injuries and sickness. Rising costs are a clear indicator that health and safety requirements are being breached, perhaps due to poor training or a lack of training. Such costs also lead, in the longer run, to higher insurance premiums, and risks of fines and claims.
- performance appraisals completed compared with targets. This indicates the extent to which the appraisal of staff has been undertaken by managers, but does not provide detailed feedback on the effectiveness of these processes.
- percentage of goals achieved. Goals should be collaboratively determined by employees and managers. The return on human investment is a goal, which may be determined in many ways including dollar sales per employee. Rising sales per employee are often seen as an indicator of improved customer service and employee productivity.
- levels of labour turnover, particularly those initiated with employees. Higher levels can indicate workplace problems, ranging from a poor workplace culture and poor working relationships, to lack of clear job descriptions and opportunity for promotion or personal growth.

Benchmarking of such variables is undertaken frequently by businesses seeking to operate at world's best practice, or in accordance with standards in quality assurance programs.

SNAPSHOT

Case study: Key human resource benchmarks (median) — a summary

	2016	2017	2018	2019	2020
Return on human investment ratio	$0.30	$0.38	$0.32	$0.19	$0.47
Managerial/ professional male to female staffing rate	1.96	1.79	1.82	1.43	1.60
Unscheduled absence per employee (absenteeism)	7.03 days	7.25 days	7.74 days	7.87 days	8.22 days
Employee-initiated separation rate	8.39 per cent	8.29 per cent	7.36 per cent	7.61 per cent	7.26 per cent
Total separation rate	15.16 per cent	16.01 per cent	13.59 per cent	15.06 per cent	13.24 per cent
Training investment per employee*	$635	$821	$898	$1021	$1111

*excluding trainees' remuneration

Qualitative evaluation

Qualitative evaluation involves detailed feedback and research on key issues, which allows judgements to be made about changes in behaviour or quality of service provided. Major sources of such information may include feedback from middle management, surveys and focus groups about workplace culture, relationships at work, and the quality of customer service and leadership.

Benchmarking major variables is essential in planning for continuous improvement.

- High or increasing absenteeism and labour turnover rates are indicators of problems including boredom, poor relationships, and lack of training or opportunities to develop.
- Analysis of industrial disputes and the issues raised may provide useful feedback about issues such as health and safety, rewards and benefits, and relationships in the workplace.
- Feedback from performance appraisals provides information useful in evaluating and planning training, recruitment and selection, development, rewards, and separation processes.
- Feedback from supervisors, consultative committees, customers and employees in organisational surveys provides useful insight into worker satisfaction, empowerment and customer service.

Research by external businesses and institutions also provides valuable information for analysis and comparison. Businesses, therefore, need to consider domestic and international trends and management practices when planning strategies for improving the effectiveness of human resource management and business performance.

21.2.3 Changes in staff turnover

Staff turnover refers to the separation of employees from an employer, both voluntary and involuntary, through dismissal or retrenchment. It is often shown as a percentage of total staff numbers. Staff turnover in Australia averages around 12–15 per cent per year, and fluctuates with the economic cycle, with around half being voluntary turnover due to resignation and retirement.

Turnover varies greatly between industries, with the hospitality and hotel industry commonly experiencing rates of 90 per cent per annum. In assessing the significance of turnover, it is therefore important for businesses to benchmark their turnover against that of other businesses in the industry; and to determine the type of staff leaving and their reasons. There are likely to be 'pull' factors outside the business or 'push' factors inside the business.

staff turnover the loss of employees who leave the business for a variety of reasons

BizFACT

Exit interviews are used to find out why an employee is leaving the organisation. Surveys indicate that less than 5 per cent of employers actually make use of information gathered from exit interviews.

Staff may leave to seek new opportunities or promotion as a result of skills developed in a particular industry; this may not be a negative reflection on the workplace they are leaving. Others may leave due to a 'toxic' workplace riddled with internal politics.

The costs of high labour turnover are great, and involve high costs through payouts for entitlements, hiring, inducting and training new staff (see figure 21.6). Productivity and service quality (a major issue in the hospitality and hotel industry), corporate skills and knowledge are lost, particularly if there has been poor succession planning. This is often described as the biggest cost of high turnover rates. Lack of a focused workplace culture in such an environment reduces employee commitment and loyalty.

FIGURE 21.5 The hospitality and hotel industry experiences high rates of staff turnover, as much as 90 per cent per annum.



Some level of turnover is considered healthy in businesses, as new ideas are brought in and often stimulate innovation in work practices. However, a major change or a significant increase in turnover is a major warning sign.

BizFACT

Much employee turnover in Australia occurs in newly recruited staff with less than one year in the job. Unskilled employees with mundane or repetitive jobs, low pay and little participation in decision making are also more likely to resign.

High resignation rates are often linked with absenteeism rates as indicators of dissatisfaction in the workplace.

FIGURE 21.6 Hypothetical total turnover costs for a middle manager in a large Australian business

Exit interviews	$1000
Administration	$100
Lost productivity	$15 000
(a) Costs of separation of employee from company	= $16 100
Prepare job descriptions, review résumés and interviewing	$3000
Recruitment agency and advertising	$20 000
Pre-employment tasks and orientation	$1000
Lost productivity	$30 000
Training of new employees	$40 000
(b) Costs of replacement and training new employee	= $94 000
Total turnover cost (a + b)	= **$110 100**

SNAPSHOT

Case study: Managing employees at Nationwide Health



Nationwide Health is a national care organisation that employs 8000 people across Australia. While the business has performed well and management is pleased with this performance, there is concern about aspects of employment relations, in particular the high rate of staff turnover. Rates for this important human resource indicator appear to spike before and during school holidays and has become unsustainable. It appears that it is more of issue at Nationwide Health as it has a predominantly female workforce and anecdotally many of its staff were critical of the lack of interest being displayed in achieving work–family balance.

Management did eventually become aware of the issue and despite initial staff misgivings, it was keen to resolve the issue and stem the tide of staff separation. After a brief consultation period to hear concerns directly it introduced a more flexible work environment for staff that allows for job sharing, shorter night shifts, school holiday programs for children, negotiating with local childcare centres for cheaper rates, banked (accrued) leave and flexible rostering.

Since its introduction of its more flexible approach to workplace management, turnover has fallen to less than 2 per cent (much lower than the industry average) and the return to work rate for women following maternity leave increasing to 97 per cent.

KEY IDEAS

- Human resource indicators are used by many businesses to evaluate the effectiveness of the business, team or individual.
- The best way to maximise employee productivity and motivation is through a constructive corporate culture, where employees are trusted, collaborate, have strong personal relationships and are highly trained and mentored.
- Benchmarking is a process in which indicators are used to compare business performance between internal sections of a business or between businesses.
- Benchmarking may be undertaken using informal benchmarking, performance benchmarking, best practice benchmarking and balanced scorecard benchmarking.
- A human resource audit can be used to systematically analyse and evaluate human resource activities and their effectiveness.
- Quantitative measures should be able to demonstrate the actual effect of indicators in economic terms.
- Qualitative evaluation involves detailed feedback and research on key issues, which allows judgements to be made about change in behaviour or quality of service provided.
- Staff turnover refers to the separation of employees from an employer, both voluntary and involuntary, through dismissal or retrenchment.
- In assessing the significance of turnover, it is important for businesses to benchmark their turnover against that of other businesses in the industry; and to determine the type of staff leaving and their reasons.

21.2 Activities

learnON

To answer questions online and to receive **immediate feedback** and **sample responses** for every question, go to your learnON title at www.jacplus.com.au. A **downloadable solutions** file is also available in the Resources tab.

21.2 Quick quiz on	21.2 Exercise	21.2 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 2, 6, 10, 11, 15, 16, 20	3, 4, 5, 7, 8, 9, 14, 17, 18, 19, 21, 22, 23	12, 13, 24, 25, 26, 27

21.2 Exercise

Revision

1. **Clarify** the relationship between indicators, benchmarking and human resource audits.
2. Look at table 21.1 and draw a table listing one indicator from each functional area. Next to the indicator, **outline** how it can be used to evaluate the effectiveness of human resource management.
3. **Explain** how corporate culture can influence the success of a business.
4. Sonic Ltd has low staff turnover, low levels of absenteeism and very few accidents. **Deduce** what this reveals about Sonic's corporate culture. **Justify** your answer.
5. **Why** is benchmarking a useful tool for managers?
6. **What** are some of the most common methods of benchmarking used today?
7. **Discuss** some of the difficulties associated with benchmarking.
8. **Explain** why the effectiveness of human resource management in a business cannot be evaluated using a quantitative approach alone.
9. **Why** are staff turnover rates significant indicators of the effectiveness of human resource management in a workplace?

Read the 'Healthy management' case study and answer questions 10 to 13.

10. **Outline** the recent changes at City Health.
11. **Summarise** the proposed City Health strategic plan.
12. Who is Dr Jan Dvorak? **Evaluate** her management style.
13. **Analyse** the changes at City Health and Dr Dvorak's approach to management in relation to their impact on the company's new corporate culture.

Read the case study 'Evaluating human resource management effectiveness at the Woolworths Group' and answer questions 14 to 17.

14. **Justify** the variables used to evaluate the effectiveness of human resource strategies within the annual reports of businesses in Australia.
15. **List** the focus of the Woolworths Group's human resource management strategies.
16. **Outline** the human resource strategies that will need to be a focus of the business in the years ahead.
17. **Recommend** alternative human resource strategies that you believe will enable the business to better manage its staff.

Read the 'Key human resource benchmarks (median) — a summary' case study and answer questions 18 and 19.

You are the human resource manager of a major chain store. When you examine your key indicators for the last year, you find your return on human investment is $0.16, absenteeism is 12 days per employee, your total separation rate is 40 per cent and your training investment per employee is $483.

18. **Explain** how your business compares to the 2020 human resource benchmarks.
19. Create a report that **proposes** possible causes of, and solutions for, these differences.

Read the 'Managing employees at Nationwide Health' case study and answer questions 20 to 24.

20. **What** industry sector does Nationwide Health belong to?
21. **Describe** the human resource management issue faced by management at Nationwide Health.
22. **Why** was the issue most obvious during school holidays?
23. **How** did management address the issue it faced?
24. **Evaluate** the effectiveness of the strategies used by Nationwide Health's management to address the issue. Are there others you could suggest?

Extension

25. **Create** a logical, structured report on the following topic:
    'A key aspect of effective human resource function is the monitoring, evaluation and modification of plans and performance.' Refer to business examples or case studies in your response.
26. **Assess** how benchmarking can assist in a strategic approach to human resource management in achieving the goals of the business.
27. The Australian Workplace and Industrial Relations Survey has revealed that most workplaces with more than 20 employees use these practices:
    - training for supervisors
    - equal employment opportunity and affirmative action policies
    - performance appraisal of non-managerial employees
    - productivity improvement systems, such as key indicators and benchmarking.

    Predict the possible benefits to be gained from the use of each of these practices.

21.2 Exam questions

Question 1 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q18

The table compares four businesses on an annual basis.

	A	*B*	*C*	*D*
Absenteeism (average per employee)	8	5	8	5
Accidents per 500 employees	4	2	2	4
% of staff turnover	11	9	9	11
Average output per employee	10	14	10	14

Which business is likely to be managing its human resources most effectively?

A. *A*
B. *B*
C. *C*
D. *D*

Question 2 (4 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q23c

A business has been rapidly expanding and requires additional staff.

The expansion of the business has led to conflict and uncertainty in the workplace.

Recommend TWO indicators that could be used by the business to measure the effectiveness of human resource management

Question 3 (4 marks)

Source: HSC 2016 Business Studies Exam, Section II, Q23c

Heather owns a financial planning business with offices in four countries, including Australia.

Heather's workforce is diverse and culturally competent.

What are the advantages of this for Heather's business?

Question 4 (1 mark)

Source: HSC 2012 Business Studies Exam, Section I, Q9

Information about four companies is shown in the table.

	Company A	Company B	Company C	Company D
Staff turnover (% of workforce)	15	11	11	15
Output per worker (products per hour)	8	12	8	12
Absenteeism (average days per employee)	9	8	9	8

Which company is likely to have the best employee relations?

A. Company A
B. Company B
C. Company C
D. Company D

Question 5 (1 mark)

Source: Adapted from HSC 2006 Business Studies Exam, Section I, Q20

Which of the following is a measure of effective human resource management?

A. The high cost of retrenchment packages
B. Increased use of temporary workers and overtime
C. Industry average levels of voluntary staff turnover
D. Increased training associated with replacing special skills

More exam questions are available in your learn ON title.

21.3 Absenteeism, accidents, levels of disputation and worker satisfaction

SYLLABUS LINK In this subtopic you will learn about absenteeism, accidents, levels of disputation worker satisfaction as indicators in assessing the effectiveness of human resource management.

Source: *Business Studies Stage 6 Syllabus* © Copyright 2010 NSW Education Standards Authority (NESA).

21.3.1 Absenteeism

Absenteeism refers to a worker who neglects to turn up for work when they were scheduled to do so. High levels of absenteeism and/or lateness may indicate that workers are dissatisfied or that there is conflict within the workplace (see the following case study).

absenteeism refers to a worker who neglects to turn up for work when they were scheduled to do so

FIGURE 21.7 Absenteeism may indicate dissatisfaction or conflict within a workplace.



SNAPSHOT

Case study: Absenteeism — sickies cost!



Jordan, a kitchen manufacturer, is overheard complaining to Lloyd, a recording studio owner

Lloyd: When am I getting that kitchen delivered? The bands keep making a mess of my studio! I keep finding nuggets and chips on my equipment!

Jordan: Mate, I'm doing my best. I've got up to seven of my 95 staff absent at the moment. They're such bludgers! I'm going to sack them.

Lloyd: Have you thought about your workplace practices?

Jordan: I haven't got the time for that fuzzy stuff.

Lloyd: Does this happen a lot?

Jordan: Yeah, I lose 50 per cent of my staff every year.

Lloyd: You know, you should get some advice. I don't have a problem at all, but, as you know, I'm a good guy! My staff don't want to take time off because the work is great. I give them time off to look after their kids if they need it and get everyone to learn someone else's job, so they can take over when the others are off. I give them free CDs and concert tickets when they work hard. Even The Weeknd said he wouldn't mind working here when he came on a tour! What do you do for your staff?

Jordan: None of that. Work is work — not a play centre!

Lloyd: Mate, don't you do your key performance indicators? It's costing you probably $1500 every time your staff has more than a week's sick leave a year. Most people take off around 9 days a year, and I bet there are a few race days in that lot. Multiply that by seven staff, add 30 per cent for lost productivity, and you get the idea! And that's not counting all the make-up work. They reckon it costs you around $360 a day every time someone is off sick.

Jordan: Geez! My hip pocket is hurting. What should I do?

Lloyd: Talk to my wife. She's a human resource manager for a big record company. She'll tell you to find out why they take time off, through meetings or a suggestion box.

Jordan: I can imagine the rude stuff I'd get in the box.

Lloyd: Try being a decent employer. Sit down and work out with them a clear policy for absences. You can reduce your absenteeism by 20 per cent by putting in a plan. If you give 'em rewards and fun staff activities, you'll get the benefit of having them there. You won't have all these upset customers because no one follows up on their calls properly, and you won't have to constantly reschedule things. Tell them how much it matters. Listen to your staff and then save money, mate.

In terms of lost revenue, such unofficial expressions of conflict may be even more costly to firms than official forms of conflict. Firms need to have much higher staffing levels to cope with high absentee levels. Therefore, revenue is lost as work is disrupted and can lead to lower productivity and higher labour costs.

During the early stages of the COVID-19 pandemic, a number of initiatives were taken to support worker absences from the workplace in an attempt to control the spread of the virus.

These included the introduction of the JobKeeper scheme, unpaid pandemic and/or annual leave at half pay (in most federal awards) and award flexibility in some cases. The JobKeeper scheme allowed eligible employers to claim a payment from the government to assist them with paying worker's wages/salaries.

The Fair Work Commission made a decision to vary 99 awards by adding unpaid pandemic leave and annual leave flexibility. For many this variation provided two weeks of unpaid leave and the ability to take twice as much annual leave at half their normal pay (if agreed to by their employer).

BizFACT

Estimates are that Australians have on average nine days of unplanned leave per year, at a cost of $570 million per year.

21.3.2 Accidents

Around 4.2 per cent of Australia's 13.4 million employees (2018) experience a work-related injury or illness each year. According to Safe Work Australia, in 2020 there were 114 435 workers' compensation claims for serious work-related injuries or illnesses involving one week or more off work, a permanent incapacity or fatality. The median time lost for a serious claim was 6 weeks, with the highest rates being among labourers and community and personal service workers.

Clerical and administrative workers and sales workers make the fewest serious claims.

The most common types of workplace fatalities are associated with road crashes, while falls from a height, or being hit by falling or moving objects are also common causes of workplace death.

All businesses need to adopt a systematic, legally compliant approach to managing work health and safety (WHS), as discussed in chapter 18.

WHS indicators are benchmarked internationally using a number of indicators, including:

- Lost Time Injury Frequency Rates (LTIFRs). A lost-time injury is an event that results in a fatality, permanent disability or time of one day/shift or more lost from work. The LTIFR is the number of lost-time injuries per million hours worked, calculated as follows:

FIGURE 21.8 Financial costs of accidents and injuries in the workplace — the 'iceberg effect'



$$\frac{\text{Number of lost – time injuries} \times 1\,000\,000}{\text{Total hours worked in accounting period}}$$

- Safe Work Australia rates based on accepted workers' compensation claims that involved the loss of one or more working weeks (termed serious claims). Claims for shorter periods are not counted in this rate.

BizFACT

Since a high in 2007 when there were 310 workplace deaths, figures have generally trended downwards. The 45–54 years age group is the most vulnerable, with 710 worker fatalities since 2003.

BizFACT

Whereas a safe workplace once meant protecting workers against physical injury, employers are increasingly looking for ways to keep staff safe from psychological harm and providing support if something does go wrong.

Workers in the finance and insurance and the health and community services industries appear especially vulnerable, with an increase in recent insurance claims.

The most common psychological injury was anxiety stress disorder, closely followed by work-related harassment or bullying.

The total cost to NSW employers of mental ill-health at work through higher levels of absenteeism (sick days) and reduced productivity through presenteeism is estimated to be $2.8 billion per year. If employers invest in psychological safety at work, the return is estimated to be up to $4 for every $1 spent.

BizFACT

Recent figures indicate that work-related injury and disease cost the Australian economy as much as $62 billion or 4 per cent of gross domestic product per year.

SNAPSHOT

Case study: Accidents in the workplace — 10 most common injuries and how to avoid them

Following is an overview of the 10 most common causes of workplace injuries.



1. **Overexertion injuries:** Injuries related to pulling, lifting, pushing, holding, carrying and throwing activities at work. Overexertion has not only consistently been the number one workplace injury but is also the most expensive.
2. **Slipping/tripping:** Falls on wet and slippery floors or trips over something lying on the floor.
3. **Falling from heights:** This type of fall happens from an elevated area such as roofs, ladders and stairways. They can be caused by slip and fall accidents or due to faulty equipment.
4. **Reaction injuries:** These are injuries caused by slipping and tripping without falling. These incidents can cause muscle injuries, body trauma and a variety of other medical issues.
5. **Falling object injuries:** Objects that fall from shelves or are dropped by another person can cause very serious injuries. Head injuries are a common result of this type of accident.
6. **Walking into injuries:** This occurs when a person accidentally runs into concrete objects such as walls, doors, cabinets, glass windows, table and/or chairs. Head, knee, neck and foot injuries are common results.
7. **Vehicle accidents:** Employees who drive for business purposes are often injured in motor vehicle accidents, some of which can be fatal.
8. **Machine entanglement:** Occurs in factories where heavy equipment and machinery are used. Clothing, shoes, fingers and hair are all vulnerable when no precaution is taken.
9. **Repetitive motion injuries:** These tend to be less obvious but are definitely harmful in the long run. Repetitive motions such as computer work that involves typing can strain muscles and tendons, causing back pain, vision problems and hand problems.
10. **Workplace violence:** Arguments in the workplace that lead to physical confrontation.

Effective workplace management involves making the workplace safe for all staff. To avoid situations such as those outlined above, SafeWork NSW has identified a number of strategies to make the workplace safe. These include:

- inspecting the workplace for potential hazards
- prioritising work tasks according to the greatest risk of injury and ensuring that safe work procedures accompany it
- regularly reviewing safe work procedures to ensure currency
- consulting with staff about ways to eliminate or reduce risk arising from potential hazards
- providing induction, training and supervision for workers so that all work tasks are conducted safely.

Best practice businesses:

- have regular safety audits and comprehensive safety programs, and use data to improve
- build a culture of safety. They communicate effectively about health and safety using visible policy statements, safety signs and reminders.
- provide careful induction and regular ongoing training for staff to ensure they are aware of safety rules and prepared for emergencies
- consult employees and health and safety personnel on the implications of changes in the workplace.

Such businesses save on compensation claims, absenteeism, lost work time, replacement costs for damaged equipment, and loss of morale in the workplace. Customers appreciate the effort businesses make in producing a safer product or service; therefore, such businesses also improve their image to their customers.

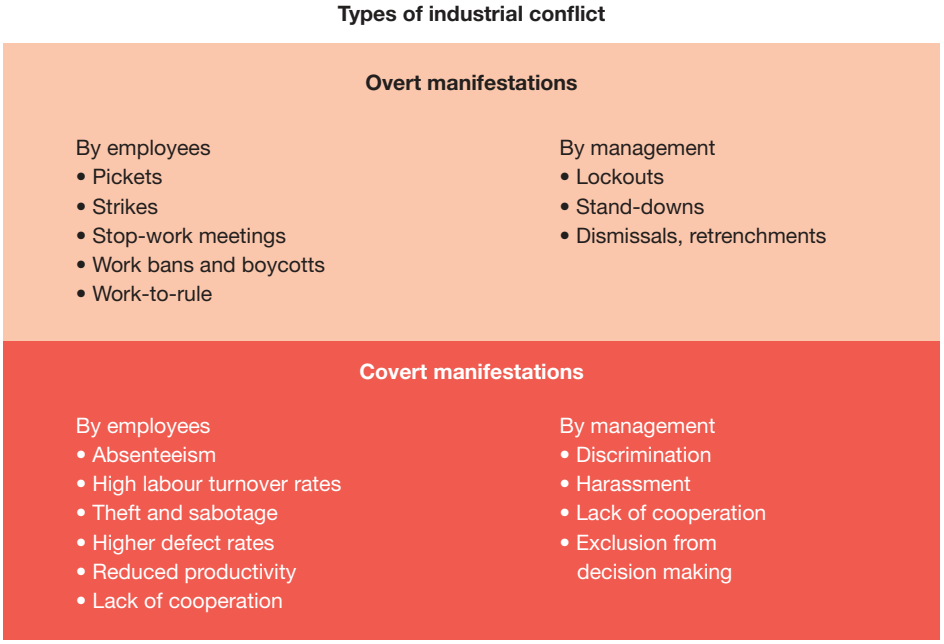
21.3.3 Levels of disputation

Chapter 20 examined the causes of industrial disputes and examined the most common manifestations or types of industrial action — strikes and lockouts. There are however, many more, often costly, overt and covert manifestations of disputes that employers need to monitor and evaluate.

Indicators of industrial disputation

Although strikes and lockouts are officially recorded indicators of industrial disputes, a range of other forms are used in the workplace, as shown in figure 21.9.

FIGURE 21.9 Types of overt and covert industrial conflict



- Work bans — a ban or boycott is a refusal to work overtime, handle a product, piece of equipment, process, or even a refusal to work with particular individuals. A green ban often refers to a refusal to carry out work that is considered harmful to the environment or natural resources such as forests.
- Work-to-rule — this action occurs when employees refuse to perform any duties additional to the work they normally are required to perform. This is most common as a form of industrial action in community services.
- Go slow — in this action, employees work at a slower rate than normal, causing customer complaints, and an expensive backlog of work to be caught up at a later date.
- Sabotage — vandalism, cyber attacks and internal theft are not uncommon, but are rarely discussed publicly by firms. They may involve employees taking action to harm or destroy the image of a firm, for example by contaminating food or disrupting production.

BizFACT

If teachers refused to do bus supervision or mark homework, this would be a work-to-rule action.

Employers should be concerned if a number of formal grievances are reported, as they are an indicator of poor quality relationships in the workplace and can be very damaging if they attract media attention or move through the legal system. Careful investigation should indicate whether these issues relate to the policies and processes operating within the business, or to specific individuals who may need further training and development or formal counselling. Ongoing grievances are likely to be reflected in higher levels of staff turnover and/or industrial disputes.

BizFACT

The ABS publishes statistics on industrial disputation in Australia. Only disputes that amount to 10 or more working days lost are counted in ABS statistics. The ABS officially recognises a range of strike actions and lockouts by employers, but does not identify work-to-rule actions, go slows and bans (e.g. overtime bans), claims, fines or other indicators.

As outlined in chapter 20, apart from negotiations related to the making of awards and agreements, managerial policy is one of the most common causes of disputes. Disputes arising from managerial policy may include the decisions and policies of line managers, organisational restructuring, discrimination, decisions that impact on work and family life, and changing work practices such as the use of outsourcing and contractors. Such disputes, when not reflected in strikes and lockouts, are more commonly reflected in grievances, fines, bans, accidents, poor customer service, declining productivity, and higher absenteeism and labour turnover.

FIGURE 21.10 Job insecurity is often linked to worker demonstrations.



Disputes are more common in large businesses where relationships and communication between employees and management tend to be more impersonal, and the scope for mistrust and misunderstanding is greater. It should be noted that industrial action is not necessarily experienced in every workplace. In more than two-thirds of Australian workplaces, workers have never taken industrial action. More covert manifestations, however, such as high absenteeism or low productivity, are more common.

FIGURE 21.11 A recent survey showed that salary, proximity to home and job security are key motivators when looking for a job. It also showed that bad management, not feeling appreciated, wanting a new challenge and too much stress were the top reasons people sought alternative employment. Overall, the survey found that 6 out of 10 Australians were happy in their job.



21.3.4 Worker satisfaction

Employee satisfaction is a key factor in employee commitment, job performance and staff turnover. Employee satisfaction surveys are useful in helping employers measure and understand how their staff feel about their work, their management and the culture of an organisation. They can be undertaken using paper surveys, online polls, focus groups or external consultants, and supplement data from performance feedback and exit interviews. Such surveys can be used to improve management style and processes, benefits and rewards systems, the physical working environment, employee relationships, and other employee needs.

Employee feedback needs to be confidential and analysed by professionals qualified to interpret such feedback. Managers need to track, communicate and act upon the results.

Although pay is an important factor in choosing a job, it is not that significant in employee satisfaction, unless there are significant pay differentials in the workplace.

In fact, employees who have good relationships with co-workers, enjoy their work activities, receive relevant training that allows them to do their job well, and gain opportunities to grow are more likely to be satisfied and stay with the business.

Effective leadership is one of the most important influences on employee satisfaction, particularly when employees feel recognised and encouraged, where management is transparent, promotion is merit based, and communication is honest and respectful. The quality of management is also a critical factor in employee satisfaction and retention, particularly with a widespread view in Australia that management is 'all talk and no action'.

BizFACT

DHL Express have been acknowledged as a great place to work and are the global market leader in international express delivery operating in 220 countries. As a service-based business, DHL offers a promise to deliver a customer's shipment by a set date or time.

DHL try to make a worthwhile contribution to society and the environment wherever possible.

During the COVID-19 pandemic, team building events were held virtually to keep engagement levels high. Also COVID-19 care packs were distributed and delivered to each employee working from home. These packs included a symbolic medal for being "Change Champions" for adapting quickly to the change.

Employee satisfaction is improved by matching the purpose of the business with the skills and cultural fit of the employee.

Employees who indicate emotional exhaustion with the job, particularly if it impacts on family life, are often less satisfied with work. Employees value a family-friendly culture, adequate breaks during the day, effective resourcing to do their job, rewards for effort and performance, opportunities for sabbaticals or 'leave' options, and workplace wellbeing strategies such as a gym.

Support for emerging leaders is also appreciated by employees. Ongoing training and mentoring or coaching is much more effective than pay differentials in fostering employee commitment.

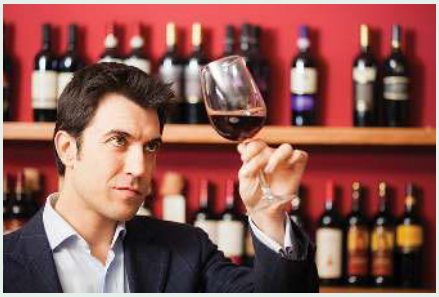
FIGURE 21.12 Employees are more satisfied and committed when given continuous 'on the job' training for competencies rather than offsite training



It is the holistic approach to employees, which values and cares for them, that is the most effective in building commitment, satisfaction and retaining effective employees.

SNAPSHOT

Case study: Evaluating human resource effectiveness at Fine Wines



Ryan, the human resources manager at Fine Wines, concludes his presentation to the other managers in the business and comments, 'So, the major problem we have at the moment is this persistent absenteeism across the business'.

'That would appear to be the case Ryan, but how do we compare to our competitors? Is it an industry-wide issue or just a problem we have?' asks Priya, the CEO of the organisation.

'Well in the finance section it's mostly the parents with young kids', offers Mel.

'Not in my department', says Caroline, the marketing manager. 'The ones taking time off, especially on a Monday and a Friday are the graduates — they want to party all weekend and then have their recovery on a work day!'

The group finds this amusing.

'What about the operations department?' asks Priya.

'Well', replies Spiro, the operations manager, 'with us it's the young single blokes; the older blokes or those that are married seem to get it — you work and then you only have days off if necessary'.

'What about the women in your department?' asks Priya looking in Spiro's direction.

'No dramas there — in fact their attendance is excellent. Even if they don't feel well, they drag themselves in to work. As a matter of fact, during the winter just passed I had to tell a few of them they needed to go home and rest. It's not the high rates of absenteeism but more that they come to work when they shouldn't!' replies Spiro.

'In my department it tends to be the older permanent workers that are away the most. The contractors are never a problem', Jane, manager of IT, offers.

'So, across all the departments it seems that absenteeism exists among certain groups of workers. We don't seem to have dealt with the problem. I am curious about this, especially why it is happening. Ryan, I recommend you get everyone in your department together, investigate the problem in greater depth and get back to us all at the next meeting', Priya instructs.

'All good, Priya I'll get onto it', Ryan replies.

on Resources

Video eLesson Workplace accidents and Australia Post (eles-1047)

KEY IDEAS

- Absenteeism is measured as the average rate of employee absences on an average day, without sick leave or leave approved in advance.
- High levels of absenteeism and/or lateness may indicate that workers are dissatisfied or that there is conflict within the workplace.
- Around 5.3 per cent of Australia's almost 13 employees experience a work-related injury or illness each year.
- A low level of accidents, as measured by the Lost Time Injury Frequency Rate (LTIFR), indicate effective human resource management strategies.
- Employers need to closely monitor both overt and covert manifestations of industrial disputes to evaluate relationships in the workplace.
  Employers should be concerned if a number of formal grievances are reported, as they are an indicator of poor quality relationships in the workplace and can be very damaging if they attract media attention or move through the legal system.

- Employee satisfaction can lead to a more positive workplace culture and reduce staff turnover, and is essential if the business wants to ensure higher revenues.
- Employees who have good relationships with co-workers, enjoy their work activities, receive relevant training that allows them to do their job well, and gain opportunities to grow are more likely to be satisfied and stay with the business.
- Employee satisfaction is improved by matching the purpose of the business with the skills and cultural fit of the employee.

21.3 Activities

learnON

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21.3 Quick quiz on	21.3 Exercise	21.3 Exam questions

Select your pathway

LEVEL 1	LEVEL 2	LEVEL 3
1, 3, 8, 11, 12, 15	4, 5, 6, 7, 10, 13, 14, 16, 17, 18, 19, 21	2, 9, 20, 22

21.3 Exercise

Revision

1. The absenteeism rate at Extracus Minerals has increased by 78 per cent over the past 12 months. **Identify** the possible causes of the increase.
2. **a.** In small groups, discuss whether it is acceptable for an employee to take a 'sickie':
   i. to care for a sick child or elderly parent
   ii. to farewell a friend about to leave for an overseas holiday
   iii. because they feel unappreciated at work.
   b. Summarise your responses and present them to the rest of the class.
   c. Compare your responses with those from other groups.
   d. Analyse the groups' responses.
3. **What** are the direct and indirect costs of accidents and injuries in the workplace?
4. **Propose** a practical strategy to ensure young employees apply work health and safety rules effectively.
5. **Account** for the use of covert types of industrial conflict by (a) employees and (b) management.
6. **Why** are industrial disputes more common in large businesses?
7. **Explain** how the level of industrial disputes can indicate the effectiveness of a business's human resource strategies.
8. **Identify** the major factors that lead to employee satisfaction in the workplace.
9. **Evaluate** the effectiveness of employee satisfaction surveys.
10. **a. Discuss** the issues that should be considered in designing an employee satisfaction survey.
    b. Construct an employee satisfaction survey for a workplace that you are familiar with.

Read the 'Absenteeism — sickies cost' case study and complete questions 11 to 14.

11. **Outline** all the possible reasons for Jordan's high levels of absenteeism and labour turnover.
12. **Describe** the major costs of this level of absenteeism and turnover.
13. Draw up a table listing all of Lloyd's suggestions and **explain**, next to each suggestion, why it may be useful in resolving Jordan's problems.
14. Interview an adult about their opinions on absenteeism. **Discuss** their views with your class.

Read the 'Accidents in the workplace — 10 most common injuries and how to avoid them' case study and complete questions 15 and 16.

15. **Outline** the 10 most common causes of workplace injuries.

16. Imagine you have been appointed to the role of a WHS manager. **Recommend** initiatives that you believe would be effective in reducing the occurrence of the listed common injuries.

Read the 'Evaluating human resource effectiveness at Fine Wines' case study and answer question 17.

17. Organise groups and allocate a role to each as a member of Ryan's HR team at Fine Wines. Each group should **discuss** the effectiveness of human resource management in the business with respect to the issues identified and **recommend** strategies that the HR team could present to the CEO to address the problem. Present the findings to the class.

Extension

18. **Explain** how you would develop your own future workplace to maximise employee satisfaction, performance and retention in a cost-effective manner.

Read the following and answer questions 19 to 21.

Jasmine manages a printing business, which is now merging with a large stationery business. The new business's location is half an hour's drive north of the current location, which is in an inner suburb of a large city, close to public transport. Jasmine and her new partner, Paul, will both reduce their workforce by one-third and merge their staff. The new structure will have several sections including printing, customer sales, accounting and finance, and warehouse and distribution. Significant change will occur.

19. **Discuss** some of the human resources issues that may arise during the change.
20. **Analyse** how the human resource managers may be involved in each step. **Determine** all the things that will need to change, such as production systems, and 'people management' issues involved in merging two workforces, such as teamwork, communication and resistance to change.
21. **Recommend** a communication strategy for Jasmine in the merger and identify its benefits.
22. You operate a travel agency, Worldover, employing 50 staff in a flat management structure. You employ four managers, responsible for customer service and sales, administration, marketing, and finance and accounting. Staff turnover in sales and customer service is 45 per cent, in administration and marketing it is 10 per cent, while the accounting and clerical staff has remained largely intact over the past decade. Staff turnover is high during the first weeks of employment. Staff in customer service are frequently involved in disputes with administration and marketing staff. Although there has been no real decline in customers 'walking through the doors', sales have fallen 30 per cent in recent years. Feedback from customers indicates that frequent errors are made in bookings, and that service is not consistent.
    a. Recommend possible solutions for the business's problems.
    b. How could staffing needs be more effectively planned?
    c. **Create** a grid-based rewards system showing the short- and long-term financial and non-financial rewards that may help you improve customer service.

21.3 Exam questions

Question 1 (20 marks)

Source: HSC 2020 Business Studies Exam, Section IV, Q27

Evaluate human resource strategies used to achieve THREE indicators of effective human resource management.

Question 2 (10 marks)

Source: HSC 2020 Business Studies Exam, Section II, Q21

a. Outline the role of ONE external stakeholder who represents the interests of employees in workplace disputes. **(2 marks)**
b. Distinguish between voluntary and involuntary separation. **(4 marks)**
c. Explain how technological influences and globalisation can lead to a company reducing staff numbers. Support your answer with relevant examples. **(4 marks)**

Question 3 (1 mark)

Source: HSC 2019 Business Studies Exam, Section I, Q17

The table compares four businesses on an annual basis.

	A	*B*	*C*	*D*
Absenteeism (average per employee)	8	5	8	5
Accidents per 500 employees	4	2	2	4
% of staff turnover	11	9	9	11
Average output per employee	10	14	10	14

Which business is likely to compromise work safety in return for an increase in output?

A. *A*
B. *B*
C. *C*
D. *D*

Question 4 (6 marks)

Source: HSC 2017 Business Studies Exam, Section II, Q23c

A business has been rapidly expanding and requires additional staff.

The expansion of the business has led to conflict and uncertainty in the workplace.

Recommend TWO indicators that could be used by the business to measure the effectiveness of human resource management.

Question 5 (4 marks)

Source: HSC 2015 Business Studies Exam, Section II, Q25a

The table contains data about a business in 2014 and 2015. Use the information in the table to answer the question that follows.

	2014	*2015*
Absenteeism per employee	10 days	18 days
Accidents per 1000 employees	20	25
Number of strike days	20	10
Training expenditure per employee	$2000	$500
Staff turnover	10%	5%
Fixed costs	$1 000 000	$800 000
Expense ratio (expenses ÷ sales)	20%	10%

To what extent is human resources management effective in this business? Support your answer with examples from the data.

More exam questions are available in your learn ON title.

21.4 Review

21.4.1 Summary

Corporate culture, benchmarking key variables and changes in staff turnover

- Human resource indicators are used by many businesses to evaluate the effectiveness of the business, team or individual.
- The best way to maximise employee productivity and motivation is through a constructive corporate culture, where employees are trusted, collaborate, have strong personal relationships and are highly trained and mentored.
- Benchmarking is a process in which indicators are used to compare business performance between internal sections of a business or between businesses.
- Benchmarking may be undertaken using informal benchmarking, performance benchmarking, best practice benchmarking and balanced scorecard benchmarking.
- A human resource audit can be used to systematically analyse and evaluate human resource activities and their effectiveness.
- Quantitative measures should be able to demonstrate the actual effect of indicators in economic terms.
- Qualitative evaluation involves detailed feedback and research on key issues, which allows judgements to be made about change in behaviour or quality of service provided.
- Staff turnover refers to the separation of employees from an employer, both voluntary and involuntary, through dismissal or retrenchment.
- In assessing the significance of turnover, it is important for businesses to benchmark their turnover against that of other businesses in the industry; and to determine the type of staff leaving and their reasons.

Absenteeism, accidents, levels of disputation and worker satisfaction

- Absenteeism is measured as the average rate of employee absences on an average day, without sick leave or leave approved in advance.
- High levels of absenteeism and/or lateness may indicate that workers are dissatisfied or that there is conflict within the workplace.
- Around 5.3 per cent of Australia's almost 13 employees experience a work-related injury or illness each year.
- A low level of accidents, as measured by the Lost Time Injury Frequency Rate (LTIFR), indicate effective human resource management strategies.
- Employers need to closely monitor both overt and covert manifestations of industrial disputes to evaluate relationships in the workplace.
  Employers should be concerned if a number of formal grievances are reported, as they are an indicator of poor quality relationships in the workplace and can be very damaging if they attract media attention or move through the legal system.
- Employee satisfaction can lead to a more positive workplace culture and reduce staff turnover, and is essential if the business wants to ensure higher revenues.
- Employees who have good relationships with co-workers, enjoy their work activities, receive relevant training that allows them to do their job well, and gain opportunities to grow are more likely to be satisfied and stay with the business.
- Employee satisfaction is improved by matching the purpose of the business with the skills and cultural fit of the employee.

21.4.2 Key terms

absenteeism refers to a worker who neglects to turn up for work when they were scheduled to do so
balanced scorecard benchmarking used for measuring whether the activities of a business are meeting its objectives established in the strategic plan. It benchmarks key performance variables with targets aligned with the strategic plan.
benchmarking a process in which indicators are used to compare business performance between internal sections of a business or between businesses
best practice benchmarking involves comparing performance levels with those of another best practice business in specific areas using a structured process to gain skills and knowledge and to modify organisational processes
corporate culture the values, ideas, expectations and beliefs shared by members of a business
human resource audit a diagnostic tool used to evaluate HR policies and practices in order to identify problems and develop solutions in an attempt to rectify problems
indicators performance measures that are used to evaluate organisational or individual effectiveness
informal benchmarking includes any strategies such as networking through informal discussions with colleagues in other businesses, undertaking visits to other businesses, researching best practice online and attending conferences
performance benchmarking involves comparing the performance levels of a process/activity with other businesses
staff turnover the loss of employees who leave the business for a variety of reasons

on Resources

Digital documents	Key terms glossary (doc-35678) Chapter crossword (doc-36226)
Interactivity	Chapter crossword (int-7181)
Exam question booklet	Chapter 21 Exam question booklet (eqb-0043)

21.4 Activities

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Exercise 1: Multiple choice questions

1. Why is human resources benchmarking used?
   - **A.** To compare one business's human resource function with another business's human resource function
   - **B.** To evaluate the effectiveness of the human resource manager's contribution
   - **C.** To compare business performance between internal sections of a business
   - **D.** To reduce high staff turnover

2. Which of the following is not a strategy to build a positive workplace culture?
   - **A.** Creative perks
   - **B.** Family-friendly practices
   - **C.** High levels of training and mentoring
   - **D.** Free after work drinks for supervisors only

3. What does the following data show?

	2013	2014
ROI	$0.19	$0.40
Unscheduled absence	7.74 days	7.03 days

A. There has been an improvement in the management of human resources.
B. Fewer employees are separating.
C. There has been an improvement in training and rewards.
D. The return to work rate has improved.

4. The manager of Never-Scratch Sunglasses is seeking to evaluate a wide range of aspects of a company's performance against its strategic plan. What would be a useful initial approach?
A. An outside consultant to analyse problems and suggest solutions
B. A management meeting to investigate the best process for looking for variations.
C. Legal compliance analysis
D. Benchmarking one division against another

5. Indicators of improvements in the human resource function could include which of the following?
A. Falling sales per employee
B. Higher staff turnover
C. Reduced time lost to injuries and sickness
D. Fewer opportunities for promotion

6. Exit interviews are a useful tool for evaluation for human resource management. These are which of the following?
A. Used by most Australian businesses
B. Used by around 5 per cent of Australian businesses
C. Used by 25 per cent of Australian businesses
D. Useful only for evaluating job descriptions and job specifications

7. Which employees are most likely to be injured at work?
A. Labourers
B. Young females in the beauty industry
C. Older females in aged care
D. Older males engaged in physical work

8. What are the most commonly used indicators to assess general HR effectiveness?
A. Labour costs and resignation rate
B. Growth in market share and labour turnover costs
C. Number of staff and labour costs
D. Labour costs and sales per employee

9. Which of the following would not be an indicator of poor workplace culture?
A. High levels of training
B. High levels of absenteeism
C. Critical feedback from customers
D. High staff turnover

10. What are two covert forms of industrial dispute?
A. Sabotage and harassment
B. Work-to-rule and discrimination
C. Exclusion from decision making and boycotts
D. Reduced productivity and work-to-rule

Exercise 2: Exam practice questions

Question 1 (5 marks)

a. **What** is corporate culture? **(1 mark)**

b. **Describe** the importance of corporate culture in a business you have studied. **(4 marks)**

Question 2 (4 marks)

Justify TWO key variables as indicators used when benchmarking human resource management.

Question 3 (5 marks)

Critically **analyse** why absenteeism is sometimes seen as an indication of worker dissatisfaction.

Question 4 (6 marks)

a. **List** ONE direct and ONE indirect cost of accidents in the workplace. **(2 marks)**

b. **Recommend** TWO strategies that can be used to reduce accidents in the workplace. **(4 marks)**

Question 5 (4 marks)

Distinguish between overt and covert industrial conflict.

Question 6 (5 marks)

Evaluate the effectiveness of human resource management in a business you have studied.

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Topic 4 Human resources review

Human resources: Practice examination

Section I — Multiple choice questions (10 marks)

1. An employer, for legal purposes, does which of the following?
   - **A.** Exercises control over employees
   - **B.** Determines the degree of supervision required for an employee
   - **C.** Has the responsibility of the payment of wages
   - **D.** All of the above
2. The four main elements of the human resource cycle/staffing process are which of the following?
   - **A.** Acquisition, development, managing diversity and separation
   - **B.** Acquisition, recruitment, motivation, maintenance and separation
   - **C.** Acquisition, development, maintenance and separation
   - **D.** Acquisition, development, maintenance and performance management
3. Which of the following would not be considered a potential advantage of outsourcing?
   - **A.** Lack of quality control
   - **B.** Access to experts
   - **C.** Cost savings
   - **D.** Expand capacity
4. Which of the following correctly describes awards?
   - **A.** Collective agreements that set out wages and conditions of employees
   - **B.** Legally enforceable formal agreements made by employers and employees at the industry level
   - **C.** Collective agreements made at a workplace level with an employer
   - **D.** Agreements made between an employee and an employer
5. Which of the following features are not part of an employment contract?
   - **A.** Duties
   - **B.** Location of the workplace
   - **C.** Bonuses
   - **D.** Trade union membership
6. Benefits employers gain from demonstrating corporate social responsibility in managing staff include which of the following?
   - **A.** Improved staff retention and reduced absenteeism as staff feel more valued
   - **B.** Business costs are reduced through reduced claims and fines
   - **C.** Reduced training and marketing costs
   - **D.** All of the above
7. Performance management includes which of the following?
   - **A.** Developing strategies to improve the way a business operates to improve efficiency
   - **B.** Systematically evaluating and managing employee performance in order to achieve the best outcome for the business
   - **C.** Planning for future human resource needs both at the managerial and non-managerial level
   - **D.** Designing a job and how it will interact with other jobs and employees in such a way as to motivate and retain an employee
8. Which of the following represents a non-monetary reward for employees?
   - **A.** Bonuses
   - **B.** Superannuation
   - **C.** Allowances
   - **D.** Challenging work

9. What is the term for an unresolved dispute that requires the Fair Work Commission to make a legally binding decision?
   - **A.** Conciliation
   - **B.** Grievance procedure
   - **C.** Negotiation
   - **D.** Arbitration
10. Which of the following are indicators used to evaluate the effectiveness of human resource management?
   - **A.** Absenteeism, staff turnover, workplace injuries, industrial disputes
   - **B.** Inventory turnover, sales per employee, industrial disputes, labour costs
   - **C.** Workplace injuries, staff turnover, sales per employee, profit margins
   - **D.** Industrial disputes, absenteeism, labour costs, marketing costs

Section II — Short answer questions (50 marks)

1.	**a.**	**Define** the term 'human resource management'.	**2 marks**
	b.	**What** is the role of human resource management in business?	**4 marks**
2.	**a.**	**Why** is work–life balance important for employees?	**2 marks**
	b.	**Propose** strategies for managing employees' work–life balance.	**3 marks**
	c.	An accountant is often late for work, his productivity has decreased and some clients have complained that he is slow to respond to their requests. As a human resource manager, **analyse** how you would handle this situation.	**6 marks**
3.	**a.**	**Outline** two ways in which governments influence human resource management.	**2 marks**
	b.	**Distinguish** between an enterprise agreement and an individual contract.	**4 marks**
	c.	**Explain** the workplace dispute resolution process.	**6 marks**
4.	**a.**	**List** three indicators of the effectiveness of human resource management.	**3 marks**
	b.	**Evaluate** strategies used to support more effective human resource management.	**6 marks**
5.	**a.**	**Describe** the process of human resource management.	**2 marks**
	b.	**Distinguish** between performance appraisal and performance management.	**4 marks**
	c.	**Propose** a set of guidelines an employer may use to eliminate discrimination in the workplace.	**6 marks**

Section III — Extended response questions

1. Cooper is the sales manager at Morgan's Cycles. At the weekly breakfast meeting he indicated there had been a substantial decrease in sales in the current financial year. He claimed the marketing staff were directly responsible for this decline and stated that consequently jobs may be lost. Many members of the sales team were disappointed with Cooper's comments and some were quite angry. The previous year's sales had exceeded the company's target but Cooper did not acknowledge it at the meeting.
   Brian, the chief executive of the business, hears of the tension in the sales department and hires you to write a business report where you:
   - **outline** the interdependence between marketing and human resources
   - **recommend** strategies for more effective human resource management
   - **evaluate** indicators of the effectiveness of human resource management.
2. David has been newly appointed as the human resource manager for a national golf club manufacturer. He meets with the managers of each of the key functional areas and notes that, in particular, there appear to be problems with the operations processes and that, more generally, workplace culture seems poor.
   He has seen the outdated machinery in some parts of the factory and workers reported to him at the time that it produces equipment of low quality. Where newer machinery has been introduced, there appears to be a mismatch between worker skills and the capacity to use the machines effectively. He has also heard there are often accidents in the factory. Workers appear dissatisfied and are threatening industrial action.
   David contacts you to write a business report. In your report:
   - **outline** the operations influences that may have affected the business
   - **explain** how effective operations strategies will help the business sustain its competitive advantage
   - **analyse** how understanding human resource processes can address the business's corporate culture.
3. **Assess** the advantages of a diverse, culturally competent workforce for a global business.
4. **Analyse** the causes of workplace disputes and the strategies used to resolve them.

Human resources: Practice business report — 20 marks

Your answer will be assessed on how well you:
- demonstrate knowledge and understanding relevant to the question
- apply the hypothetical business situation
- communicate using relevant business terminology and concepts
- present a sustained, logical and cohesive response in the form of a business report.

The global pandemic has had a dramatic effect on employment in the higher education sector in Australia. Universities have been forced to undertake immediate cost reduction in the area of human resources, including employee pay cuts, reduced casual staff, minimal salary increases and hiring freezes. Other workers have been offered redundancies and, for those that remain, there is the need to retrain and demonstrate agility by delivering lectures and tutorials online.

The longer-term consequences of such cost cuts appear to be ongoing human resource management concerns around staff shortages, loss of teaching experience and, as a consequence, a decline in quality of programs and courses.
- Outline the human resource stakeholders affected by the changes brought on by the cost reductions.
- Describe the technological and social changes that may affect employees.
- Analyse the human resource processes that will need to be addressed.

on Resources

Digital document Sample HSC Business Report (doc-14150)

APPENDIX: Understanding Key Process Verbs

Assessment using key process verbs

The purpose of a key process verb in a question is to provide instructions on how to answer a question and how much to write. There is a direct relationship between the type of key process verb and the mark value allocated. The more thinking skills the key process verb requires, the higher the mark allocated.

Below is a colour coded list of the key process verbs that may be used for assessment. It is divided into three categories based on Bloom's Taxonomy. Each category represents the level of thinking skills required to complete a question. We have also included in the Key Process Verb list common exam terms such as 'Why', 'How', 'What' to help explain how to answer questions using these terms.

Mark allocation

The suggested marks used in these examples are specifically for short answer questions. Essay questions may also include a number of key process verbs.

Lower order thinking questions	**Clarify, define, describe, extract, identify, list, outline, recall, recount, state, summarise, what, when**	**1–3**
Middle order thinking questions	**Account, apply, calculate, classify, compare, construct, contrast, deduce, demonstrate, discuss, distinguish, examine, explain, how, interpret, investigate, justify, propose, recommend, to what extent, why, with reference to**	**3–6**
Higher order thinking questions	**Analyse, appreciate, assess, create, critically analyse/evaluate, detail, determine, evaluate, extrapolate, predict, synthesise**	**6–12**

Time allocation

In order to complete each question, time allocation is very important. If a student does not complete the examination in time, because they have not calculated the minutes/marks correctly, they will lose marks. A formula for calculating minutes/marks is as follows:

$$Marks/minute = \frac{Total\ exam\ time\ in\ minutes}{Total\ exam\ marks} = minutes/mark$$

$$Example: Marks/minute = \frac{180\ exam\ minutes\ (3hrs)}{100\ exam\ marks} = 1.8\ minutes/mark$$

In the above example, the student would need to allocate 1.8 minutes per mark in an examination. Therefore, a 4-mark question should be allocated 1.8 minutes × 4 = 7.2 minutes (or rounded to seven minutes). This ensures the allocation of an appropriate amount of time for each question.

Definitions and examples

LOWER ORDER THINKING key process verbs	LOWER ORDER examples
Short answer questions using the lower order thinking key process verbs will typically have a mark value between 1 and 3.	
Clarify — make clear or plain.	**Clarify** the reasons for…
Define — state meaning and identify essential qualities.	**Define** the term…
Describe — provide characteristics and features.	**Describe** four roles…
Extract — choose relevant and/or appropriate details.	**Extract** the issues that may arise…
Identify — recognise and name.	**Identify** two effects of…
List — make a list of.	**List** the four components of…
Outline — sketch in general terms; indicate the main features of.	**Outline** the roles of…
Recall — present remembered ideas, facts or experiences.	**Recall** the factors that…
Recount — retell a series of events.	**Recount** under what circumstances…
State — describe the main points clearly and specifically.	**State** how a business may address…
Summarise — express, concisely, the relevant details.	**Summarise** how the two issues affected the…
What — describe, provide characteristics or features.	**What** are business plans…
When — indicate at what time or in what circumstances.	**When** do business owners…

MIDDLE ORDER THINKING key process verbs	MIDDLE ORDER examples
Short answer questions using the middle order thinking key process terms will typically have a mark value between 3 and 6.	
Account — account for; state reasons for; report on. Give an account of; narrate a series of events or transactions.	**Account** for the improvements to…
Apply — use, utilise, employ in a particular situation.	**Apply** one of the processes relevant to…
Calculate — ascertain/determine from given facts, figures or information.	**Calculate** which you believe to be the more…
Classify — arrange or include in classes/categories.	**Classify** the following list of consumers into the…
Compare — show how things are similar or different.	**Compare** the problems experienced by…
Construct — make; build; put together items or arguments.	**Construct** a SWOT analysis for the following small businesses…
Contrast — show how things are different or opposite.	**Contrast** a range of businesses with different legal structures…
Deduce — draw conclusions.	**Deduce** what impact this had on the…
Demonstrate — show by example.	**Demonstrate** the opportunities a business can…
Discuss — identify issues and provide points for and/or against.	**Discuss** the role of…
Distinguish — recognise or note/indicate as being distinct or different from; note differences between.	**Distinguish** between internal and external growth…
Examine — inquire into.	**Examine** the reasons for…

Explain — relate cause and effect; make the relationships between things evident; provide why and/or how.	**Explain** the processes undertaken…
How — explain.	**How** does Tracy track…
Interpret — draw meaning from.	**Interpret** the reasons for the business owner deciding to…
Investigate — plan, inquire into and draw conclusions.	**Investigate** three options available to the employees…
Justify — support an argument or conclusion.	**Justify** your selection…
Propose — put forward (for example a point of view, idea, argument, suggestion) for consideration or action.	**Propose** a plan that may provide the business with…
Recommend — provide reasons in favour.	Use the information provided to **recommend** a strategy…
To what extent — show the impact, how broadly something is affected.	**To what extent** does human resource management have an impact on...
Why — explain the cause and effect relationship.	**Why** is it important to...
With reference to — in regards to, relating to.	**With reference to** a case study...

HIGHER ORDER THINKING key process verbs	HIGHER ORDER examples
Short answer questions using the higher order thinking key process verbs will typically have a mark value between 6 and 12.	
Analyse — identify components and the relationship between them; draw out and relate implications.	**Analyse** the impact of changes to the…
Appreciate — make a judgement about the value of.	**Appreciate** the importance of government bodies…
Assess — make a judgment of value, quality, outcomes, results or size.	**Assess** the importance of…
Create — produce; design; invent; devise a new solution or plan.	**Create** a marketing strategy suitable to a business at this stage…
Critically analyse/evaluate — add a degree or level of accuracy, depth, knowledge and understanding, logic, questioning, reflection or quality.	**Critically analyse** this statement…
Detail — give specific information about it.	**Detail** the four steps involved...
Determine — make a decision or work out an answer after appropriate thought and investigation.	**Determine** whether the change required would…
Evaluate — make a judgement based on criteria; determine the value of.	**Evaluate** the processes…
Extrapolate — infer from what is known.	**Extrapolate** the data found in…
Predict — suggest what may happen based on available information.	**Predict** the outcome for a business if the following…
Synthesise — put together various elements to make a whole.	Consider a business's function and **synthesise** this information…

GLOSSARY

absenteeism refers to a worker who neglects to turn up for work when they were scheduled to do so

acceptable quality products that are safe, lasting and with no faults, look acceptable and do all the things someone would normally expect them to do

accounting equation a equation that shows the relationship between assets, liabilities and owners' equity, which forms the basis of the accounting process

acquisition the process of attracting and recruiting the right staff for roles in a business

advertising a paid, non-personal message communicated through a mass medium

advertising media refers to the many forms of communication used to reach an audience

affirmative action measures taken to eliminate direct and indirect discrimination, and for implementing positive steps to overcome the current and historical causes of lack of equal employment opportunity for women

ageing of the workforce refers to the increase in the average age of the population, due to sustained low fertility and increasing life expectancy. As a result, there are proportionally fewer children under 15 in the population, and more people in older age groups.

analysis working financial information into significant and acceptable forms that make it more meaningful, and highlighting relationships between different aspects of a business

appreciation an upward movement of the Australian dollar (or any other currency) against another currency

assets items of value owned by a business

attitude a person's overall feeling about an object or activity

audit an independent check of the accuracy of financial records and accounting procedures

Australian Securities Exchange (ASX) the primary stock exchange group in Australia

availability of funds refers to the ease with which a business can access funds (for borrowing) on the international financial markets

award the legally enforceable minimum terms and conditions that apply to a business or industry

award simplification the process of reducing the number of matters in each award and eliminating inefficient work practices

B2B direct access from one business (the supplier) to another (the buyer), allowing the supplier to assess the needs of the buyer and meet them in a timely manner

B2C the selling of goods and services to consumers over the internet, with payment usually by credit card

balance sheet a summary of a business's assets and liabilities at a particular point in time, expressed in money terms; represents the net worth of the business

balanced scorecard benchmarking used for measuring whether the activities of a business are meeting its objectives established in the strategic plan. It benchmarks key performance variables with targets aligned with the strategic plan.

behavioural segmentation the process of dividing the total market according to the customers' relationship to the product

benchmarking a process in which indicators are used to compare business performance between internal sections of a business or between businesses

best practice refers to business practices that are regarded as the best or of the highest standard in the industry

best practice benchmarking involves comparing performance levels with those of another best practice business in specific areas using a structured process to gain skills and knowledge and to modify organisational processes

'better off overall test' (BOOT) requires that each of the employees to be covered by the agreement is better off overall than under the relevant modern award

blog an online journal that can be added to by readers

bottleneck an aspect of the transformation process that slows down the overall processing speed or creates an impediment, leading to a backlog of incompletely processed products

brand a name, term, symbol, design or any combination of these that identifies a specific product and distinguishes it from its competition
brand loyalty when a favourable attitude towards a single brand results in repeat sales over time
brand name that part of the brand that can be spoken
brand symbol or **logo** a graphic representation that identifies a business or product
budget a financial document used to estimate future revenue and expenses over a period of time
bundle pricing where customers gain a 'package' of goods and services in addition to the tangible good they purchased
capital–labour substitution machinery and technology displace people by doing the work they do
carbon footprint the amount of carbon produced and entering the environment from operations processes
cash flow the movement of cash in and out of a business over a period of time
cash flow statement a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time
casual employee an employee in employment that is short term, irregular and uncertain; they are not entitled to paid holiday or sick leave
centralised industrial relations system a collectivist approach in which disputes are referred to industrial tribunals, such as the Fair Work Commission, for conciliation and arbitration
channel any method used for carrying a message
clean payment occurs when the exporter ships the goods directly to the importer before payment is received
code of conduct a statement of acceptable and unacceptable behaviours in a business
code of ethics a statement of a firm's values and principles
code of practice a statement of the principles used by a business in its operations. It generally refers to practices that are seen as ethical or socially responsible.
collective agreement an agreement made between a group of employees (or one or more unions representing employees) and an employer or group of employers
commercial bills primarily short-term loans issued by financial institutions, for larger amounts (usually over $100 000) for a period of generally between 30 and 180 days
common law law developed by courts and tribunals
competition-based pricing where the price covers costs (cost of raw materials and the cost of operating the business) and is comparable to the competitor's price
competitive positioning relates to how a business will differentiate its products
compliance costs the expenses associated with meeting the requirements of legal regulations, i.e. abiding by all laws
computer-aided design (CAD) a computerised design tool that allows businesses to create product possibilities from a series of input parameters
computer-aided manufacturing (CAM) software that controls manufacturing processes
constitutional corporation one that falls under section 51(xx) of the Constitution of Australia — identified as foreign corporations and trading or financial corporations formed within the limits of the Commonwealth
consumer guarantees provide consumers with rights to certain remedies from retailers and manufacturers where goods purchased fail to comply with the consumer guarantee provisions in the ACL
consumer market a market that consists of individuals — that is, members of a household who plan to use or consume the products they buy
continuous improvement an ongoing commitment to improving a business's goods or services
contractor an external provider of services to a business. It may be an individual or a business.
control occurs when KPIs are assessed against predetermined targets and corrective action is taken if required
controlling involves the comparison of planned performance against actual performance and taking corrective action to make sure the objectives are attained
corporate culture the values, ideas, expectations and beliefs shared by members of a business
corporate social responsibility (CSR) open and accountable business actions based on respect for people, community/society and the broader environment. It involves businesses doing more than just complying with the laws and regulations.

cost as a performance objective, refers to the minimisation of expenses so that operations processes are conducted as cheaply as possible

cost centres particular areas, departments or sections of a business to which costs can be directly attributed

cost leadership involves aiming to have the lowest costs or to be the most price-competitive in the market

cost of goods sold the value of stock that a business has sold to its customers

cost-based competition derived from determining breakeven point (the level at which the firm's total revenue is exactly equal to its total costs) and applying strategies to create cost advantages over competitors

cost-based pricing a pricing method derived from the cost of producing or purchasing a product and then adding a mark-up

critical path analysis (CPA) a scheduling method or technique that shows what tasks need to be done, how long they take and what order is necessary to complete those tasks

currency swap an agreement to exchange currency in the spot market with an agreement to reverse the transaction in the future

current assets assets that a business can expect to convert into cash within 12 months. They usually include cash and accounts receivable.

current liabilities liabilities that a business must repay within the short term. They usually include overdraft and accounts payable.

customer choice (buying behaviour) the decisions and actions of customers when they search for, evaluate, select and purchase goods and services

customer orientation the process of collecting information from customers and basing marketing decisions and practices on customers' wants and interests

customer relationship management (CRM) the systems that businesses use to maintain customer contact

customer satisfaction measures how goods and services supplied by a business meet or exceed customer expectation

customer service refers to how well a business meets and exceeds the expectations of customers in all aspects of its operations

customisation refers to creation of individualised products to meet the specific needs of the customers

customised approach or **local approach** a global marketing strategy that assumes the way the product is used and the needs it satisfies are different between countries

customised goods those that are varied according to the needs of customers. These goods are produced with a market focus rather than a production focus.

customised pricing occurs whenever consumers in different countries are charged different prices for the same product

debenture a promise issued by a company to repay a loan for a fixed rate of interest and for a fixed period of time

debt finance relates to the short-term and long-term borrowing from external sources by a business

decentralised industrial relations system a system in which employers and employees negotiate wages and working conditions in the individual workplace, through collective or individual bargaining and without the involvement of tribunals

demand the quantity of a product consumers are willing to purchase at a particular price

demographic segmentation the process of dividing the total market according to particular features of a population, including the size of the population, age, sex, income, cultural background and family size

dependability as a performance objective, refers to how consistent and reliable a business's products are

derivatives simple financial instruments that may be used to lessen the exporting risks associated with currency fluctuations

development refers to enhancing the skills of the employee in line with the changing and future needs of the organisation

discretionary income disposable income that is available for spending and saving after an individual has purchased the basic necessities of food, clothing and shelter

discrimination when a policy or a practice disadvantages a person or a group of people because of a personal characteristic that is irrelevant to the performance of the work

distribution the ways of getting the goods or services to the customer
distribution channels or **marketing channels** the routes taken to get the product from the factory to the customer
dividend a distribution of a company's profits (either yearly or half-yearly) to shareholders, calculated as a number of cents per share
e-commerce the buying and selling of goods and services via the internet
e-marketing (electronic marketing) the practice of using the internet to perform marketing activities
e-procurement the use of online systems to manage supply, which allows suppliers direct access to the business's level of supplies
efficiency the ability of a business to minimise its costs and manage its assets so that maximum profit is achieved with the lowest possible level of assets
employee a worker under the control of an employer. This control includes the workplace location, the way that the work is to be performed and the extent to which supervision will be exercised.
employee poaching the practice of enticing employees to work for another business
employee selection involves gathering information about each applicant for a position, then using that information to choose the most appropriate applicant
employer one who exercises control over employees, has responsibility for the payment of wages and/or salaries and has the power to dismiss employees
employer association an organisation that represents and assists employer groups. They are usually respondents to the awards covering the employees of their members, and covering employers in the same or related industry.
employment contract a legally binding, formal agreement between employer and employee
enterprise agreement a collective agreement made at a workplace level between an employer and a group of employees about terms and conditions of employment
environmental sustainability (ecological sustainability) to shape business operations around practices that consume resources today without compromising access to those resources for future generations
equal employment opportunity (EEO) refers to equitable policies and practices in recruitment, selection, training and promotion
equity as an external source of funds, refers to the finance raised by a company through inviting new owners
equity (in the workplace) the provision of equal opportunities for all employees to gain access to jobs, training and career paths
equity finance relates to the internal sources of finance in the business
established technology technology that has been developed and is widely used and simply accepted without question
ethical business practices those practices that are socially responsible, morally right, honourable and fair
ethical consumerism involves buying products that are not harmful to the environment, animals and society
expenses the costs incurred in the process of acquiring or manufacturing a good or service to sell and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service
explicit service the tangible aspect of the service being provided, such as the application of time, expertise, skill and effort
extended marketing mix the combination of people, processes and physical evidence with the four main elements of the marketing mix
external finance funds provided by sources outside the business, including banks, other financial institutions, government, suppliers or financial intermediaries
external recruitment involves filling job vacancies with people from outside the business
facilities the plant (factory or office) and machinery used in the operations processes
factoring the selling of accounts receivable for a discounted price to a finance or factoring company
Fair Trade movement an alternative method of international trade that promotes environmentalism, fair wages, alleviation of global poverty and a fair price for farmers and workers
fiduciary a person in a position of financial trust with respect to others' money
FIFO (first-in-first-out) a method of pricing inventory that assumes that the first goods purchased are also the first goods sold and therefore the cost of each unit sold is the first cost recorded.

financial budgets relate to financial data of a business and include the budgeted income statement, balance sheet and cash flows

financial controls the procedures, policies and means by which a business monitors and controls the allocation and usage of its resources

financial decision making requires relevant information to be identified, collected and analysed to determine an appropriate course of action

financial forecast the business's predictions about the future

financial management the planning and monitoring of a business's financial resources to enable the business to achieve its financial objectives

financial resources those resources in a business that have a monetary or money value

financial risk the possibility of financial loss to businesses

fixed costs costs that are not dependent on the level of operating activity in a business. Fixed costs do not change when the level of activity changes — they must be paid regardless of what happens in the business.

fixed position layout an operational arrangement in which employees and equipment come to the product

flexibility how quickly operations processes can adjust to changes in the market

foreign exchange market (**forex** or **fx**) a market that determines the price of one currency relative to another

foreign exchange rate the ratio of one currency to another; it tells how much a unit of one currency is worth in terms of another

forward exchange contract a contract to exchange one currency for another currency at an agreed exchange rate on a future date, usually after a period of 30, 90 or 180 days

frequency the average number of times someone is exposed to the message of an advertisement

fringe benefits tax (FBT) a tax employers must pay on certain benefits they provide to their employees or their employees' associates, such as a family member. It is based on the taxable value of the various fringe benefits provided.

Gantt chart a type of bar chart that shows both the scheduled and completed work over a period of time. It is often used in planning and tracking a project.

gearing the proportion of debt (external finance) and the proportion of equity (internal finance) that is used to finance the activities of a business. Gearing ratios determine the firm's solvency.

general skills include flexibility and versatility, social confidence, positive attitude, motivation, and the ability to work as a team and/or independently

generic brands products with no brand name at all

geographic segmentation the process of dividing the total market according to geographic locations

global branding the worldwide use of a name, term, symbol or logo to identify the seller's products

global economic outlook the projected changes to the level of economic growth throughout the world

global pricing how businesses coordinate their pricing policy across different countries

global sourcing a broad term that refers to businesses purchasing supplies or services without being constrained by location. In the supply chain management activity, global sourcing means buying or sourcing from wherever the suppliers are that best meet the sourcing requirements.

globalisation refers to the removal of barriers of trade between nations. Globalisation is characterised by an increasing integration between national economies and a high degree of transfer of capital (facilities and/or machinery), labour, intellectual capital and ideas, financial resources and technology.

grievance procedures formal procedures, generally written into an award or agreement, that state agreed processes to resolve disputes in the workplace

gross profit that part of a business's profit that represents operating income minus cost of goods sold

growth the ability of the business to increase its size in the longer term

hedging the process of minimising the risk of currency fluctuations

human resource audit a diagnostic tool used to evaluate HR policies and practices in order to identify problems and develop solutions in an attempt to rectify problems

human resource management the management of the total relationship between an employer and employee

implementation the process of putting marketing strategies into operation

implicit service is based on a feeling and is therefore intangible. The implicit aspects of a service are the psychological wellbeing — the feeling of being looked after — that comes with the provision of the service.

implied conditions the unspoken and unwritten terms of a contract
improvement refers to systematic reduction of inefficiencies and wastage, poor work processes and the elimination of any bottlenecks
in good faith means the parties meet with a willingness to reach an agreement
income statement a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.
independent contractor often known as a consultant or freelancer, independent contractors undertake work for others; however, they do not have the same legal status as an employee
indicators performance measures that are used to evaluate organisational or individual effectiveness
individual contract when an employer and an individual employee negotiate a contract covering pay and conditions
Individual Flexibility Agreements (IFA) allow an employer and an employee to come to an agreement that varies the modern award or enterprise agreement to address their individual circumstances
industrial dispute a disagreement over an issue or group of issues between an employer and its employees, which results in employees ceasing work
industrial market includes industries and businesses that purchase products to use in the production of other products or in their daily operations
inertia a psychological resistance to change
informal benchmarking includes any strategies such as networking through informal discussions with colleagues in other businesses, undertaking visits to other businesses, researching best practice online and attending conferences
information the knowledge gained from research, investigation and instruction, which results in an increase in understanding
inputs the resources used in the transformation (production) process
insourcing delegating a job to someone within the business, as opposed to someone outside the business
interdependence the mutual dependence that the key business functions have on one another
interest rates the cost of borrowing money
intermediate goods goods manufactured and used in further manufacturing or processing
intermediate market consists of wholesalers and retailers who purchase finished products and resell them to make a profit
internal finance funds generated from inside the business; for example, profits can be retained to finance expansion
internal recruitment involves filling job vacancies with people from within the business
interpretation making judgements and decisions using the data gathered from analysis
inventory or **stock** the amount of raw materials, work-in-progress and finished goods that a business has on hand at any particular point in time
inventory control a system that maintains quantities and varieties of products appropriate for the target market
job design the number, kind and variety of tasks that a worker is expected to carry out in the course of performing their job
job enlargement involves increasing the breadth of tasks in a job
job enrichment involves increasing the responsibilities of a staff member
job rotation involves moving staff from one task to another over a period of time in order to multiskill employees
job sharing when two people share the same job
judicial power refers to the power of courts to interpret and apply laws
just-in-time (JIT) an inventory management approach which ensures that the exact amount of material inputs will arrive only as they are needed in the operation process
kaizen Japanese for 'improvement'. It emphasises continuous improvement in all areas of a business, from the way the CEO manages to the way assembly line workers perform their jobs.
key performance indicators (KPIs) specific criteria used to measure the efficiency and effectiveness of the business's performance

label that part of the package that contains information
labelling the presentation of information on a product or its package
lead time the time it takes for an order to be filled from the moment it is made
leadership style refers to ways that managers communicate with their employees to inspire and motivate them to work together to achieve an organisation's goals
leading edge technology the technology that is the most advanced or innovative at any point in time
learning changes in an individual's behaviour caused by information and experiences
leasing the payment of money for the use of equipment that is owned by another party
letter of credit a document that a buyer can request from their bank that guarantees the payment of goods will be transferred to the seller. The letter of credit is issued by the importer's bank to the exporter promising to pay them a specified amount once certain conditions have been met.
liabilities items of debt owed to outside parties
LIFO (last-in-first-out) a method of pricing inventory that assumes that the last goods purchased are also the first goods sold and therefore the cost of each unit sold is the last cost recorded
liquidity the extent to which a business can meet its financial commitments in the short term (less than 12 months)
lockouts when employers close the entrance to a workplace and refuse admission to the workers
log of claims a list of demands made by workers (often through their union) against their employers. These demands cover specific wages and conditions. Employers may also serve a counter-log of claims on the union.
logistics a term broadly referring to distribution but includes transportation (including transportation modes), the use of storage, warehousing and distribution centres, materials handling and packaging
loss leader a product sold at or below cost price
loyalty program a rewards-based program offered by a business to customers who frequently make purchases
maintenance the process of managing the needs of staff for health and safety, industrial relations and legal responsibilities, including compensation and benefits, of all staff
manufacturer's brand or **national brand** a brand owned by a manufacturer
mark-up a predetermined amount (usually expressed as a percentage) that a business adds to the cost of a product to determine its basic price
market a group of individuals, organisations or both that: need or want products (goods or services), have the money (purchasing power) to purchase the product, are willing to spend their money to obtain the product, are socially and legally authorised to purchase the product
market-based pricing a method of setting prices according to the interaction between the levels of supply and demand — whatever the market is prepared to pay
market-customised pricing prices that are set according to local market conditions
market coverage refers to the number of outlets a firm chooses for its product
market research the process of systematically collecting, recording and analysing information concerning a specific marketing problem
market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristics
market share the business's share of the total industry sales for a particular product
marketing the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives (American Marketing Association). A more simplified definition is that marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.
marketing approach focuses on finding out what customers want — through market research — and then satisfying that need
marketing concept a business philosophy that states that all sections of the business are involved in satisfying a customer's needs and wants while achieving the business's goals
marketing data the information relevant to the defined marketing problem
marketing mix refers to the combination of the four elements of marketing, the four Ps — product, price, promotion and place — that make up the marketing strategy
marketing objectives the realistic and measurable goals to be achieved through the marketing plan

marketing plan a document that lists activities aimed at achieving particular marketing outcomes in relation to goods or services. The plan provides a template for future action aimed at reaching business goals, such as profit maximisation.

marketing ROI measures how much revenue a marketing campaign is generating compared to the cost of running that campaign

marketing strategies actions undertaken to achieve the business's marketing objectives through the marketing mix

mass customisation a process that allows a standard, mass-produced item to be personally modified to specific customer requirements

mass marketing approach a marketing approach that seeks a large range of customers

mass markets in mass markets, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers

materialism an individual's desire to constantly acquire possessions

materials the basic elements used in the production process, consisting of two types: raw materials and intermediate goods

mediation the confidential discussion of issues in a non-threatening environment, in the presence of a neutral, objective third party

mix flexibility the mix of products made, or services delivered, through the information process

modern award an industry or occupation-based award that covers all private sector employers and employees who perform work that falls within their scope. They replace all existing national system awards (except those applying to a single enterprise). They do not cover employees earning higher incomes.

monetary rewards those rewards reflected in pay or having financial value

monitoring the process of measuring actual performance against planned performance

mortgage a loan secured by the property of the borrower (business)

motive an individual's reason for doing something

negotiation a method of resolving disputes when discussions between the parties result in a compromise and a formal or informal agreement

net profit the difference between the gross profit and expenses

net working capital the difference between current assets and current liabilities. It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity

niche market a narrowly selected target market segment (also known as a concentrated or micro market)

noise any interference or distraction that affects any or all stages in the communication process

non-monetary rewards those rewards that do not have a financial value, such as social activities or retirement planning

non-store retailing retailing activity conducted away from the traditional store

offshore outsourcing involves taking the activities to a provider in another country

on-costs additional costs involved in hiring an employee, above the cost of their wages. These costs traditionally add around 25 per cent of the cost of the wage and include sick leave, holiday leave, leave loading, superannuation, retirement and redundancy payments, and other costs.

onshore outsourcing involves the use of domestic businesses as the outsourcing provider

operating budgets relate to the main activities of a business and may include budgets relating to sales, production, raw materials, direct labour, expenses and cost of goods sold

operations the business processes that involve transformation or, more generally, 'production'

opinion leader a person who influences others

option something that gives the buyer (option holder) the right, but not the obligation, to buy or sell foreign currency at some time in the future

orders decisions that require employees or employers to carry out a direction from the tribunal. They may be inserted in awards or agreements.

outputs the end result of the business efforts — the good or service that is provided or delivered to the customer

outsourcing contracting out business functions involving the use of third-party specialist businesses; for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.

overdraft when a bank allows a business or individual to overdraw their account up to an agreed limit and for a specified time, to help overcome a temporary cash shortfall

owners' equity the funds contributed by the owner(s); represents the net worth of the business

packaging the development of a container and the graphic design for a product

participation rate the percentage of a given group of individuals of working age who are employed or actively seeking work

payables sums of money owed by the business to other businesses from whom it has purchased goods and services. Payables are recorded as accounts payable.

payment in advance a payment method that allows the exporter to receive payment and then arrange for the goods to be sent

people the people element refers to the quality of interaction between the customer and those within the business who will deliver the service

perception the process through which people select, organise and interpret information to create meaning

performance appraisal a process of assessing the performance of an employee, generally against a set of criteria or standards

performance benchmarking involves comparing the performance levels of a process/activity with other businesses

performance management addresses both individual and business performance. Successful individual performance will often translate into the business's strategic objectives being met.

performance management (administrative) this model assesses the progress of the business in meeting its strategic goals and where necessary identifying the areas for improvement, such as establishing new goals or employee performance

performance management (developmental) this model improves individual performance through establishing objectives such as reaching sales targets that are consistent with achieving the organisation's goals

performance objectives goals that relate to particular aspects of the transformation processes

personal selling the activities of a sales representative directed to a customer in an attempt to make a sale

personality the collection of all the behaviours and characteristics that make up an individual

physical distribution all those activities concerned with the efficient movement of the products from the producer to the customer

physical evidence everything that the customer sees when interacting with a business

pickets protests that take place outside the workplace, generally associated with a strike. Unionists stop the delivery of goods and try to stop the entry of non-union labour into the workplace.

place or **distribution** activities that make the products available to customers when and where they want to purchase them

placement involves locating the employee in a position that best utilises the skills of the individual to meet the needs of the business

podcasting the distribution of digital audio or video files over the internet

precautionary principle requires that, where environmental impacts are uncertain, a business undertakes actions that are most likely to cause the least environmental impact

prestige or **premium pricing** a pricing strategy where a high price is charged to give the product an aura of quality and status

price the amount of money a customer is prepared to offer in exchange for a product

price discrimination the setting of different prices for a product in separate markets

price leader a major business in an industry whose pricing decisions heavily influence the pricing decisions of its competitors

price penetration when a business charges the lowest price possible for a product or service so as to achieve a large market share

price points (or **price lining**) selling products only at certain predetermined prices

price skimming when a business charges the highest possible price for the product during the introduction stage of its life cycle

primary data the facts and figures collected from original sources for the purpose of the specific research problem

primary market deals with the new issue of debt instruments by the borrower of funds

primary target market the market segment at which most of the marketing resources are directed

private or **house brand** a brand that is owned by a retailer or wholesaler

process layout the arrangement of machines so that the machines and equipment are grouped together by the function (or process) they perform

process production deals with high-variety, low-volume production

processes refers to the flow of activities that a business will follow in its delivery of a service

product deletion the elimination of some lines of products

product differentiation distinguishing products (goods or services) in some way from those of competitors

product layout layout in which the equipment arrangement relates to the sequence of tasks performed in manufacturing a product

product life cycle the stages a product passes through: introduction, growth, maturity and decline

product mix the total range of products offered by a business

product placement the inclusion of advertising in entertainment

product production (mass production) production that is characterised by the manufacturing of a high volume of constant quality goods

product utility the usefulness and value that a product has from the consumer's point of view

product/service differentiation the process of developing and promoting differences between the business's products or services and those of its competitors

product/service positioning the technique in which marketers try to create an image or identity for a product compared with the image of competing products

production approach a marketing approach that focuses on the production of goods and services

products goods or services that can be offered in an exchange for the purpose of satisfying a need or want

profit centres those aspects of a business that directly derive revenue and profits

profit maximisation occurs when there is maximum difference between the total revenue coming into the business and total costs being paid out

profitability the excess of revenue or income over expenses or costs

profitability management involves the control of both the business's costs and its revenue

project budgets relate to capital expenditure, and research and development

project production deals with layout requirements for large-scale, bulky activities such as the construction of bridges, ships, aircraft or buildings

promotion the methods used by a business to inform, persuade and remind a target market about its products

promotion mix the various promotion methods a business uses in its promotional campaign. Methods include:

- advertising
- personal selling and relationship marketing
- sales promotions
- publicity and public relations.

psychographic segmentation the process of dividing the total market according to personality characteristics, motives, opinions, socioeconomic group and lifestyles

psychological factors influences within an individual that affect his or her buying behaviour

public relations (PR) those activities aimed at creating and maintaining favourable relations between a business and its customers

publicity any free news story about a business's products

puffery exaggerated claims used for promotional purposes, that no reasonable person would take as factual

quality a specific reference to how well designed, well made and functional goods are, and the degree of competence with which services are organised and delivered

quality assurance (QA) involves the use of a system to ensure that set standards are achieved in production

quality control (QC) involves the use of inspections at various points in the production process to check for problems and defects

quality management those processes that a business undertakes to ensure consistency, reliability, safety and fitness of purpose of product

quality of conformance the focus on how well the product meets the standard of a prescribed design with certain specifications

raw materials the essential substances in their unprocessed state

reach the number of people exposed to the message of an advertisement

receivables sums of money due to a business from customers to whom it has supplied goods or services. Receivables are recorded as accounts receivable.

record systems the mechanisms employed by a business to ensure that data are recorded and the information provided is accurate, reliable, efficient and accessible

recruitment the process of finding and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies at the right cost

redundancy occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition

reference or **peer group** a group of people with whom a person closely identifies, adopting their attitudes, values and beliefs

relationship marketing the development of long-term and cost-effective relationships with individual customers

remuneration the financial (e.g. pay) and non-financial (e.g. career security) benefits that employees receive in return for their work effort

resource market consists of those individuals or groups that are engaged in all forms of primary production, including mining, agriculture, forestry and fishing

retrenchment when a business dismisses an employee because there is not enough work to justify paying him or her

robotics used in engineering and specialised areas of research, as well as on assembly lines where a programmable machine capable of doing several different tasks is required

sale and lease-back the process of selling an owned asset to a lessor and then leasing the asset back through fixed payments for a specified period of time

sales analysis the comparing of actual sales with forecast sales to determine the effectiveness of the marketing strategy

sales approach a marketing approach that emphasises selling because of increased competition

sales promotion the use of activities or materials as direct inducements to customers

scheduling the length of time activities take within the operations process

secondary data information that has already been collected by some other person or organisation

secondary market deals with the purchase and sale of existing securities

secondary target market a smaller and less important market segment than the primary target market

segmentation variable a characteristic of an individual or group that is used by marketing managers to divide a total market into segments

self-image how a person views himself or herself

self-regulation a system by which a business or industry controls its own activities rather than being publicly regulated by an outside organisation such as the government

separation the process of employees leaving voluntarily or through dismissal or retrenchment processes

sequencing the order in which activities in the operations process occur

skills audit a formal process used to determine the present level of skilling and any skill shortfalls that need to be made up either through recruitment or training

social class or **socioeconomic status** a person's relative rank in society, based on his or her education, income or occupation

social justice in the workplace involves businesses being responsible or behaving in a fair and ethical manner towards their employees, customers and the broader community

social media advertising (SMA) a form of online advertising using social media platforms such as Facebook, YouTube and Twitter to deliver targeted commercial messages to potential customers
societal marketing approach a marketing approach that emphasises social responsibilities, as well as the importance of maintaining and improving the wellbeing of customers and society
sociocultural influences forces exerted by other people and groups that affect an individual's buying behaviour
solvency the extent to which the business can meet its financial commitments in the longer term (more than 12 months)
sourcing the purchasing of inputs for the transformation process
specific skills highly specialised skills that are required for some jobs within science, technology and engineering sectors
speed refers the time it takes for the production and the operations process to respond to changes in market demand
spot exchange rate the value of one currency in another currency on a particular day
staff turnover the loss of employees who leave the business for a variety of reasons
stakeholder any individual or group that has a common interest in or is affected by the actions of an organisation
standardisation refers to the making of products that are homogeneous or identical
standardised approach a global marketing strategy that assumes the way the product is used and the needs it satisfies are the same the world over
standardised goods those that are mass produced, usually on an assembly line. Standardised goods are uniform in quality and meet a predetermined level of quality. These are generally produced with a production focus.
standardised pricing the practice of charging customers the same price for a product anywhere in the world
statistical interpretation analysis the process of focusing on the data that represents average, typical or deviations from typical patterns
statutes laws made by federal and state parliaments; for example, laws relating to employment conditions
storage involves finding a secure place to hold stock until it is required
strategic refers to long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business
strategic plan a plan that encompasses the strategies that a business will use to achieve its long-term goals
strategy long-term, broad aims affecting all key business areas; that is, the strategic role of each key business function involves the managers of each function contributing to the strategic direction or strategic plan of the business
strikes situations in which workers withdraw their labour
structural change a change in the nature and pattern of production of goods and services within an economy. This includes a significant growth in the level of services in an economy compared to other sectors.
subsidiary a company that is owned by another company (referred to as the parent) and it is often located in another country
sugging 'selling under the guise of a survey'; a sales technique disguised as market research
superannuation a scheme set up by the federal government, which requires all employers to make a financial contribution to a fund that will provide benefits to an employee when they retire
supply the quantity of a product businesses are willing to offer for sale at a particular price
supply chain management (SCM) involves integrating and managing the flow of supplies throughout the inputs, transformation processes (throughput and value adding) and outputs in order to best meet the needs of customers
survey the gathering of data by asking or interviewing people
SWOT analysis involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment
target market a group of present and potential customers to which a business intends to sell its product
tariff a tax on an imported product
task design involves classifying job activities in ways that make it easy for an employee to successfully perform and complete the task

technology the design, construction and/or application of innovative devices, methods and machinery in operations processes

telecommute to 'commute', or travel to work, electronically. This means that home or another location becomes the worksite and work is delivered via email or the internet.

total product concept the tangible and intangible benefits (attributes) a product possesses

trade union an organisation formed by employees in an industry, trade or occupation to represent them in efforts to improve wages and working conditions of their members

trademark signifies that the brand name or symbol is registered and the business has exclusive right of use

training to develop skills, knowledge and attitudes that lead to superior work performance

transformation the conversion of inputs (resources) into outputs (goods and services)

transformed resources those inputs that are changed or converted in the operations process

transforming resources those inputs that carry out the transformation process

transnational corporations (TNCs) any businesses that have production facilities in two or more countries and that operate on a worldwide scale

triple bottom line refers to the financial profitability, social impact and the environmental impact of a business

unconscionable conduct any practice by a business that is not reasonable and often illegal

unfair dismissal occurs where an employee is dismissed by their employer and they believe the action is harsh, unreasonable or unjust

unsecured note a loan from investors for a set period of time. Unsecured notes are not secured against the business's assets.

value for money the desire to obtain the best quality, features and performance for a given price of a product

variable costs costs that vary in direct relationship to the levels of operating activity or production in a business. Such costs include labour costs and costs of energy.

volume refers to how much of a product is made

warehousing the use of warehouses for the storage, protection and, later, distribution of stock

warranty a promise made by a business that they will correct any defects in the goods they produce or services they deliver

word-of-mouth communication when people influence each other during conversations

workers' compensation a range of benefits to an employee suffering from an injury or disease related to their work. It is also provided to families of injured employees when the injury/disease was caused by, or related to, their work.

working capital the funds available for the short-term financial commitments of a business

working capital management determining the best mix of current assets and current liabilities needed to achieve the objectives of the business

workstations the desk areas required by office workers, usually fitted with access to a computer monitor, keyboard, telephone, mouse and mouse pad and storage, and close access to a printer and scanner

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