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Business Studies

An Introduction to the
St. Gallen Management Model

4th edition

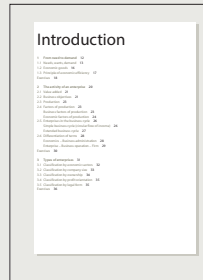
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Structure of this book

Introduction

These chapters provide an easy entry into the topic of business administration. They deal with needs and services provided by enterprises as well as the different types of enterprises, independent of the St.Gallen Management Model.



Body

These chapters provide a comprehensive explanation of business administration in terms of the St.Gallen Management Model, which will be explained in five parts (A–E). For better clarity, the parts are associated with different colors.



Toolbox

This section provides tools for the identification of problems as well as the determination, assessment and implementation of solutions.



Index

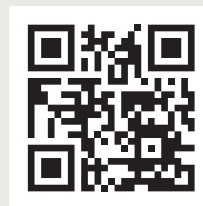
Key terms and other important technical words are listed alongside the number for the book page where they are defined.



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Working with this book

Title page

The title page lists the chapters to come in this section of the book and shows the part of the model to which they relate.

Contents in detail

Lists all sections of the chapter.

[illegible]

Contents overview

serves as a navigation aid within the chapter.

Header

Central questions to be answered in the course of the chapter.

Key terms used in business administration.

Anchoring in the model locates the chapter graphically and descriptively in the St. Gallen Management Model.

Examples provide for a problem-oriented anchoring of the theory.

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
Chapter contents

Theory illustrated by examples.

Exercises

At the end of each chapter is a set of exercises. They serve as a way to apply and deepen knowledge and have a medium to high level of difficulty. Simpler exercises are posed by the central questions at the beginning of each chapter.



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Figure 1 The relationship between the quality of a product and the quantity of a product. The Y-axis represents Quality and the X-axis represents Quantity. The graph shows three curves: Total cost curve (TC), Marginal cost curve (MC), and Average cost curve (AC). The MC curve is U-shaped and intersects the AC curve at its minimum point. The TC curve is S-shaped and intersects the MC curve at its minimum point. The AC curve is U-shaped. The graph is divided into three regions: High quality, Medium quality, and Low quality. The High quality region is characterized by high quality and low quantity. The Medium quality region is characterized by medium quality and medium quantity. The Low quality region is characterized by low quality and high quantity. The graph shows that as quality increases, the quantity of the product decreases, and the total cost increases. The marginal cost curve is the steepest, followed by the average cost curve, and then the total cost curve. The total cost curve is the flattest, followed by the average cost curve, and then the marginal cost curve. The graph illustrates the trade-off between quality and quantity, and the role of marginal and average cost curves in determining the optimal quality and quantity of a product.

Elements of the content pages

Highlights

Basic knowledge and precise definitions appear in bold in the chapter color.

1 Word annotations

The annotations explain unfamiliar or foreign words.

18.4 Dynamic methods of investment appraisal

These static methods are indeed handy, but they do not consider differences in the timing of revenue and expenditure. The dynamic methods are somewhat more sophisticated in this respect as they take into account the differences in the timing of cash flows. They are based on the concept of present value.

The value that future cash has today is the present value (PV).

The present value is obtained by **discounting** the future amount of money with an interest rate on capital that is the expression of an alternatively achievable rate of return (opportunity costs). This interest rate is based on the idea that money available today could also be set aside to earn interest. The higher the general level of interest rates, the more relevant this approach. In practice, the interest rate is calculated from the interest rate on risk-free government bonds (in Switzerland, the yield on long-term government bonds) plus a risk premium, depending on the risk of the investment (e.g., 2.5% yield on federal bonds + 5% risk premium = interest rate of 7.5%).

To calculate this value, three variables must be known:

- the future amount of money (C_t) in t years
- the year (t) in which money is received and
- the interest rate (i).

The formula for calculating the present value (C_{0p}) is as follows:

¹ Discounting: By discounting an amount at time zero, you can calculate the amount that you would have to invest today at a given interest rate in order to possess a particular asset at a later date.

Key terms

Important technical terms in business administration appear in bold on their first occurrence or where they are best explained. These also appear at the beginning of each chapter and in the index.

Economic conditions

The **economic cycle** is the wavering, undulating course of economic development, a rise and fall of all the important economic factors, such as production, employment, interest rates, and prices. In times of economic recovery (rebound), the demand for consumer goods¹ and services increases, followed by capital goods².³ Production then runs at capacity, leading to an increase in employment (boom, growth). When production capacity is overloaded, the price level increases, lowering demand for consumer goods and services, as well as capital goods (downturn), which can lead to a **recession**⁴ or even a depression (crisis). During such phases, as orders drop off, enterprises often have to lay off workers and put off investments.

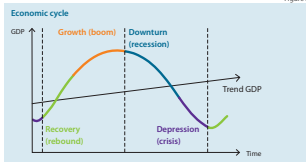
¹ Consumer goods: goods that are used in households

² Capital goods: goods that are used in businesses

³ p.161 Economic goods capital goods

⁴ Recession: A recession occurs when the rate of growth in two consecutive quarters compared to the previous quarter - is negative.

→ Exercise 5



The national bank can, through monetary policy (loosening or tightening of the money supply), and the state through economic measures (stimulus, tax cuts), partially smooth out these fluctuations.

Example Airline - Crisis

The corona virus triggered a global crisis that also shook the airlines. In the crisis, the state is asked for help and the banks for liquidity.

Gross domestic product

The **gross domestic product (GDP)** is the totality of all value added¹ created in an economy in one year.

→ p.21 Value added

It is used to compensate the factors of production² (e.g., wages for work or interest on capital). In an economic boom the gross domestic product increases.

→ p.23 Factors of production

Figures

These help visualize a topic, sum it up and therefore provide better and more thorough understanding of the material.

Examples

All examples have a grey background. Real or fictitious companies are used to help illustrate the theory. Fictitious companies are denoted with quotation marks.

→ Cross-reference arrows

Arrows indicate a corresponding exercise at the end of the chapter or a close reference to another chapter.

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Solutions

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Digital content

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also director and president of the board.

a What arguments justify such a form of organization?

b What dangers could one person carrying out several responsibilities at the same time present in terms of ensuring effective corporate governance?

6 Search the Internet for the annual report of a company of your choice in order to learn about its corporate governance.

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D10 Distribution policy

→ p. 195 Table of contents

Central questions

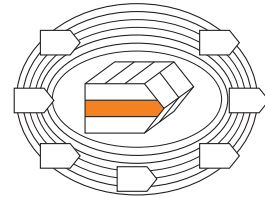
- a) What is meant by distribution policy?
- b) Which distribution providers can be distinguished?
- c) What is a sales channel?
- d) What are the advantages and disadvantages of direct and indirect sales?
- e) What is franchising?
- f) What is meant by retail vs. wholesale outlets?
- g) What are the main functions of physical distribution?
- h) What questions are raised in the distribution of services?

Key terms

Distribution policy, distribution provider, intermediaries, retail, wholesale, sales channel, direct sales, indirect sales, e-commerce, franchising, physical distribution, magical triangle of transport modes

Anchoring in the model

In the context of business processes, products and services are created. They are then distributed through various channels to customers. Within the marketing mix, the distribution policy is responsible for the organization of distribution.



Example JUST International AG*

JUST International AG describes itself as an Appenzeller global company guided by Swiss tradition but thinking and acting internationally. JUST has been developing and producing high-quality plant and herb products for health, beauty and well-being for 90 years and distributes them in around 35 countries. In order to be able to supply the large number of markets efficiently and sustainably, JUST has two production sites, one in Switzerland and one in Argentina. In Switzerland more than 150 permanent employees work at the production site and around 120 more work in the field. Worldwide, more than 90,000 sales advisors personally bring JUST products to the customer's home. Direct sales at JUST have many forms and are based on the personal interaction between the JUST consultant and the end customer. Whether at a product party, door-to-door, via telephone and internet or at markets and trade fairs. What are the advantages and disadvantages of this direct form of sales? What other possibilities are there to successfully sell a product? To what extent does the choice of sales opportunity depend on the nature and properties of the product?

* Further information at:
www.just.ch

Figure 179



10.1 Functions of distribution policy

Every business aims to sell as many of the products or services it produces as possible. That is because, if these do not reach the customer, no revenue will be generated. Additionally, the products must also be stored, a further cost to the enterprise in terms of warehouse operations and capital commitment[→]. For this reason, a good distribution policy is essential for an enterprise.

→ p.230 Capital commitment and warehouse operations

The distribution policy includes all the decisions and actions that affect a product or service on its path from producer to end user.

The main goal of the distribution policy is the availability of products. The right product needs to be available to the customer at the right place, at the right time, in the right quantity, and in the desired quality.[→] The distribution costs (i.e., storage and transport costs) should be kept as low as possible. At the same time, environmental considerations play an increasingly important role in distribution policy. From these objectives, the three main functions of distribution policy can be derived, as well as relevant questions:

→ p.228 Materials management

Table 101

Main functions	Questions
Determining the distribution providers	Who will distribute the products?
Determining the sales channels	How should the products reach the customer?
Determining the physical distribution	Should transportation be handled in-house or by a third party? Which mode of transport should be chosen?

10.2 Distribution providers

In deciding on distribution providers, the question arises of whether the enterprise should perform distribution functions itself or use outside distribution organizations.

The distribution provider of an enterprise is responsible for the transfer of products or services from the manufacturer to the end user.

In-house distribution bodies

Using in-house distribution, the collection and processing of orders is handled by the sales department of an enterprise. The essential in-house distribution bodies are members of management, salespeople, and field service personnel, as well as sales offices:

Table 102

Distribution body	Explanation	Examples
Members of management	With this type of sales, members of management maintain personal contact with major customers and present the latest products or services to them.	Textile and clothing industry, where members of management themselves present their latest collections
Salespeople, field service personnel	These distribution bodies are responsible for their respective enterprise and have to comply with its rules and obligations. Such salespeople visit customers regularly and usually receive a fixed wage and sometimes a commission based on their sales.	Insurance, JUST sales consultant
Sales office	This form is chosen mainly by large enterprises, which establish and manage their own branch offices. Sales offices are, for example, responsible for customer consultations, sales agreements, and delivery from the enterprise's own warehouses.	Fashion industry, service sector

Example Direct sales by the JUST sales consultant

Figure 180

Through personal contact with customers, JUST International AG would like to present their products better and make them more tangible. This is done through four different types of direct sales: In direct sales with individual advice, JUST sales consultants visit customers at home. The party system is at the heart of direct sales. The JUST products are presented at a party in a private environment. The cheerful and relaxed atmosphere at parties contributes to a better experience of the JUST brand. When it is not possible to visit a JUST sales consultant, customers can conveniently order the products via the call center via telephone or via the Internet in the online shop. The products are also sold in numerous markets and trade fairs.



External distribution providers

Many manufacturers, however, do not sell their products directly to the end buyer. For this reason, manufacturers and end users are connected to each other through a number of partners. These external distribution providers are called **intermediaries**. The most important intermediaries are sales agents, brokers, and retail and wholesale outlets:

Table 103

Distributor	Explanation	Example
Sales agent	Sales agents are independent businesspeople who can freely pursue their own actions and work their own hours. The products do not become the property of the agents. Thus they bear no risks associated with the goods, such as spoilage or a customer's inability to pay. The remuneration of such a distribution provider is usually based mostly on sales.	Stationery industry
Broker	Brokers seek to match up buyers and sellers of certain products, earning a commission when transactions are concluded.	Land sales, insurance and banking
Retail	Retailers buy goods and sell them to the final customer, usually without additional processing.	Supermarket, jewelers
Wholesale	Wholesalers purchase goods in large quantities and usually sell them on to resellers (i.e., not the end user).	Cash and carry

In practice, retail and wholesale outlets represent the most important intermediaries and will be expanded upon further below.

Retail is the sum of the activities of selling goods and services directly to consumers for their personal, non-commercial use.

The retail sector is very dynamic and adaptable. The structure of the retail trade can be explained according to the criteria assortment [→], price, and sales location. → p.291 Sales program

Table 104

Assortment	Price	Sales location
<ul style="list-style-type: none"> – Specialist shops (e.g., sporting-goods store) – Boutique shops (e.g., wine shop) – Big-box stores (e.g., MediaMarkt) 	<ul style="list-style-type: none"> – Discount stores (e.g., Lidl) – Gourmet food store (e.g., Delicatessa at Globus) 	<ul style="list-style-type: none"> – Mail order (e.g., Cornelia) – Showroom (so-called stationary retail)

In the case of wholesale, as opposed to retail, larger quantities are sold and the targeted distribution area is larger. To this end, advertising, the sales atmosphere in the stores and, in some cases, the location of a wholesaler are of lesser importance. There are countless forms of wholesale. The most important are, briefly, as follows:

- *Classic consumer goods dealers*: These sell primarily to the retail market and offer comprehensive service.
- *Production supply dealers*: The customers of these dealers are production companies and commercial customers. They sell products that are not intended for resale but for further use in production.
- *Pick-up wholesalers (cash and carry)*: The customers come to the sales location and purchase cheap products in large quantities, paying on the spot. The cash-and-carry wholesaler mostly limits its offerings to a certain range of goods.
- *Shipping wholesalers*: These usually present their articles to customers through catalogs. The products ordered are then sent to the customer.

Wholesale is the sum of the activities of selling goods and services to resellers, processors, and consumers at large.

10.3 Sales channels

In determining the sales channel, the question arises of whether distribution should be performed through direct or indirect sales channels. In business practice, various mixed forms of direct and indirect systems exist. Franchising represents a special hybrid form.

In choosing a suitable sales channel, the goal is to approach and attract as many customers as possible. This choice is a long-term decision that affects, for example, the availability of products, the product image, and product prices.

A sales channel (also, distribution channel) includes all steps that are responsible for providing a product or service to the customer.

The design of the sales channel takes on very different forms in reality. The sales channel will depend on the following influencing factors:

- *Product-related*: shelf life of a product or its need for explanation
- *Customer-related*: geographical distribution or shopping habits
- *Competition-related*: sales channels of the competition or number of competitors
- *Business-related*: available capital or the marketing plan →

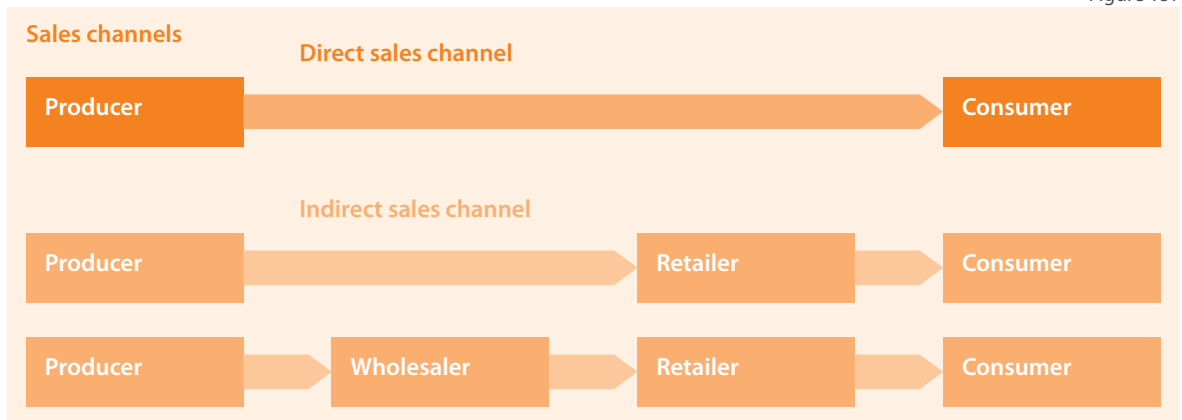
→ p.273 Marketing plan

Direct and indirect sales

The most important question in terms of the sales channel is whether intermediaries should be positioned between the enterprise and end users, or if the enterprise should sell its products directly. There is also a correlation between the choice of distribution providers and the decision about appropriate sales channels. If an intermediary is used for the sale of goods and services (external distributor), distribution will, by definition, take place through an indirect sales channel.

Direct sales are characterized by the producer functioning as a direct vendor to the consumer. However, indirect sales involve one or more intermediaries (dealers).

Figure 181



A direct sales channel is recommended for the following product types:

Table 105

Product types	Explanation	Example
Perishable products	These require a fast transfer. The quality of these products can suffer from delay or frequent reloading.	Fish, seafood
Non-standard products	Especially when order-based production is used, a direct route to the customer is recommended.	Special machines
Valuable products	Such products usually lead to high storage costs and often require after-sales service →, such as regular maintenance.	Central heating
New, innovative, and complex products	The manufacturer of such products has the necessary know-how.	Installation of a new EDP ¹ system

→ p.353 After-sales management

¹ EDP: Electronic Data Processing

An indirect sales channel is recommended in the following situations:

Table 106

Situation	Explanation	Example
Many customers	The greater the number of customers, the greater the producer's sales effort would be.	Perfume
Frequently required	The more frequently a product is in demand by each customer, the greater the producer's sales effort would be.	Food
Large sales area	The further customers are from the producers, the greater their shipping expenses would be.	Automobile

Example JUST – Direct sales

JUST prioritizes competent, personal, and customer-oriented consultation, which is why it adheres to the principle of direct sales. However, the company constantly adapts the basic idea of direct sales to changing social and technological conditions. With the spread of the Internet, online sales were greatly expanded. This means that customers can learn about products at any time and then order directly from the producer.

When the purchasing process takes place virtually instead of via data transmission, this is called **e-commerce**¹. In this type of distribution, all steps, from ordering to payment, are conducted via the Internet. Compared to the traditional sales channels, e-commerce has the advantage of very low transaction costs[→] because, apart from warehousing, the seller no longer requires a physical space for sales.

¹ E-commerce: Internet retail, virtual marketplace

→ p.125 Transaction costs

Example Orell Füssli Thalia AG – E-commerce

At books.ch, the e-commerce platform of Orell Füssli Thalia AG, the sale of books takes place online via an Internet portal. A customer does not need to visit a bookstore but can easily shop for a book from home, have it delivered or downloaded to an e-book reader, and pay e.g. by credit card.

→ Exercises 1 and 2

Franchising

In the business world, a variety of mixed forms of direct and indirect sales channels exist. A special mixed form is represented by franchising[→], which has proved to be successful at, for example, McDonald's, Benetton, and The Body Shop.

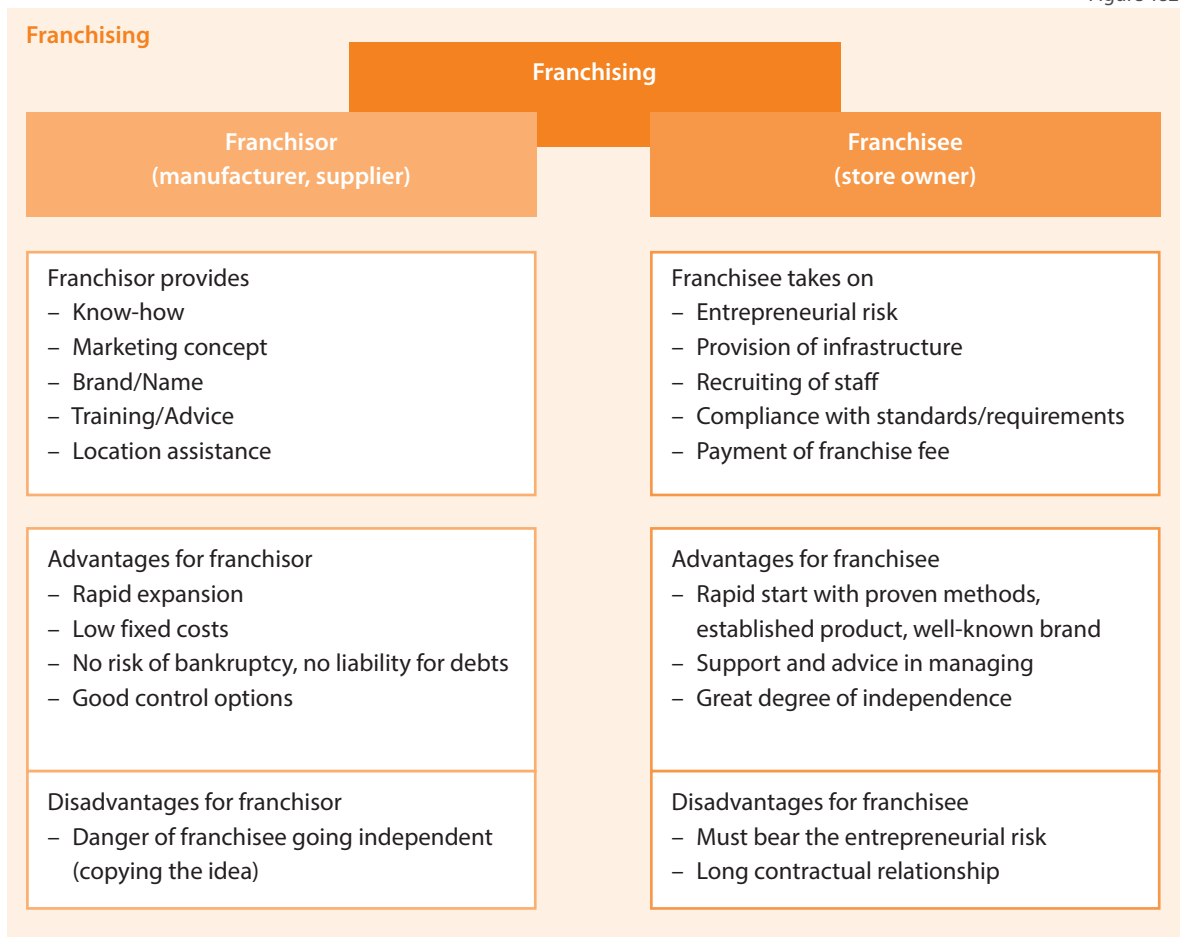
→ p.136 Franchising

Franchising is defined as a contractual collaboration between two legally independent companies where the franchisee pays the franchisor a fee and is, in exchange, granted the right to sell products and services under a particular brand.

In this way, franchising is a mixed form of direct and indirect sales, because it is not apparent to the customer that the franchisee and the franchisor are different companies. From the customer's point of view, the enterprise has therefore chosen a direct sales channel. The franchisor does not have direct contact with customers, but serves only the franchisees, which handle purchases from the customers. From this perspective, it is an indirect sales channel.

The franchisee is provided with a business method that has already been successfully tested, along with the necessary know-how. Thus, it can operate directly, without the risk involved in building a business, while at the same time maintaining a degree of independence. The franchisor receives a single payment when the contract is signed and usually periodic payments of around 5–7% of sales; it can also achieve widespread sales of the product with limited financial means. Finally, it can take advantage of the franchisee's local expertise.

Figure 182



→ Exercise 3

10.4 Physical distribution

Physical distribution deals with the actual transportation of the goods produced. The decisions made in this area are independent of the strategic decisions about the distribution provider and sales channel.

Make or buy

An enterprise must basically consider whether it will perform the role of physical distribution itself or use a transport company and outsource this activity. In physical distribution, the enterprise is facing a kind of “make or buy decision→.” In the same way the question arises at a manufacturing company of whether to make the parts of a product itself (make) or procure them externally (buy), an enterprise must decide whether to handle the physical distribution itself or whether a third party should be used. A pizza delivery firm, for example, maintains its own fleet of vehicles and takes over the physical distribution of the ordered pizzas. In other cases, freight-forwarding companies are preferred. The transport of goods represents the core competence of a freight-forwarding or shipping company. It therefore has the necessary know-how and takes care, for example, of customs formalities involved in the cross-border transport of goods. The decision regarding the appropriate mode of transport is then left to the shipping company.

→ p.122 Make or buy

Table 107

Advantages	Disadvantages
Maintaining a private fleet of vehicles is associated with high investment and maintenance costs. Furthermore, the invested capital is tied up and cannot be used simultaneously for other purposes (opportunity costs).	On the other hand, an enterprise loses a portion of its independence through the use of a freight-forwarding company.

Transportation

The transport of goods can be handled by various modes of transportation (truck, train, ship, plane).

For the transport of goods, a combination of various transport modes is possible. Intermodal transport, so-called piggyback service, for example, combines road and rail traffic. In the near future, drones could also be used for distribution. They would be particularly suitable for lighter goods and for use in less-densely populated areas.

Decision criteria

The modes of transport used in physical distribution depend on various factors. The following criteria influence the decision regarding the appropriate modes of transport:

Table 108

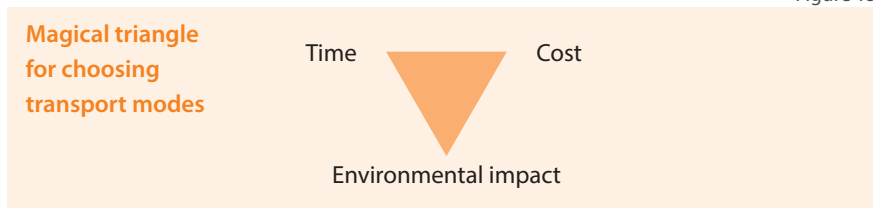
Criteria	Explanation
Time	Which transport mode guarantees the timely delivery of goods?
Economy	Which transport mode is cheapest?
Ecology	Which transport mode has the lowest environmental impact→?

→ p.265 Transport intensity

The triangle below is called “magical” because all the objectives cannot be achieved simultaneously to the same degree. By opting for one mode of transport, the goods cannot be transported quickly as well as cheaply and in a way that is eco-friendly. For example, transport by ship is, compared to air transport, more environmentally friendly and cost-effective, but it is certainly slower. Those responsible for the distribution policy must decide which objective is most important in a given situation.

→ Exercises 4, 5 and 6

Figure 183



10.5 Distribution systems for services

The decision for an appropriate distribution system does not only play a role with products. In the case of services, it is particularly important that potential partners and locations are selected in such a way that the population can be adequately supplied with the respective service despite their geographical location. For example, hospitals must be geographically distributed so that basic medical care for the entire population is ensured. For less-serious medical issues or in remote locations, a telephone consultation is also possible as an alternative to visiting a doctor. New information technology makes it possible for some service sectors to provide certain services without direct, face-to-face contact. These include banking services through ATMs and e-banking.

Exercises – D10 Distribution policy

1

What is the relationship between the choice of distribution providers, sales channels, and intermediaries?

2

Factory outlets, such as in Landquart, represent a form of direct sales.

- a Use information from www.landquartfashionoutlet.ch to describe its sales channel.
- b Name the advantages and disadvantages of factory outlets.

3

McDonald's is a famous example of a franchise business. Search the Internet for information to answer the following questions.

- a What does McDonald's, as a franchisor, offer to franchisees?
- b What requirements does McDonald's have of its franchisees?
- c Discuss: Would you apply to become a McDonald's franchisee? What are reasons for and against this decision?

4

What are the main functions of physical distribution and what decisions need to be made in this area?

5

You run a shipping company and are responsible for handling the physical distribution of goods to your customers. Which modes of transport would you choose in the situations below. In making your decision, consider the criteria of time, cost, and environmental impact, and justify your answer.

- a Transport of goods that must arrive as soon as possible in Hamburg from St. Gallen.
- b Transport of heavy goods from Rotterdam to Genoa.
- c Transport of fruit and vegetables from Wil to Winterthur.

6

Compare prices for clothes by mail order to stationary retail (showroom), using the following criteria: time, cost, environment, selection, and advice. Cite the advantages and disadvantages from the perspective of a customer-oriented enterprise.

Figure 184



Figure 185

