

# Rise and fall of standard pricing



## **The Rise and Fall of Standard Pricing and Its Effect on Everyday Operations For European and American Firms**

The overall purpose of this paper and study is to investigate cost or lean accounting within the operations management realm and how its unpredictable rise and fall allow organisations to continuously learn and utilize knowledge management as a core value. It was also important to use a larger organisation that has history of outstanding operations and customer centered focus upon services. This investigation will require an in-depth study of work processes, communication and leadership with regard to knowledge management as a value within the team construct while looking at how this reflects leaning accounting principles. What tools are available and what kind of evolution is Nestle undergoing in order to remain competitive in a changing economy? How does this change knowledge management and communication company wide? What this study argues is that accounting practices are changing due to the evolving business plan. This is a movement toward modern accounting and it is important to see the relationships between costing accounting, its fluctuations and how they impact the health of the organisation as a whole with regard to productivity and job satisfaction.

How an organisation applies methods of costing into its framework for accounting of expenses and its direct rise and fall over the time period of the product life cycle, directly influences the production, operation, distribution and employee retention of the global company. In fact changes in accounting practices have led to many tried and true business models to no longer exist. Costing and its rise and fall can have a direct relationship with success and competitive advantage in the market place. However the purpose of this <https://assignbuster.com/rise-and-fall-of-standard-pricing/>

study is to explore and reflect upon how accounting practices change operations management and the supply chain management model as a tool of managers and team members alike. Really it is how accounting practices have changed business practices because of new legislation focusing on global companies in Europe and the United States. Accounting costs, expenses and losses reflects the health of the organisation and with change comes confusion. This study argues that with such changes comes a lack of defining the company's value within the market but also the value it has for its employees, as they become active participants and investors.

#### GENERAL OVERVIEW

How corporate accounting is handled is changing worldwide. How each expense is accounted for within an organisation's financial sheets has been evolving. Such a proposal for change has received much commentary from not only the financial community and corporate America but also key members of Congress, European union leaders and the public. Such a response results from the uncertainty that such change will benefit businesses and economic growth. It is feared that such change will have the opposite effect and cause world leaders to lose its competitive edge in the global market. Still this has not stopped the fuel of the fire as the American Financial Accounting Standards Board (also referred to as FASB) has struggled for an answer to such a dilemma. The urgency for a solution has only been stressed recently in light of such debacles like Enron and Tyco. It is believed that companies do need to account honestly for expenses but at what price to its employees, the public and the economy? Part of the issue with current legislation to change the practice of accounting for employee

<https://assignbuster.com/rise-and-fall-of-standard-pricing/>

stock options is that there is no real way to value their worth. This creates an unsettling feeling among investors and employees struggling to understand this benefit.

## ACCOUNTING OVERVIEW

What this truly means for any corporation functioning globally or even locally is that effective cost accounting because a volatile issue for management to consider. One could argue that such rise and fall of how costing/pricing pays a part in the entire operation has a negative effect upon how the company's valuation is seen on the open market. Costing at every step of the product life cycle plays a huge part in how this valuation is decided from inventory at the shop floor level, to everyday operations management, to an employee's value with the company and their net worth personally. Changes within the global economy in the recent years the disappearance of tried and true business models leaves many with a poor taste in their mouths because one must understand how efficiency, affordability and effective leadership come into play. Effective pricing or costing of routine operations and corporate behaviours must be tracked and studied in order to carve the fat. This study aims to look at exactly what the rise and fall of pricing or costing means to a global organisation conducting business on many levels. For the purpose of proving the argument that such changes in accounting practice has a negative effect on the organisation, one will look at examples from the shop floor to the employee's estimated value with the company in the form of job satisfaction. Accounting for such expensing and pricing correctly is what makes the organisation strong but also accurate in valuation. With this

in mind, traditional business models like Wal-Mart and Nestle are discussed because these are globally operating corporations.

Debates about whether or not the fair value of the employee and the company stock options should be expensed on the income statement continue to rage among industry representatives, politicians, and pundits. Expense recognition of stock options can have significant impacts on net income and earnings per share, so this is a debate worth having. But many of those who analyze companies consider operating cash flow a better performance metric than income. One reason is that operating cash flow is thought to be free from the infection that makes income grossly weakened. In the case of employee worth and stock values, however, there is proof that this assumption is flawed. Option exercise affects operating cash flows in ways that analysts need to understand. Repurchasing shares to fund option exercise also results in financing cash outflows. The net cash flow impacts of options are often negative, but can be quite volatile from year to year.

## LITERATURE REVIEW

### STANDARD PRICING AS ACCOUNTING PRACTICE

It can be difficult to assess why a product has a certain cost or price to the consumer. How is it that companies arrive at certain amount for a product or service? What are the factors that play into this amount and do they change over time while in the market? Mish defines clearly, price as being “ the value or worth; the quality of one thing that is exchanged or demanded in barter or sale for another” (2004, p. 985). A mistake that happens to many companies is they allow the market to manage the price of the product and

<https://assignbuster.com/rise-and-fall-of-standard-pricing/>

avoid strategic management of pricing in general. What is usually done according to Nagle is “ they list the prices based on their own needs and then adjust transaction prices to based on what customers say they are willing to pay. Only a few companies question why someone is willing to pay no more than a particular amount or how that willingness could be changed” (2002, p. 1). In order to be strategic in pricing, a company must confident and understand that “ pricing involves managing customers’ expectations to induce them to pay for the value they receive” (Nagle 2002, p. 1).

Fortunately, when it comes to financial products, many customers remain in the dark about product and services. Sometimes a service oriented company such as the Bank of England can take advantage of such undulation but as more information becomes available due to the Internet, it is becoming increasingly more difficult for a company to set the pace this way. More than not, more companies especially financial ones that rely on customer relationships, allow for a value-based price structure that is contingent on the customer paying when value is delivered. This type of pricing system relies heavily on segmentation of the demographic when it comes to offering promotions and incentives to buster customer loyalty. Much of this applies to financial type products that are well defined for the consumer either through education or these products are a must in life like the credit or loan product. Keeping this in mind, many financial products consist of high quality products and add-ons that when offered by one company allows that company to diversify and establish the price. The table here below aids in illustrating this point.

Table 1: Pricing Strategies

<i>P/Q</i>	<i>Higher Price</i>	<i>Lower Price</i>
High	Premium	Good Value
Quality	Strategy	Strategy
Lower	Overcharging	Economy
Quality	Strategy	Strategy

(Anderson & Bailey 1998, p. 2)

It is also important for a company to keep in mind demand for the product or service. This is why diversification and globalization are quickly becoming elements of strategy as companies look for new ways to target consumers and enter new areas where their original product has a new life cycle. This is a matter of economics but important for understanding marketing strategy with regards to cost switching or price switching. “ The greater the price elasticity, the closer the company can price products to similar competitive products and vice versa” (Allen 2002). In an industry like the mortgage industry where homeownership is more prevalent in Western nations, elasticity is high and therefore, it is fair to remain competitive with other companies. Also a company like Nestle can bet that charging less may lead to more food products created as customers find they get more service for less money. In this respect elasticity can work either way. It really depends

<https://assignbuster.com/rise-and-fall-of-standard-pricing/>

on degree of risk one company is willing to take. Still it remains to be found if such a tactic even works when it comes to customer loyalty, as this will be explored in greater detail later. However, it remains to be seen if price loyalty does exist. It seems “ the key to effectively competing for loyalty is ensuring the quality of the customer experience, not the quantity of customer rewards or discount prices” (Compton 2005, p. 1). However, the price needs to be adjusted for what the customer expects. It can be a cycle that changing continuously depending on the product or service.

Carmona, and et al (2004), writes of the origin of activity based costing method of accounting or ABC that came into vogue in Europe during the 1920s. What ABC does specifically as Carmona, and et al (2004) speak of Vollmers’s work as:

Deployed significant efforts to account for distribution and marketing costs, which ‘ tend to be ignored today.’ This first event is then taken as record of the origin (both in terms of time and space), from which the new practice mainly spread both temporally and spatially. (p. 36)

This is the start of a movement toward the double entry system and this saw delay and many weaknesses because it did not present a clear, complete picture of accounting. Its weaknesses were found in inefficiencies with charges and discharges. As a result, early double-entry systems were seen as unreliable and not useful to big business. It would not be until later that advanced book keeping procedures would take into account advanced operating processes in production. Carmona, and et al (2004) found these systems although not perfected were used in England and the Colonies as



early as 1760 (p. 37). It seems this was the trend as no real streamlined, conforming system would be adopted until modern business practices came into place in the United States.

Move to a global arena and model of production purposes and a more refined system is needed because a lot more is at stake. Global business is all about the details. It became common practice more investment applied, the more generally accepted accounting practices became as a diffusion of new technology. Accounting practices became more generally accepted behaviours as businesses became bigger and more prominent in communities across the world. Practices are implemented as Abu-Raddaha, and et al (2000) surmises the following:

The information provided by accounting should facilitate international trade and capital flows, not hamper them. It should inform, not just report. More importantly the information demands of both domestic and international financing and other commercial relationships, have to be satisfied. (p. 19).

Everything must remain in balance or presented as a well-oiled machine.

How does an organisation get to this point of transformation with its accounting practices? Modern accounting asks for more participation and optimisation from the start to finish by the corporate accountant. The actions of the corporate accountants must change as the movement toward lean functioning continues to take place. It should not be a painful process but one of creativity, flexibility and growth. There is a concern that lean accounting requires one to turn off creativity and be boxed into one function or thought process. This will be explored later as a post-modern viewpoint of <https://assignbuster.com/rise-and-fall-of-standard-pricing/>

business where each person has a function within the total quality management or TQM perspective. Modern business may use this as a framework but the modern business model has evolved beyond this fixed view. The truth of the matter is that modern accounting practices could not be further from this view of being boxed in but rather goes beyond breaking the box and creating a different mindset where thinking is seen differently than before. Accounting is seen differently as not having finite possibilities but infinite reasoning. Traditional methods are flawed as proposed by Van Der Merwe and Thomson (2007), “ the direct costing approach doesn’t absorb any overhead or even fixed costs...resource consumption accounting or RCA makes no arbitrary assignments at all” (p. 29). A lean, effective method allows for a more detailed account of capacity costs and a basic approach to data collection. Modern times call modern values and thought processes with regard to business seamless behaviour across the production floor. The lean method maintains a “ one-touch flow system” (Van Der Merwe & Thomson 2007, p. 29) for information diffusion across the life cycle. This one-touch flow system can be integrated with a supply chain easily and reflects this value added element as a method for better, honest accounting.

## OPERATIONS MANAGEMENT

A most important factor for facilities management to recognize is the use of Total Quality Management (TQM) or a variation of TQM. TQM according to David Steingard is “ a set of techniques and procedures used to reduce or eliminate variation from the production process or service delivery system in order to improve efficiency” (Steingard 2002, p. 2). TQM fits with the facilities management way of doing things as many of their functions require

repetition or constant monitoring of daily, weekly and monthly items.

Because this is a modernist concept and the modernist movement believed in certainty and static methods of looking at the world, there is not much room for the uncertainty that change creates in today's workplace using strictly TQM. Therefore either change in this environment must be controlled change or a variation of TQM must be used for the process to work and involve new technologies. Otherwise, TQM alone invents a work environment reminiscent of Franz Lang's *Metropolis* and dehumanizes the employee. A variation TQM can be used in facilities management to aid defining team member responsibilities as it sees the whole team as a " machine creates a system of interlocking parts each with clearly defined use, centralized authority and high degrees of worker discipline culminating with the goal of routinised, efficient and predictable system performance" (Steingard 2002, p. 2). Each team member plays a role in the functioning of the machine. Still much like today's business environment where change is constant, this system requires continued adjustment, modification improvement of function. TQM as way of defining a work process cannot operate entirely in today's global market because it succeeds at the expense of innovation and the growth of the employee. It also does not leave room to incorporate change and new ways of improving functions. Still a memory of pure TQM feeds the " modernist machine of consumer capitalism which encourages over-consumption, planned obsolescence, ecological damage and depletion of natural resources" (Steingard 2002, p. 4). This memory has also burdened management as the obsession for perfection, control, consistency, productivity and efficiency increases over time. In today's facilities team, there must be a healthy medium to not only use past methods for increased

productivity and efficiency but also to include modern tools and equipment to make the job easier.

In order to remain competitive, technology cannot be ignored, the systems it provides must be implemented in order for logistics to remain seamless and keep up with demand and customer expectation. For instance failure to embrace logistics and technology results in inventory costing a company more money to store than it is worth. McCulloch writes, “ Right now sitting around the globe is a bunch of inventory (worth an estimated) United States \$1 trillion—United States \$1 trillion of boxes of stuff is just sitting around a warehouse” (‘ Warning: Don’t Snub Logistics’, p. 1). This has the potential to represent about 60 percent of the average company’s working capital. This is capital in limbo that is not maximizing its investment potential.

A sign of successful shop floor operations is reliance on very little warehousing. In other words, warehousing is measured as the amount of days per month a product sits in the warehouse and if logistics is implemented effectively, this number will decrease and stabilize. The retail average storage of inventory is 26 days of investment not being utilized, profit being lost and daily expenses being incurred in an endless holding pattern. In order to reduce the amount of days inventory sits means companies must create tighter relationships with suppliers via the web or perfect a system of communication between resources to cut out warehousing all together. Instead of inventory remaining stored because of wireless communication and data collection, the product can go straight from the supply source to the retailer’s shelves via a distribution centre that acts much like mail sorting centre. This can work because technology

enables a retailer to send data immediately to the supplier of products that are moving off the shelves with a click of a button. From this electronic message, the supplier knows what the retailer needs, what products are popular, how much and sends them instantly to the retailer's distribution centre. In organisations the size of Nestle or Wal-Mart, logistics strategy requires much forethought and planning, as there are many branches and divisions that are involved in the process. The idea is to reduce expenses and increase value to the organisation by making the company more productive and efficient. This needs to be done as seamlessly as possible to continue brand loyalty and customer relations while maintaining market share and competitive advantage. In many ways, implementation of this strategy creates a delicate balance.

In order to have better Business to Business or B2B relationships, one must understand the connection. Robert Thierauf and Hoctor (2003) explain, " B2B is about connecting shared businesses and information processes of the extended trading networks, planning, shipping and logistics, inventory management and customer retention to name a few" (Thierauf & Hoctor, p. 181). In other words, an optimized planning process can save millions dollars and allow a multination corporation to carry out its objective and gain market share. This means applying advanced technology such as i2 used by Dell Computers and typical ERP vendors. In today's act of doing business, B2B exchanges are based on supply chain management or SCM technologies (Thierauf & Hoctor, 2003, p. 182). This will mean considerable investment in such technology but the benefit of market share will prove it to be a valued investment over the long-run (Burn & Hachney 2002; Scerbo 1999).

Running these centres effectively certainly poses a challenge of management. Manufacturers must develop new skills and confront channel conflicts with dealers, distributors and independent operators. Leaders in these positions must have an understanding of managing the conflicts in these channels. But well-managed distribution centres would more than justify the risks, as it would save the organisation a significant amount of overhead.

With operating expenses as the main cost, it is possible to make the distribution venture essentially self-funding. Facilities can be rented on short-term leases and surrendered if the location isn't successful within a year or two. The cost of goods and labour can be managed as volume grows. Companies should remember that a manufacturer's original warranty work usually accounts for about half of the labour expenses and for as much as 20 percent of the total value of services rendered, but these costs are typically charged back to the business unit rather than borne by the company's distribution. In markets poorly served by local dealers or other distributors, for instance, a centre should gear itself to its company's end users or consumers by choosing a high-traffic retail site. Profits at these locations are generated largely through the sale of accessories and optional services to walk-in or mail order customers; outlets thus need appealing product displays or sales presentations.

Different kinds of retail distribution centres pursue different economic models. Although gross margins on sales to end-users are higher, orders tend to be smaller. Locations that focus on distributors can achieve scale faster and be just as profitable. The largely similar economics of service

centres vary only according to which customer segment is best served at each location. Companies run their own centres and tie management bonuses to profit and growth goals at each site. Either way, some support functions, such as marketing, human resources and information and financial systems, are best managed at the corporate level.

Warehouses and distributions centres are caught in a squeeze between customer service demands and cost drivers. The challenge for most organisations is create a network that can deliver on customer demands while keeping costs down. This is the number challenge in supply chain management. Supply chain management presents a huge undertaking when it comes to overhead operating costs. Many of the tools have come down in price because usability has gotten easier. As a result, more and more companies are adopting a supply chain management philosophy for distribution and are re-evaluating its effectiveness every two years as opposed to before at every five years. Management members are interested to see if the efficiency of the centre matches its service level provided.

Research has found a direct relationship between the number of distribution points, transportation costs and customer service targets. The network and its design are driven by improvements so that the cost of transportation can be offset. This may include reviewing an organisation's transportation arrangements. Loading patterns should also be examined to find ways to cube out containers and trailers (Trunick, p. 1). What possibilities can be used to have a cost-effective outcome for the distribution centre? Does this mean consolidating shipments or a move to parcel and less than truckload shipments? Can shipments be combined to make greater use of truck cargo

space? Can the organisation hire rail or air as better shipping alternatives to using company trucks over longer distances? In addition to examining loading can the routes used by the trucks be adjusted to be add to cost-efficiency? An organisation would benefit using their state's transportation management system or a department of transportation, DOT to map out distribution volumes and patterns. This would help in providing dynamic routing options that can be flexible to change distribution needs in the network. This can benefit the fleet by reducing fuel supply needs and help control costs and usage. These efficiencies would result because the routes would decrease in mileage and also wear/tear on the vehicles and insurance costs.

Efficiency inside the four walls of the distribution centre can also be improved. Relatively speaking the size of the average distribution centre has grown from 300, 000 square feet to one million square feet (Trunick, p. 2). This is simply due to operating space needed to move inventory from point a to point b. But the real reason the distribution centre is larger today is mainly because organisations have seen the need to put all operations under one roof. By putting multiple facilities into one larger distribution centre improves the time it takes to transport inventory. Still the larger centre is made possible because of improved transportation systems but also implementation new technologies that not only enhance a brick and mortar store but also a virtual one. Plus, the organisation has the manpower under one roof. The company only rents one building and keeps the inventory in one place rather than moving it from warehouse to warehouse. This allows the company to provide better service to the consumer. Because of these



factors, information systems are critical to the success of the larger distribution centre. Data has the need to travel from one area to another and that is why more and more companies are investing in radio frequency terminals both handheld and vehicle mounted.

Investment of these RFID systems is not inexpensive and many retailers such Wal-Mart and Target are looking for ways to enrich the present technology and systems without implementing a whole new infrastructure into the walls of the centre. By being able to enhance present systems proves to be cost effective because not only is an upgrade cheaper but also it is easier to train employees to run. It is a company's ability to effectively handle investment of new technologies that allows the centre to run better. Still as Trunick writes, the concern is not found in hardware but in data. " Databases have traditionally been structured to feed a number of different systems, but that's not a long term architectural solution" (p. 2). Part of the problem a distribution centre faces with data storage is being able to provide the data in real time and allowing the data to remain clean and not crowd. As a result many companies are searching for better solutions than using RFID in supply chain management. It has not proven to be productive in the distribution centre setting not like 8 percent in the warehouse setting (Trunick, p. 2).

One new technology that was introduced to the Nestle facilities management team in 2006 was the use of a computerized tracking system for client user orders. This system was implemented to better track the status of job orders among the team members. This system acted to alert a team member of potential deadlines and current job load status. It also allowed management

to better track individual and team progress. This resulted in a monthly recognition program to signify when quotas had been met or when a team member received a client user compliment. This system also had the capability to record the negative such as being late to a service call or failing to complete monitoring of weekly items for inspection. The system would then e-mail the team member and the direct supervisor if such conduct occurred (Facilities Training Group 2007, p. 11). This system replaced the old process of “ tracking” client user orders that consisted of logging each order into a spiral notebook. With the advent of the company’s intranet site, management hoped to improve communication between the facilities team and the client user by offering an electronic request system. This would reduce the amount of time the facilities team spent fielding phone called requested and allow for multi-tasking of various jobs.

What management had hoped the system implementation would result in, did not happen mainly due to team member lack of communication and resistance to change due to a pre-existing TQM elements within the old process of handling client user orders. Management had hoped as the Business Open Learning Archive details, “ automation would exploit available technology to speed up operations, make them more reliable and to reduce unit costs and their risks and costs. This would bring flexibility to the system already in practice” (Operations Technology 2005, p. 1). This type of new technology or just-in-time or JIT technology requires careful handling and extensive training. What facilities management team leaders had not prepared for was the team member response. Many of them despite being competent, responsible employees did not have knowledge of computer

systems. Many of the team members had been with the company over twenty years and had been hired to the division. Many of these types, fall into the category of being older but also having a specific specialization in which they were in the field most of the time (Facilities Training Group 2007, p. 24) not requiring any other extensive skills. Another factor management had not anticipated was a considerable language barrier as many team members who had worked together for years, continued working in their native tongue of Spanish. A final aspect of the mixed response for the team had more to do with timing than anything. Management provided a three-day training session and then allowed two weeks for the new system to be adopted. The transitional period was too short and was met with much resistance from many members of the team. Many did not accept the change or completely understand the new system. Many did not check their email or use the tracking component. Finally, despite company wide advertisement of the new online request feature, most client users did not use it and continued to phone in requests. This resulted in not a decrease in time spent on the phone but due to the new system's lack transition and rejection by some of the team, the group received three times as many calls in one week (Facilities Training Group 2007, p. 33). The team had to hire a temporary employee to aid in taking calls while team leaders provided on the job training and supervised walk-through of the new process. The period of six weeks it took the team to get back up to speed resulted in not only miscommunications among team members but also time lost to better serving the client users. As a result, many of the circulation systems did not receive their weekly maintenance and this negatively affected the climate control performance for the building's seventh floor northwest corner

(Facilities Training Group 2007, p. 39). With time the team members adjusted to the new technology with few still relying on the hand-written method. Still the process of introducing the system was not handled effectively and resulted in a period of adjustment where many processes met with negative results.

## OPERATIONS LIFE CYCLE

Wal-Mart became a textbook example of managing rapid growth without losing sight of a company's basic values. In Wal-Mart's case, the basic value was, and is, customer service. Still it was Wal-Mart's ability to focus on multiple values that lends to its current success. As technologies changed, American social needs became more immediate d