CHAPTER 2

Influences on operations management

OVERVIEW

2.1 Introduction
2.2 Main influences on operations management
2.3 Corporate social responsibility

2.1 Introduction

As we have already covered, operations management is a crucial key business function. As such, successful management of operations processes is essential to business success. To successfully manage the operations function, managers must deal with a range of external influences that impact on operations. These influences are shown in figure 2.1.

Influences on operations have a dual effect on businesses. First, they can cause the business to undergo change and to continually adjust to external factors. Responsiveness to change is a constant issue for business. A second effect is the threat and the opportunity that these influences represent to operations processes.

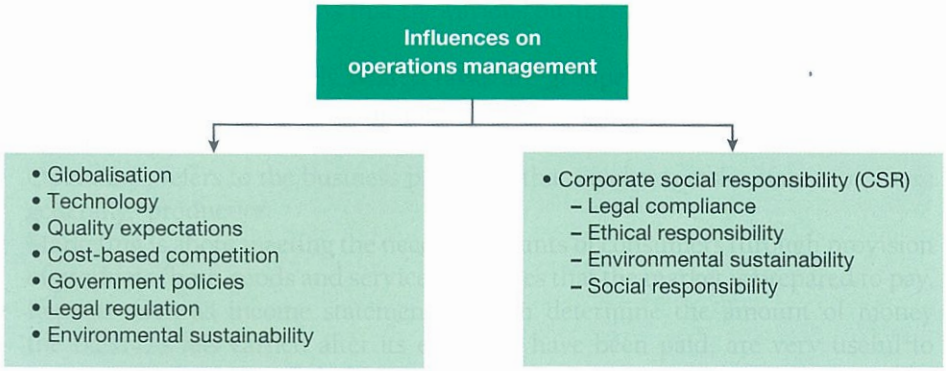


FIGURE 2.1 Influences on operations management

2.2 Main influences on operations management

In this section, we will explore the seven main influences on operations management shown in the left-hand side of figure 2.1. The effect of corporate social responsibility (CSR) will be examined in the latter part of the chapter.

2.2.1 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

BizWORD

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.*

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 and operations management

Globalisation is a very significant influence on operations management. 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. Figures 2.2 and 2.3 indicate how operations can be organised around the needs of a global market.

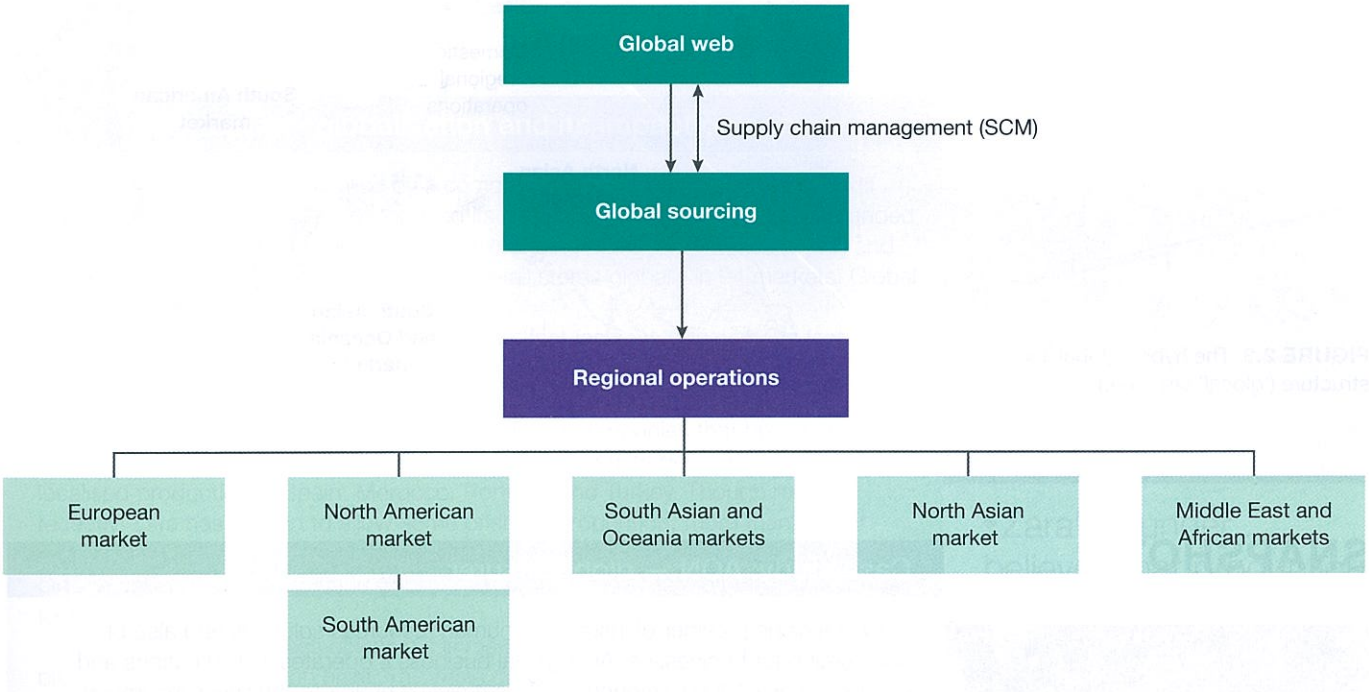


FIGURE 2.2 The organisation of operations to meet the needs of a global market based on the global web: a network of production sites located around the world

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 massive economies of scale advantages. This is evident with businesses like Apple, which has product designed in the United States, but manufactured in China for a global market.

The production of services on a global scale within sectors such as financial services, travel and tourism services, software development and telecommunications also has significant implications on 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. As stated in chapter 1, as far as possible, large-scale service-based businesses will seek to standardise services. See the following Snapshot for an example of standardised services in a tertiary industry.

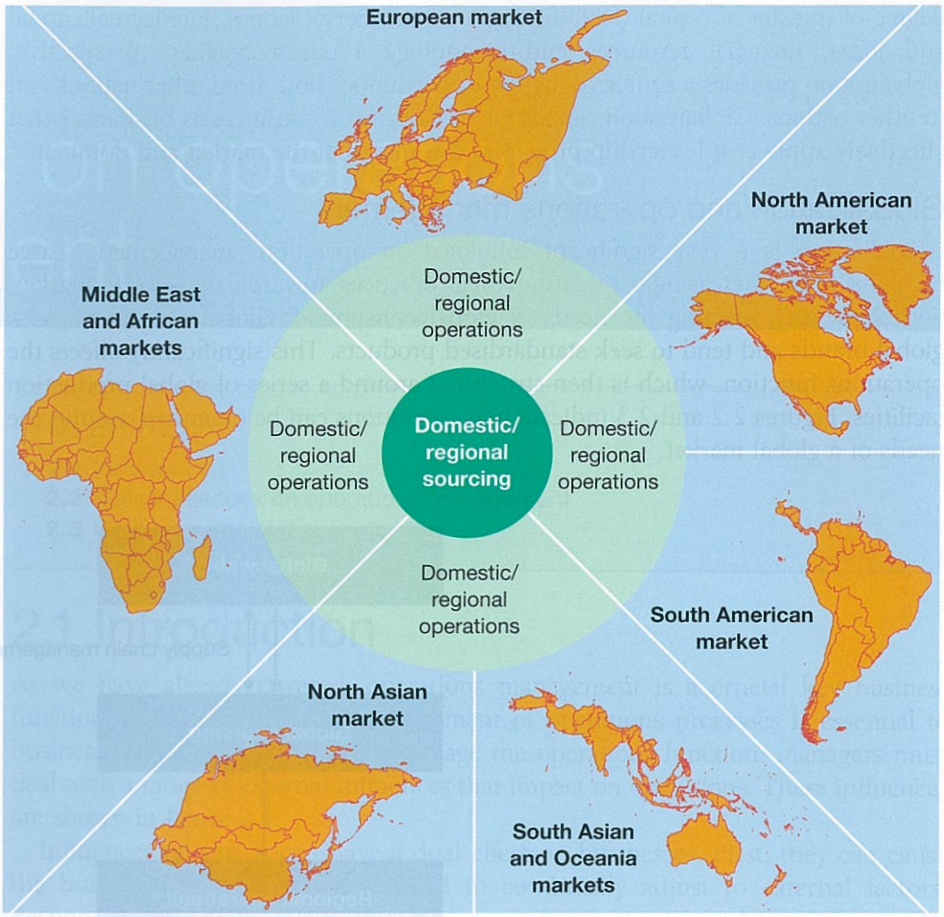
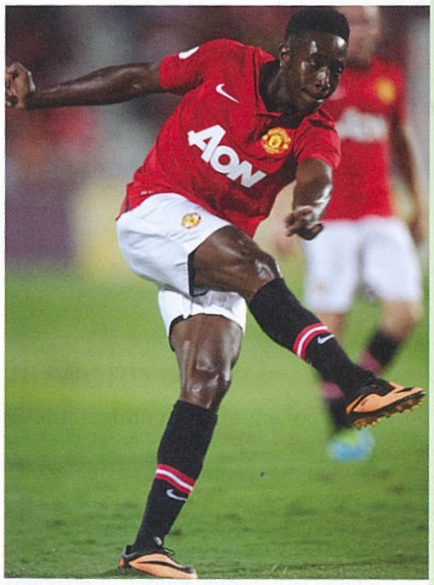


FIGURE 2.3 The hybrid global–local structure ('glocal' structure)

SNAPSHOT



'high internal standards and focus on quality . . .'

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 nations and employs over 72 000 personnel. 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 QUESTIONS

1. **What** does AON do?
2. **Explain** how standardisation can improve overall quality standards.
3. **Outline** the features that make AON's operations reliable.

Supply chain management (SCM) and the global web

A key aspect of operations management is that of supply chain management. Globalisation has had a significant effect on the operations function with respect to supply chain management. The **supply chain** refers to the range of suppliers a business has and the nature of its relationship with those suppliers. A business needs a very predictable and reliable supply chain that is highly responsive to changes in demand as experienced by the business. Sourcing, an essential aspect of supply chain management, is an operations strategy that requires finding the suppliers needed so that production processes can flow smoothly.

For large global businesses the integration of the range of suppliers creates a network sometimes called the **global web**. Global web refers to the network of suppliers a business has, chosen on the basis of lowest overall cost, lowest risk and maximum certainty in quality and timing of supplies. In supply chain management, the global web strategy is one in which the business aims to minimise costs across the range of its suppliers. Thus, a business will opt for a location with appropriate proximity to its suppliers. If a high proportion of suppliers are in one particular region, this may decide the location of the main operations processes.

BizWORD

Supply chain *refers to the range of suppliers a business has and the nature of its relationship with those suppliers.*

BizWORD

Global web *refers to the network of suppliers a business has chosen on the basis of lowest overall cost, lowest risk and maximum certainty in quality and timing of supplies.*

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). By 2017, Zara had over 2200 retail stores globally in 94 markets. Global sales were just under €11.6 billion in 2016.

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 94 markets where it retails.

Some of the source nations for fabrics include: Vietnam, Bangladesh, Morocco, China and Thailand. The company has about 1200 different suppliers and manages them through a highly centralised control of production. Sourcing globally reduces costs, as does keeping stock moving quickly rather than storing it.

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.

SNAPSHOT



'Zara's founder . . . believes that production proximity and quick logistics are two contributors to its global success.'

SNAPSHOT QUESTIONS

1. **Explain** the benefit of globalisation to Zara's scale of production.
2. **What** is a benefit of making garments close to where they are sold?
3. **How** does well-designed logistics help Zara to minimise costs?

SUMMARY

- 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.
- Globalisation affects organisational design and the supply chain.
- For large global businesses, the integration of the range of suppliers creates a network, sometimes called the global web.
- The supply chain is also affected by whether the nation is innovative or whether it is a follower.

EXERCISE 2.1 REVISION

1 **List** eight key influences on operations management.
2 **What** does the term 'globalisation' mean?
3 **State** two features of globalisation.
4 **Recall** two opportunities that globalisation represents to the operations function in business.
5 **How** does globalisation affect the operations function of a business?
6 **Explain** the importance of supply chain management (SCM) to the operations function.
7 **How** does globalisation act as both an opportunity and a threat to businesses?
8 **Define** the term 'global web'.

EXERCISE 2.1 EXTENSION

1 Wendy's Windows must decide whether to establish a factory to make a component or to contract the manufacturing to an independent supplier. **Propose** the advantages and disadvantages of each option. **Recommend** which of the two options is more efficient. **Justify** your selection.

2.2.2 Technology

BizWORD

Technology *may be defined as the design, construction and/or application of innovative devices, methods and machinery upon operations processes.*

Technology plays a very important role in the application of the operations function of business. **Technology** may be defined as the design, construction and/or application of innovative devices, methods and machinery upon operations processes. Most people are very familiar with a wide range of technologies, both personal and household. Smartphones, laptop computers, desktop computers, gaming consoles, security devices, and so on are well understood and widely available forms of technology that most people interact with. Such technologies enable people to communicate more easily and enable improved business processes. In this way, technology can be seen to be both a range of devices as well as a range of enabling *processes* and applications.

Technology and operations management

Technologies can be applied to, and integrated with, the range of processes that characterise the operations function in business. At an administrative level, technologies such as those in table 2.1 assist with organisation, planning, decision making and control of operations processes. At a processing level, technologies are used in manufacturing, logistics and distribution, quality management, all aspects of inventory management, supply chain management and sourcing, as outlined in the Snapshot on Zazzle.

TABLE 2.1 An overview of some of the technologies used in operations processes

Technologies used in the administration of operations	Technologies used in the range of operations processes
• Use of planning technologies: materials requirement planning (MRP), Gantt charts, critical path analysis (CPA) and other scheduling and sequencing tools • Use of office technologies such as computers (desktop and laptop), scanners, facsimile machines, integrated telephone systems, mobile phones • Use of software such as wordprocessing, graphics packages, spreadsheeting programs, graphing programs, multimedia programs and desktop publishing programs	• The use of large machines in manufacturing plants such as those typical of assembly line production • The use of robotics in highly sophisticated production processes requiring great precision • Use of computer-aided design (CAD), computer-aided manufacture (CAM) and computer integrated manufacturing (CIM) technologies • Rapid manufacturing (RM) and tooling technologies

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.

SNAPSHOT



'. . . the model relies on insightful business partnerships and innovative design strategies . . .'

SNAPSHOT QUESTIONS

1. **When** did Zazzle set up, and **what** does it do?
2. **Provide** 12 examples of customised products Zazzle offers to the market.
3. **Describe** the importance of customisation to the market.
4. **What** impact does licensing from trademarked brands have on Zazzle?

2.2.3 Quality expectations

One of the key goals of the operations function of business is quality. The expectation of quality is a significant influence on the operations function of business. The International Standards Organization (ISO) defines quality as being 'the totality of features and characteristics of products (goods) and services that bears its ability to satisfy stated or implied needs'. However, for our purposes, **quality** may be understood to be a specific reference to how well designed, made and functional goods are, and the overall 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 (goods and services) and their personal level of satisfaction with their experience of the product will indicate whether the quality has met with expectations or not.

BizWORD

Quality *may be understood to be a specific reference to how well designed, made and functional goods are, and the degree of competence with which services are organised and delivered.*

SNAPSHOT



'Quality products arise when a business has quality processes.'

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 blend of 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.

SNAPSHOT QUESTIONS

1. Briefly **recount** the basis of Tiffany & Co.'s reputation.
2. **How** does Tiffany & Co. meet customer expectations?

Quality expectations and operations management

Within the operations management 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 management may be summarised into several key things that customers look for in products — be they goods or services. These quality expectations for goods and services are listed and distinguished in figure 2.4.

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Syllabus area 1
Topic 2
Concept 1

Influences on operations management
Summary screen and practice questions

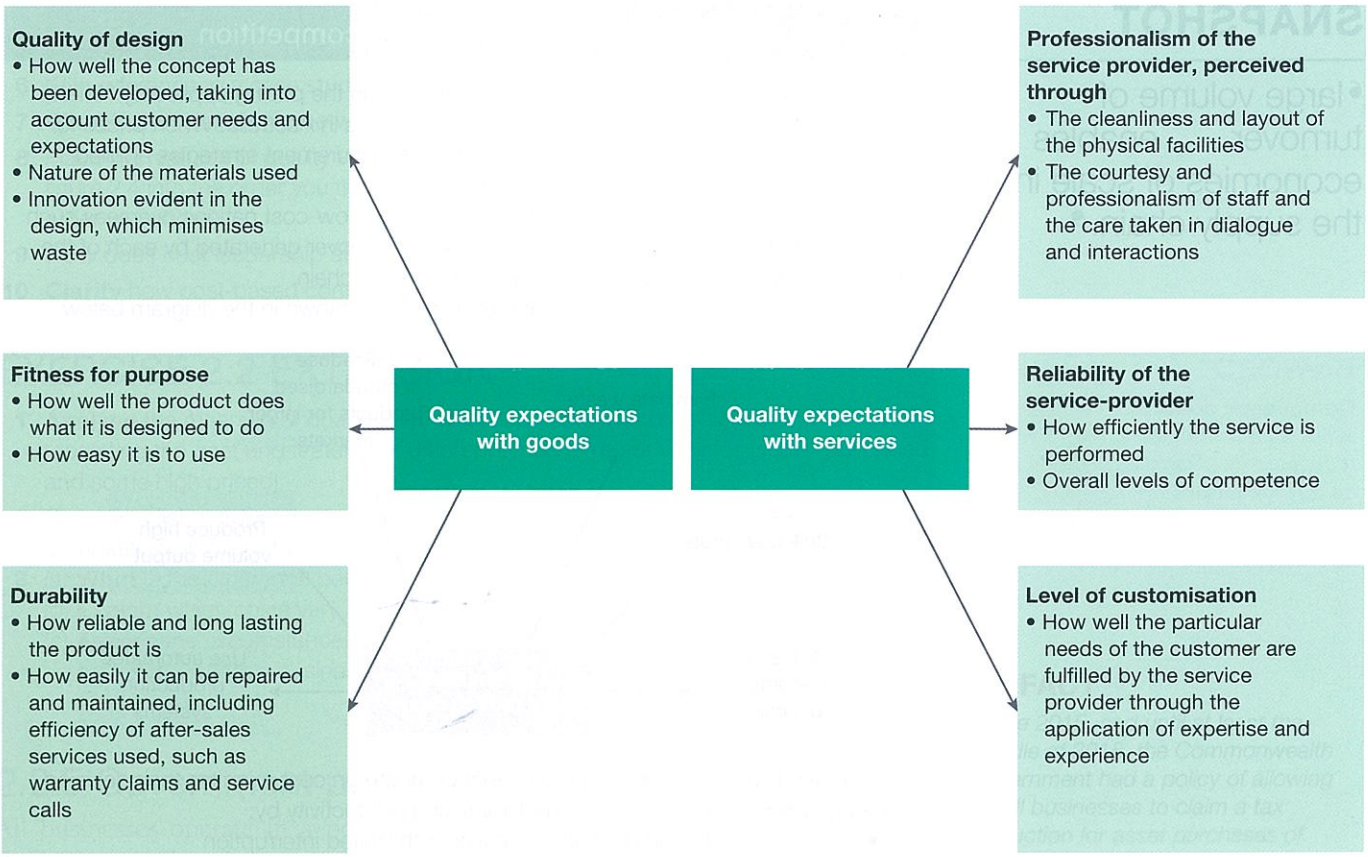


FIGURE 2.4 Distinguishing between quality expectations in goods and quality expectations in services

2.2.4 Cost-based competition

Another significant influence on the operations management function arises from the actions of competitors and the way such competitors price their products. As seen earlier in chapter 1, cost is a very significant element in business, and efficiency can be determined from assessing the cost structures in business. 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 prices cannot keep increasing; therefore, reducing costs is a way to maximise profits when revenues are fixed. Mass customisation enables cost-based competition even when products are differentiated rather than standardised.

Cost-based competition and operations management

Cost-based competition is a feature of operations management when businesses bring 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 operations management (see the following Snapshot), cost can be analysed from several different perspectives (recall table 1.1). Alternatively, costs may be divided into those which are fixed and those which are variable. **Fixed costs** are those that are not dependent on the level of operating activity in a business. This means that whether the business increases, decreases or maintains production these costs are unchanged. Examples of such costs are building leases and insurance costs. By contrast, **variable costs** are those that vary in direct relationship to the levels of operating activity or production. Such costs include labour costs and costs of energy.

BizWORD

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 applying strategies to create cost advantages over competitors.*

BizWORD

Fixed costs *are those that 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 *are those that vary in direct relationship to the levels of operating activity or production. Such costs include labour costs and costs of energy.*

SNAPSHOT

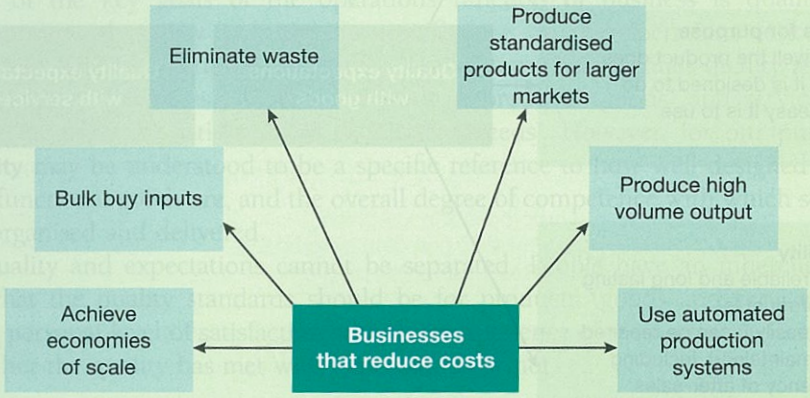
'large volume of turnover . . . enables economies of scale in the supply chain.'

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.

SNAPSHOT QUESTIONS

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

SUMMARY

- Technology plays a very important role in operations management — from administration, through to all operations processes.
- Management of quality expectations in both the manufacture of products and the delivery of services is an essential role and 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.

EXERCISE 2.2 REVISION

1 **Define** the term 'technology'.
2 **List** four forms of technology found in the household.
3 **What** is the main advantage of using communications technologies?

4 **How** does technology affect the operations function of a business?
5 **Explain** how a person's expectations affect how they view quality.
6 With reference to a case study, **detail** the benefit of building quality expectations.
7 **What** is the relationship between quality and price?
8 Place the features of quality expectations, for both goods and services, from figure 2.4 into the order you think is most important to least important. **Justify** the order you chose.
9 **How** does cost leadership affect price?
10 **Clarify** how cost-based competition affects the operations function of business.

EXERCISE 2.2 EXTENSION

1 **Analyse** the meaning of quality with reference to one motor vehicle brand. Do this by tabulating the cost and features of different types of motor vehicles (some low priced and some high priced).
2 Compile a list of five major fuel outlets. **Evaluate** the effect of cost-based competition on fuel retailers (refer to brands).
3 (a) **What** is the difference 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 where a business grows rapidly and needs additional facilities and machinery).

2.2.5 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. Government policy is, therefore, a notable source of change and a significant influence on business operations. This can be seen in the BizFact on the government policy on an instant asset write-off for small businesses.



FIGURE 2.5 The instant asset write-off policy helps businesses to easily access technology.

Government policies and operations management

Government policies often impact on business. Policies such as taxation rates, required materials handling practices, work health and safety (WHS) standards, industry training requirement, public health policies, environmental policies,

BizFACT

Since 2015, and until at least the middle of 2018, the Commonwealth government had a policy of allowing small businesses to claim a tax deduction for asset purchases of under $20 000. Typically, a business buying assets would be allowed to 'expend' the asset through an accounting process called depreciation. Depreciation allows a business to reduce the value of an asset in order to reflect its true worth after use. In this way, a business can reduce tax through claiming non-cash expenses such as depreciation. This tax benefit would typically last between five and ten years, as assets lost value and were then replaced.

The new policy of allowing a small business to claim up to $20 000 of assets as an expense, instead of having to slowly depreciate the value over years, is very beneficial. This is because it helps businesses invest in computers, vans, office furniture and other assets but get an immediate tax benefit. The tax benefit arises because expenses are matched against business income and therefore reduce profitability and lower the amount of tax payable.

Small business owners and peak bodies such as the Australian Chamber of Commerce and Industry (ACCI) believe that the instant asset write-off policy encourages investment by business and makes it more efficient.

employment relations, trade and industry policies all have an impact on business operations. Since policies can inform law-making, and lead to business opportunities, operations managers need to be fully aware of the contemporary government policies and what they comprise.

2.2.6 Legal regulation

A highly significant external factor that affects the operations function of business is that of laws and regulations. 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**.

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

BizWORD

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



FIGURE 2.6 Providing a healthy and safe workplace environment is an important part of an operation manager's responsibilities.

Legal regulation and operations management

All aspects of business must abide by the laws of business. Operations management has particular laws that influence how practices and processes are conducted. The operations function involves transformation and value adding. The transformation or conversion involves the use of any or all of labour, technology, finance, machinery and energy. The relevant laws will relate to labour and labour management, as well as the environment and public health including:

- 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

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).

- fair work and anti-discrimination laws — requiring that employees be treated with dignity and respect
- environmental protection — in the use of minimising pollution, eliminating and safely disposing of any toxic residues
- apply 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 2.7.

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 2012 (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)

FIGURE 2.7 The range of laws affecting and shaping business operations in Australia

2.2.7 Environmental sustainability

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 undertake actions that are most likely to cause least environmental impact.

Environmental sustainability and operations management

The operations management function is significantly affected by the rise in climate change awareness 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; recycle water, glass, paper and metals, and reduce their **carbon footprint**. The carbon footprint refers to the amount of carbon produced and entering the environment from operations processes.

SUMMARY

- Government policy is a source of change for business.
- Government policies affect operations management decisions.
- Policies from government can become laws and regulations.
- Businesses should comply with regulations including those relating to the environment.
- While some government policies restrict business practices, other policies encourage business and provide opportunities.
- Business operations are required to adopt environmentally sustainable practices to reduce their carbon footprint.

BizWORD

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.*

The **precautionary principle** *requires that, where environmental impacts are uncertain, a business undertake actions that are most likely to cause least environmental impact.*

Carbon footprint *refers to the amount of carbon produced and entering the environment from operations processes.*

on Resources

Video: Environmental sustainability and Ferguson Plarre Bakehouses (eles-1089)

studyon

Syllabus area 1
Topic 2
Concept 2

Globalisation and technology
Summary screen and practice questions

EXERCISE 2.3 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 **Summarise** three relevant laws that relate to labour and labour management for the environment and public health.
7 **State** the three main aspects to environmental sustainability.
8 **How** does environmental sustainability affect the operations function of business?

EXERCISE 2.3 EXTENSION

1 **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.
2 Select one of the laws listed in figure 2.7. **Evaluate** how the selected law would affect the cost and complexity of business.
3 **Examine** the notion of legal compliance. Explain how compliance adds cost to business but also regulates the conduct of business with reference to examples.
4 **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.

on Resources

Weblink: Fair Work Ombudsman

2.3 Corporate social responsibility

A relatively recent phenomenon, 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/society 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.

This can be seen with respect to Westpac Group in the following Snapshot.

BizWORD

Corporate social responsibility (CSR) *refers to 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.*

SNAPSHOT



Case study: Westpac Group — leader in CSR

The Westpac Group has been described as the most socially responsible bank in Australia. It has achieved a series of awards on account of its approach to sustainability and ethical business practices:

1992 First Australian bank to publish an environmental policy
1997 First Australian bank to create a formal community volunteering scheme
2000 Founding signatory to the UN Global Compact and launched the first socially responsible investment product in Australia
2002 Founding signatory to the Equator Principles and first Australian bank to publish a sustainability report

2014 Ranked number one in the Global 100 most sustainable companies in the world

2017 Westpac Group retained its position as the world's most sustainable bank in the 2017 Dow Jones Sustainability Indices (DJSI). This marks the fourth year in a row and tenth time it has achieved the global banking sector leadership position.

2017 progress highlights

Supporting gender equity

- Proportion of leadership roles held by women achieved the 2017 target of 50%, up from 48% in 2016.
- Introduced additional targets for our Board (30% women by end 2018) and General Managers (40% women by end 2017).
- In 2016, piloted an anonymous recruitment initiative to tackle unconscious bias by removing applicants' names, schools and other cultural indicators prior to applications being shortlisted for recruitment. In 2017, completed the roll-out of the inclusive leadership program to senior leaders. The program built upon the previous unconscious bias program, in place since 2013. Also designed a customised inclusive leadership program for middle management that will be delivered through an innovative approach introducing theories such as privilege and recognising bias.

Increasing flexible working arrangements

- Percentage of employees working flexibly increased from 63% in 2014 to 74% in 2016, with this figure remaining at 74% for 2017.

Reducing our environmental footprint

- Achieved 75% waste to recycling target following improvements in waste sorting, site audits and increased screening.
- Maintained carbon neutral status for the 4th year in a row.
- Achieved 6% improvement in electricity efficiency in commercial and retail sites, exceeding our 2017 target.
- Ranked world's most sustainable bank for 10th time in 2017 Dow Jones Sustainability Indices Review
  - — First ever Six Star Green Star rated bank branch
  - — Received Six Star Green Star rating for the St. George branch at Barangaroo — the first Green Star rating for an Australian bank branch and the highest ever rating for a retail outlet reflecting leading eco-efficiency practices

Source: Extracts from Westpac Sustainability Report 2016; Westpac Sustainability Report 2017

SNAPSHOT QUESTIONS

1. **List** three different areas where Westpac Group demonstrates an awareness of broader social, community and environmental concerns?
2. **Examine** the importance of increasing the number of women in senior leadership positions.
3. **How** could removing names from applicants affect recruitment outcomes?
4. **Create** a report on how Westpac may be described as the most socially responsible bank in Australia and one of the most responsible banks globally.

'. . . the most socially responsible bank in Australia.'

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.

2.3.1 The difference between legal compliance and ethical responsibility

All businesses should comply with all applicable laws and regulations. The government creates laws with an expectation that they will be followed. Penalties for breach of business laws act as a deterrent and can assist businesses to understand 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.

Complying with legislation costs a business money, which, as was previously explained, is referred to as compliance costs. To go further than the requirements of legislation is even more expensive for businesses. In demonstrating ethical responsibility, a business is demonstrating that it values something more than just earning maximum profits because it is allocating money over and above what it costs to comply with the law.

Legal compliance and business operations

Compliance typically falls in 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
- corporations law (also called 'Anti-trust' law), which imposes duties on directors and others who work in responsible positions within corporations.
- human rights, such as rules restricting discrimination on the grounds of disability, culture, sexual preference, gender, age or any other distinguishing feature.

Clearly, there are numerous laws that shape the conduct of business. 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

BizWORD

*A **fiduciary** is a person in a position of financial trust with respect to others' money.*

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. The process known as **outsourcing** involves the use of outside specialists to undertake one or more key business functions. Outsourcing may be done 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? This third party dealing can be a screen behind which many global businesses hide. In this way, breaches of compliance in other nations can be blamed on the party they have outsourced to.

BizWORD

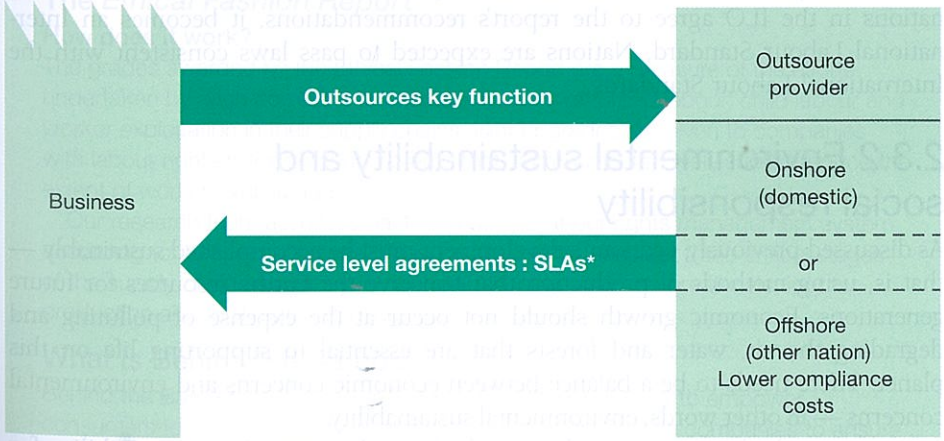
Outsourcing *or contracting out business functions involves the use of third-party specialist businesses, for example, recruitment firms. It aims to take advantage of the specialist skills provided by them and to achieve a reduction in labour costs.*

Onshore outsourcing *involves the use of domestic businesses as the outsourcing provider.*

Offshore outsourcing *involves taking the activities to a provider in another country.*



FIGURE 2.8 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 employees who work for low wages in many developing countries are not exploited by unscrupulous businesses.



* SLA: Contracted minimum standards of service

FIGURE 2.9 The way outsourcing is used by a business to reduce costs of compliance. *Note:* the use of service level agreements (SLAs) can be an ethical way to ensure the outsourcing provider adheres to high standards of conduct.

BizFACT

The main international body that discusses the workplace and sets guidelines and rules for work is the International Labour Organization (ILO). Information about the ILO can be read below.

Ethical responsibility

Ethical responsibility, as discussed earlier, 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, training and so on. A business may choose to follow international labour standards that come from 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.

FIGURE 2.10 The role of the International Labour Organization (ILO)
Source: www.ilo.org/global/about-the-ilo/lang--en/index.htm; www.ilo.org/global/about-the-ilo/mission-and-objectives/lang--en/index.htm

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.

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2.3.2 Environmental sustainability and social responsibility

As discussed previously, 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

on Resources
Video: Di Bella Coffee and CSR (eles-2284)

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 businesses 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 coincides with stakeholder expectations.

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), as explained previously, 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 businesses need to give careful consideration to their actions. The central theme is 'above and beyond' making a profit and obeying the law.

Social responsibility is good business — customers eventually find out which businesses are acting responsibly and which are not. Customers can react and stop buying a business's product if they learn that the business is exploiting employees, accepting bribes or polluting the environment. 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 turns out to be to the company's own interest. The impact of customer choices on business behaviour can be seen in the following ethical sourcing Snapshot.

BizFACT

Unilever is a global business that produces numerous well-known global brands such as Rexona, Lynx, Lipton and Dove. The business has been under increasing pressure to incorporate broader social and ethical standards into its operations processes. Pressure from environmental groups led to a decision by the company to source only sustainably produced palm oil for its products. Unilever is now the Chair of the Roundtable of Sustainable Palm Oil (RSPO). Unilever has also responded openly and positively to Oxfam, which criticised the treatment by Unilever of its employees in Vietnam. The company is an example of being open to change and understanding the importance of social and ethical responsibility.

SNAPSHOT

Ethical sourcing — clothing manufacture

Consumers are increasingly concerned about the impacts on people and the environment — both directly and indirectly — from the manufacture of the clothes they buy. The production standards of businesses that are within another business's supply chain is of concern to the market. Non-government organisations are increasingly exposing the supply chains of global brands, thus allowing consumers to make informed decisions about whether they want to purchase the brands with full knowledge about the brand's sourcing behaviour. One organisation that compiles lists detailing the level of ethical sourcing of the retail brands is Baptist World Aid. This organisation compiles the *Ethical Fashion Report*.

The *Ethical Fashion Report*

How does it work?

The grades awarded by the Ethical Fashion Report are a measure of the efforts undertaken by each company to mitigate the risks of forced labour, child labour and worker exploitation in their supply chains. Higher grades are given to companies with labour rights management systems that, if implemented well, should reduce the extent of worker exploitation.

Our research team assesses each company's labour rights management system according to 40 specific criteria. These assessments consider three critical stages of the supply chain as a proxy for the entire supply chain: raw materials, inputs production and final manufacturing.

What is Behind the Barcode?

Behind the Barcode is a series of industry reports which seek to empower consumers to purchase ethically and, by doing so, encourage companies to ensure workers are protected and not harmed; that they are rewarded and not exploited; and that they can work free from the tyranny of modern slavery.



'Since the first edition of the *Ethical Fashion Guide* in 2013, an additional 32% of companies are working to trace where their fabrics are coming from . . .'

One of these industry reports is the *Ethical Fashion Report*. It is released with an accompanying *Ethical Fashion Guide*. The research published in the 2017 *Ethical Fashion Report* grades 330 fashion brands operating in Australia and around the world, and assesses the systems they have in place to protect the workers in their supply chain from exploitation, forced labour and child labour.

Does shopping 'ethically' really make a difference?

You would be amazed at the difference your purchasing decisions can make! Since the first edition of the *Ethical Fashion Guide* in 2013, an additional 32% of companies are working to trace where their fabrics are coming from:

2013 49% **2015** 61% **2016** 79% **2017** 81%

An additional 28% of companies are working to trace where their raw materials are coming from:

2013 17% **2015** 31% **2016** 39% **2017** 45%

An additional 31% of companies are investing in paying fairer wages to workers:

2013 11% **2015** 14% **2016** 32% **2017** 42%

So yes, your advocacy and choice to purchase ethically is making a real difference. We hope that you take this little guide with you whenever you shop, to empower you to make every day ethical purchasing decisions.

The *Ethical Fashion Report* can provide consumers with insights into the buying or sourcing practices of the businesses they purchase from. From this, consumers are better informed as to whether they would like to support those businesses. Since consumer decisions will affect the revenue of businesses, a potential loss of revenue will 'encourage' businesses to behave in ways that consumers deem acceptable.

Of course, in disclosing certain information and in behaving in ethical ways, businesses will incur additional costs. However, as a general rule, businesses that behave in ethical ways can also charge more for their products, as consumers are willing to pay more for such products. In this way, all parties benefit, including the consumer who will feel happy with the way their choices contribute to improving business practices.

Source: Extracts from Baptist World Aid, *2017 Ethical Fashion Guide*

SNAPSHOT QUESTIONS

1. **Describe** the purpose and importance of the *Ethical Fashion Report*.
2. **Explain** whether it is important for consumers to be aware of where and how the products they buy are made and sourced.
3. **Assess** the likely impact of consumers making informed decisions on the way consumers buy.

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SUMMARY

- 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.
- Sometimes businesses seek to avoid compliance by using outsourcing as a business strategy.
- 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.

EXERCISE 2.4 REVISION

1 **What** is 'corporate social responsibility'?
2 **Identify** an alternative term for 'corporate social responsibility'.
3 **Recall** what corporate social responsibility places a value on.
4 **Distinguish** between legal compliance and ethical responsibility.
5 **Recall** the name given to the expenses associated with abiding by all laws.
6 **Summarise** four areas in which a business would have to demonstrate compliance.
7 **What** is one way that businesses use when aiming to reduce compliance costs?
8 **State** the main advantages to a business of off-shore outsourcing.
9 **Clarify** the ethical issues off-shore outsourcing raises concerning business behaviour.
10 **How** do compliance and ethical responsibility differ?
11 (a) **Recall** what the acronym ILO represents.
(b) **Identify** two matters relating to workplaces and the rights of employees that the ILO deals with.
12 **Explain** why businesses should be concerned with environmental sustainability.
13 **Account** for why there is growing consumer expectation for 'clean, green and safe products'.
14 **Identify** the two goals a socially responsible business tries to achieve.
15 **Determine** what the words 'above and beyond making a profit' suggest about a business's commitment to socially responsible practices.
16 Since an investment in CSR costs money, **what** is the impact on revenue and profitability if a business such as Westpac invests in CSR?
17 Reebok (a subsidiary of Adidas) and Levi Strauss place a great deal of importance on their corporate social responsibilities. Both companies have taken action against overseas suppliers based on their human rights and environmental codes of conduct. Undertake further research to **assess** their commitment to their social and environmental obligations. **Create** either an oral or written report and present it to the rest of the class.

EXERCISE 2.4 EXTENSION

1 With reference to a large business (such as Myer, BHP Billiton, Mobil or Virgin Airlines), **identify** six 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.
2 **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.

on Resources

- **Digital doc:** Chapter summary (doc-24804)
- **Interactivity:** Chapter crossword (int-7151)
- **Interactivity:** Multiple choice quiz (int-7152)
- **Weblink:** Reebok and Adidas sustainability
- **Weblink:** Levi Strauss
- **Weblink:** International Labour Organization

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