



UNIVERSITÉ DE FRIBOURG  
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Master Thesis

***High Price Island Switzerland?  
On the Reasons why Consumer  
Electronics are an Exception to the Rule***

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## List of Abbreviations

|          |   |
|----------|---|
| ASEAN    | Association of Southeast Asian Nations  |
| CE       | Consumer electronics  |
| CHF      | Swiss Franc   |
| DVD      | Digital Versatile Disc  |
| EA-15    | Euro Area, comprising Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Greece, Slovenia, Cyprus, Malta |
| EA-19    | Euro Area, comprising EA-15 countries plus Slovakia, Estonia, Latvia, Lithuania   |
| EFTA     | European Free Trade Association, comprising Switzerland, Norway, Iceland, Principality of Liechtenstein   |
| EU       | European Union  |
| EUR      | Euro  |
| FTA      | Free trade agreement  |
| GATT     | General Agreement on Tariffs and Trade  |
| IT       | Information Technology  |
| ITA      | Information Technology Agreement  |
| MERCOSUR | Mercado Común del Sur, economic and commercial group of countries in South America  |
| MNC      | Multinational Company   |
| OECD     | Organisation for Economic Co-Operation and Development  |
| PC       | Personal Computer   |
| TCO      | Total Cost of Ownership   |
| VAT      | Value added Tax   |

# 1. Introduction

Since the first gramophones and radio transmitters hit the European market over a century ago, consumer electronics have changed our lives. And the sector is still changing our daily routines with the advent of smart phones, smart cars or smart homes. Innovation and change are the only constant of this multifaceted business sector. Consumer electronics literally became a part of our culture.

Swiss are said to have a great affinity for technology. Almost no other nation spends in average as much for consumer electronics as Swiss people (Müller 2014). This is not only due to a high purchasing power: also, the prices for consumer electronics are very competitive in Switzerland compared to European countries. Currently, the price level for consumer electronics is exactly the same in Switzerland and in the European Union (EU). In previous years, the price level was even lower in Switzerland than in EU average (Eurostat 2016a). This is particularly interesting since Switzerland is commonly known for a high price level. From apparel to food and near-food products, newspapers or medicine – prices are significantly higher in Switzerland for almost every product category. The Swiss even invented an expression for their high price level and call their country an island of high prices.

## 1.1. Problem Statement

High prices in Switzerland are a main disadvantage in a competitive international environment. When arguing about the reasons for higher prices in Switzerland, the high income level is often the main focus of discussion. This argument does not seem to hold for consumer electronics. Consumer electronics aren't more expensive in Switzerland in comparison with European countries. However, the reasons for this remain unclear. Up to now, there are only assumptions why the price level of consumer electronics is so low in Switzerland. There are some studies that give rough indications on possible reasons but no in-depth study was yet conducted on the factors that shape consumer electronics prices.

Understanding the price setting mechanisms in the consumer electronics industry is crucial. It is conceivable that some myths about the high price level in Switzerland could be unmasked what would help to reach a better understanding of price formation in the Swiss marketplace. Hence, to understand the causes of this phenomenon could possibly assist economy and politics to apply the right measures in other sectors as well.

## 1.2. Objective

This master's thesis intends to answer 2 different research questions. After assembling a theoretical background, the first research question should have been answered:

- What are decisive factors that determine prices?

Understanding those mechanisms will help to establish working hypotheses for further research. Then, the main question to be answered during this study is the following:

- What are the main causes that determine the relatively lower price level of consumer electronics in Switzerland compared to EU countries?

If this master's thesis has managed to answer the second question, it would be of interest to derive conclusions out of it and to transfer the results to other industries.

## 1.3. Procedure

This thesis is divided in two parts, a theoretical background and an experimental part, as outlined in figure 1. After this introductory chapter, the thesis provides insights into the theory of price determination. Then, most common pricing strategies are highlighted. The literature review further comprises a chapter on global supply chains and their impact on pricing.

**Figure 1: Structure of the Thesis**



Source: Own Illustration

The experimental part begins with a review of the research design and methodology. As research design, a comparison between the consumer electronics (CE) and the apparel industry was chosen to answer the research question. Therefore, a total of six industry experts were interviewed. The following chapters present the results of the comparison. The results will be discussed in chapter 13, and the conclusions in chapter 14 bring the thesis down to a round figure.

# I Theoretical Background

## 2. The Theory of Price Determination

To understand why things cost what they do is one of the oldest questions posed by economic sciences, it even traces back to ancient philosophies. Price theory searches on explanations of how prices are formed and how price functions coordinate economic activity (Friedman 1986, p. 33). Whenever someone buys a product or service, he reflects if the price is accurate to him. Zeithaml (1988, p. 33) compares price to a sacrifice that is made to obtain a product. According to Friedman (2008, p.7), price theory “*deals with the allocation of resources among different uses, the price of one item relative to another.*” Other than monetary theory that deals with price levels in general, price theory is designated as a field of microeconomics (cp. Friedman, 1986).

This chapter aims first to explore the mechanisms of price determination and the historic development of price theory. Then, with regard to Porter’s five forces, the determinants of industry structures are discussed. Further, the impact of market structures on prices is reviewed. And finally the influence factors on prices are summarized in a nutshell.

### 2.1. Origins of Modern Price Theory

The origins of price theory date back to the time of ancient Greeks and Romans. To study those philosophies helps to understand the concepts of price and value, this chapter therefore starts with ancient philosophies. Those concepts were interpreted differently in Medieval Europe and later by classical price theory.

As referred to (Ott 1991, pp. 20.21), a distinction is made between objective and subjective price theory. The two theories differ in their definition of value. The objective value of a commodity is measurable and an asset of this object. The subjective value of a commodity depends on the perception of usefulness of a certain person at a certain point in time. Objective price theory goes back to Greek philosopher Aristotle. He distinguished between the value in use and the value in exchange, that is basically the true worth of a good in opposition to the relative price of that good (Ott 1991, p. 21). In consequence, commodities may have a compelling value in use but almost no value in exchange, as for example water (Capaldi and Lloyd 2011, p. 321). Aristotle did not formulate a labor theory of value, but noted that labor and utility determine the value of a good (Younkins, 2005). Thus, for Aristotle demand is governed by the desirability of a good.

From the 9<sup>th</sup> century on in Medieval Europe, the scholastic movement tried to conciliate ancient philosophy and religion. Dominican philosopher and theologian Thomas Aquinas was one of the most important representatives of scholastics philosophy. In his extensive body of work, he also wondered about economics and price formation. Following Aristotle's exchange price, he formulated the theory of a just price. A just price is a divinely defined price. The question is though how eventually the true economic value is determined. Scholars are discordant if the just price is either quite simply the market price or rather represented through the cost of production. However, the market price should not be misinterpreted as a liberal market price in today's sense because prices should, after Aquinas, always be limited by human virtues and values (Barrera 2001, pp. 64-68).

These medieval views on price and value changed with the development of the English classical school. In classical value and price theory, the labor theory of value was the dominating explanation for pricing decisions. The labor theory of value says that the price of a good is determined by the time invested in producing it. Adam Smith, David Ricardo and Karl Marx all pored about this theory and made significant modifications to it (Dooley 2002). Adam Smith (1776) argues that in the long run, market prices are determined by the natural price of a good, that is a price that arises from production cost, independent from supply and demand. Therefore, prices of commodities are defined by the input and quality of labor used to produce them. The basic prerequisite for the functioning of the market and division of labor is, after Smith, the self-interest of every individual to ameliorate its economic situation. An invisible hand ensures that the self-interest of people will always serve common welfare (Stavenhagen 1969, pp. 53-54).

With his labor theory of value, Smith adds an interesting thought to the so-called diamond-water paradox that was introduced by John Law (Law 1750). As water is essential for life, people should value it more than diamonds. But in terms of labor, it is much more difficult to acquire one kilogram of diamonds than water. For Smith, the value of a good derives from scarcity and intensity of labor invested in (Weber 2012). About a century later, it is Carl Menger and other economists who almost similarly propose another resolution to the water-diamond paradox based on marginal utility (Weber 2012). As the first liter of water is essential for life, its marginal utility decreases rapidly with every further liter (Tucker 2016, p. 156). Like that, price is in equilibrium with both cost of production and value to the consumer. This argument brought a new perception of prices and value to the discussion, neoclassical theory was born. Neoclassical theory is known for its idea of a *homo oeconomicus*, a rational and self-interested agent who always tries to maximize utility as a buyer and profits as a seller respectively. A *homo oeconomicus* would participate in perfect markets.

Such a market is *inter alia* defined by a large number of buyers and sellers, perfect information, no entry barriers, rational buyers and profit maximization (Jain and Khanna 2006, pp. 309-315). Under these preconditions, the market will automatically adjust towards equilibrium where demand and supply are balanced. In a perfect market the price is equivalent to marginal cost (Price Supervisor, 2014, p. 26). The first to formalize a general equilibrium model mathematically was León Walras (1874). As explained by van der Lecq (2000, p. 18), there is a supply function, a demand function and a market-clearing condition for each market which balances the quantities. Walras suggests that market clearing is reached through the process of *tâtonnement*, comparable to a process of trial and error. The market-clearing price is therefore an equilibrium price that reacts to shifts in the demand or supply curve (Barro 2007, p. 12).

1954, Arrow and Debreu added some profound restrictions to the Walrasian model. Hence, they could show mathematically that commodities and factors of production are efficiently allocated under perfect competition. In an Arrow-Debreu economy, there has to be a complete set of perfectly competitive markets. An auctioneer, comparable to Smith's invisible hand, is perfectly informed about demand and supply conditions in every market and there are no transaction costs (van der Lecq 2000, pp. 18-19). One of the benefits of the model is its generality. It can easily be modified and extended, for example to analyze expectations and uncertainty, international trade, or financial and monetary markets (cp. Thomson 2008).

Market segmentation is not possible in a perfect market with easily tradeable goods due to the law of one price. Not uniform prices leave room for arbitrage which has the effect to reduce price differences (Jäggi/Langenegger 2016). The law of one price was refuted through a large number of empirical studies (Iten et al. 2003, p. 9). Different factors such as tariffs or transaction costs lever out the law of one price (Price Supervisor 2014, p. 26).

## **2.2. Porter's Five Forces Model**

The industry structure determines the rules of competition and available strategies to a wide extent. After Porter (1980), the competition in an industry is rooted in five basic forces. The summarized strength of these forces qualify the profit potential of an industry and therewith the prices. Forces outside the industry are only conditionally important because they normally come upon every industry participant.

The intensity of competitive rivalry is a major force determining the competitiveness in an industry. Several factors influence rivalry among competitors. The concentration of providers, switching cost, exit barriers and the tactical focus of companies all have

an effect on rivalry. Also, the growth rate of an industry and the speed of how fast companies adapt to actions of competitors are decisive factors (McGuigan, Moyer, and Harris 2013, pp. 346-351).

The threat of substitutes is another factor that limits the profit potential of an industry. A substitute is an alternative choice for customers outside the industry, as for example a bicycle may substitute a car. A substitute product is an important market force because it sets a ceiling on the market price (Porter 2013, p. 60).

The threat of new entrants is the second force which could possibly lower the prices for a good or reduce profits of existing companies. New market entrants often follow an aggressive strategy and invest considerable funds. The threat of new entrants highly depends on the existence of market entry barriers such as economies of scale, product differentiation that goes along with customer loyalty, conversion cost and capital requirements, access to supply chains and resources as well as expected reactions from competitors (Porter 2013, pp. 41-47).

The bargaining power of consumers represents the influence of demand on price. If the bargaining power of consumers is high, they are able to put companies under pressure to lower prices. The power of customers is higher if they have many alternatives, if switching costs are low, if price transparency and sensitivity is high, and if they are well informed. Also, the concentration of buyers may play a role. These influence factors apply for industrial and commercial customers likewise (Porter 2013, pp. 61-63). The last force is the bargaining power of suppliers. Powerful suppliers may threaten to raise prices or to lower the quality of a product. Most causes of bargaining power of consumers are valid for supplier power as well.

### **2.3. The Impact of Market Structures on Prices**

Every market is different from all other markets and has its own characteristics that make it unique. Examples of such market characteristics are its growth rate and market potential, level of competition, market volume or lifecycle stage. One of the most predicative market characteristic in matter of price formation is the market structure. It is determined by the number and relative strength of market participants and the intensity of competition and demand. The market structure has strong impact on price and quantity policies of companies.

Under a hypothetically ideal market environment, there would be perfect competition with many buyers and sellers that do not influence prices or market conditions. There are markets that come close to perfect competition, such as the foreign currency market or the jewelry market, but all markets have limitations to perfect competition.

Under perfect competition the supply will be adjusted to the demand so that marginal costs are equal to marginal revenue, as was mentioned. In theory, the market price is lowest in a perfectly competitive equilibrium, that is under perfect competition (Fisher and Waschik 2005, p. 91). But in reality, markets are imperfect. If companies offer products that are similar but not perfect substitutes, this market structure is called monopolistic or imperfect competition. Other than with perfect competition, firms have to invest in advertising. Neither resource allocation nor social welfare are maximized under monopolistic competition (Mankiw 2014, p. 259).

An emerging market form are oligopolies, which is a form of competition where few firms dominate (Mankiw 2014, p. 264). Features of such markets are mutual interdependence, a lack of uniformity in the size of the companies, high investments on advertising and keen competition among the rivals (ibid., pp. 264-265). Oligopolies are characterized through group behavior, as for example quick reactions of market players to changes of competitors. For these reasons there are game theoretic approaches to explain oligopolistic price determination. Hence, oligopolistic markets have different behavior patterns. In some oligopolistic markets, cartels are formed. Such a market has identical price determination mechanisms as a monopolistic market. The opposite behavior would be price wars among rivals. Between those extremes, there are many forms of cooperation and non-cooperation. For those reasons, there is not a general oligopoly theory to explain price determination (cp. Jain /Khanna 2006).

The most striking market imperfection occurs if there is a monopoly. A pure monopoly is a market served by only one provider and whose position is protected by barriers to market entry. A partial monopoly occur if there is a powerful cartel of firms or a market dominating player (cp. Busse von Colbe/Lassmann 2013). The monopolist can choose any price / quantity combination on the demand curve (McKenzie/Lee 2008, pp. 30-31). The assumption of monopoly theory hence is that a monopolist will reduce the quantity of his good to raise prices. On these grounds, monopolies and cartels are viewed as detrimental to social welfare, which is why law makers often try to disintegrate monopolies by antitrust legislation. On the other hand, a high market concentration of buyers is an effective measure to lower the price level (Meyer 2016, p. 42).

(McKenzie 2009) however argues that in some cases even the opposite may be true. A monopoly achieved its market power by significant investments and therefore will not want to restrict output. Instead, the monopolist expands it and lowers prices. McKenzie (2009, pp. 18-19) further states that there is no incentive for entrepreneurial effort under perfect competition, because there is no chance of making a monopoly rent to cover product development cost, and therefore, politics and economics

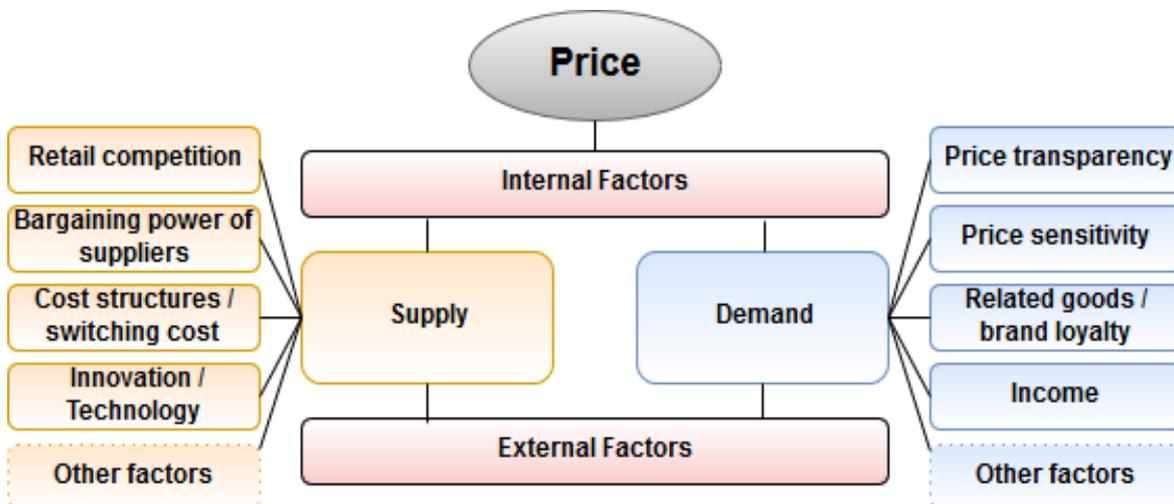
should not aspire to reach perfect competition in markets. Natural monopolies are often firms in gas, electricity, water and sewer supply businesses. Such natural monopolies are capable of providing those goods for lower overall costs as a number of competing firms could (Hirschey 2008, p. 466). In consequence, monopolies are not always damaging if they are of superior efficiency or leading in innovation (cp. Ibid).

## 2.4. Influence Factors on Prices in a Nutshell

Influence factors on price are divided into primary and secondary factors (Dreesbach 2013, p. 49). The law of supply and demand is often the first reference point to explain how prices are formed. It is scarcely surprising then, that supply and demand are the two primary factors. This model states that high supply and low demand lead to low prices, whereas low supply and high demand lead to high prices. Conversely, raising prices can lead to a decrease in demand and vice-versa. In practice, demand is more or less elastic to price changes.

Secondary factors are all factors that influence supply and demand. Porter's five forces are a helpful model to analyze secondary factors. Figure 2 shows the interaction of supply and demand under the influence of selected secondary factors.

**Figure 2: Influence Factors on Price**



Source: Own Illustration

However, not all aspects of price formation are covered by those five forces. Porter's five forces do not take costs into account. As it is a model to observe industry structures it ignores internal and external factors (Kotler/Armstrong 2010, p. 315). The broader governmental and societal environment defines external limits and are generally beyond the influence of companies (Porter, 2013, p. 30). Economic trends, political events or climatic changes are examples for external factors (Dreesbach 2013,

p. 50). Also, tariff and non-tariff barriers to trade are normally beyond the influence of companies and count therefore as external factors. Marketing objectives, organizational considerations and strategic decisions are internal factors that influence pricing decisions. A change in each of the mentioned factors may change the price of a good. They are for these reasons included in the illustration.

### 3. Pricing Strategies

Was price determination once just a cost-based calculation, is it now a complex management task with a big number of strategic and functional parameters. Diller /Herrmann (2013) observed several changes due to new information technologies. The first factor is increasing differentiation of prices with a stronger focus on certain customer segments and dynamic pricing. Secondly, online prices adapt permanently to new conditions. The internet increased price transparency significantly (Zentes/Morschett/Schramm-Klein 2012, p. 44). Price management has therefore become a constant task.

This chapter outlines different strategies of companies to set product prices. In economics, the fields of pricing, price policy or price management examine this decision-making process. According to Oettler (2014), the aim of pricing is to set prices in a manner that company goals are reached. Therefore, price management is closely related to strategic management and marketing. Price management is more than just pursuing high contribution margins; it also includes product conditions such as fast delivery, quality or goodwill. Price management is more sophisticated nowadays by using modern methods of market research. There is sophisticated software capable of analyzing big data volumes. Such price engines forecast scenarios of consumer behavior based on historical data, competitor's prices, inventory and many more factors (Zentes/Morschett/Schramm-Klein 2012, p. 262).

Pricing decisions are generally based upon three measures: Cost, competition and demand (Rao 2009, p. 14). These price drivers are also called the strategic triangle of price management. Oettler (2014) furthermore includes strategic objectives and legal circumstances as price determinants from a business standpoint. This chapter will delve deeper into the three basic drivers of pricing: cost, competition and demand.

#### 3.1. Cost-based Pricing

Costs define the minimum price of a good if the aim is to make no losses. There are different sources of costs. Production costs of a product result from labor, rents, material, energy and capital costs (Bernard 2011, p. 404). Other cost factors are transportation and warehousing, marketing activities or taxes. Swiss companies often accuse higher costs to justify a higher price level of consumer goods (Price Supervisor 2014, p. 26). A company has to ensure that the prices demanded cover these costs if they want to make a profit. Cost-based pricing focuses on this thought. Traditional cost-based price politics will first consider the features of a product followed by cost calculation, then adding a premium on top of it to determine the product price. Cost-

based pricing does not need to take supply and demand into account and is easy to implement (Pride and Ferrell 2008, p. 585).

Costs impact pricing decision in diverse manners: they provide information about minimum or target prices, or about the effects of price changes (Caspari/Caspari 2004, p. 134). Accurate information about product costs is essential to distinguish between profitable and unprofitable products. However, it is sometimes challenging to determine overall costs for providing a product or service. Often, large parts of the costs are common costs which are difficult to portion rationally among different products and especially among services (Brent 2014, p. 32). The most common cost-based pricing approach is cost-plus pricing or markup pricing where a specific amount or a predetermined percentage of the cost is added (Pride/Ferrell 2008, p. 585).

In full-cost pricing even indirect fixed costs such as overhead or capital financing are considered for price determination (McGuigan/Moyer/Harris 2013, p. 526). Full-cost pricing always runs the risk of non-competitive prices. One major disadvantages of cost-plus or full-cost pricing are the complete ignorance of demand curves and of competitors. Target profit pricing (or break-even pricing) is a way to take demand curves into consideration. Target profit pricing uses a break-even chart to visualize revenue at different sales volume levels. Companies should estimate target profit volumes and break-even points at each price to choose the most preferable alternative (Kotler/Armstrong 2010, p. 322).

Marginal cost pricing is another cost-based pricing strategy. Marginal costs include all direct variable costs as well as a portion of fixed costs a product causes. The merit of marginal cost pricing is flexibility not to recover parts of fixed costs depending on market circumstances (Ramaswamy 2013, p. 552). This pricing strategy is used to deplete production capacity or to stimulate sales during periods of low demand. A marginal cost pricing strategy though runs the risk not generating enough profit to cover overall costs (Jensen-Butler et al. 2008, p. 12). Therefore, the strategy should only be applied in the short-run.

Overall, cost-based pricing raises the risk of ignoring market forces of competition and demand. Also, brand positioning is neglected, and no incentives are offered to increase cost efficiency. As for these reasons, cost-based pricing should be combined with demand-based and competition-based strategies and primarily be used for determining minimum prices (Schmidt 2013, pp. 49-50).

Companies use cost and activity accounting to plan and control cost and return as well as to evaluate profitability of processes, cost centers or divisions. The first step

in cost and activity accounting is to divide cost into cost objects. A certain product could be a cost object. Individual costs are a direct attribute of cost objects. Fixed cost such as taxes and interests are relocated to cost objects through cost centers. Fabrication, material or purchasing would be typical cost centers. Direct costs can accurately be accounted to a cost object whereas indirect costs are assigned to cost objects through cost allocation (Drury 2008, p. 48). By dint of cost object accounting, an overall calculation is established. A preliminary calculation is suited to account the supply price of a product.

### **3.2. Competition-based Pricing**

Optimization of welfare needs an economic system that is built upon efficient competition. Competition leads to lower prices, more products on offer and a higher productivity (Price Supervisor 2014, p. 25). Many markets are dominated by rough competition on the level of retailers or suppliers. A competition-based approach to pricing could be chosen in such an environment.

Chances in a market are only accessible if actual price behavior, competitiveness, cost and other relevant factors of competitors are known (Simon 2013, p. 73). Without appropriate knowledge of competitors and their reaction to own strategies, product development and market cultivation are solely based upon assumptions. Therefore, competitive intelligence should be an important issue to every company (Deltl 2013, p. 14). Information procurement is sometimes difficult for prices that are not publicly visible or for information about cost, services and competencies. Intensive research is often necessary to gain sufficient information about competitors; and even with extensive information about competitors, their reactions are afflicted with uncertainty. Price agreements that would mitigate such uncertainties are forbidden in most countries (Herzog 2015, p. 35). Instead, there are several legal approaches to achieve price co-ordination.

Any behavior among competitors can be analyzed with game theory. Game theory provides interesting approaches to dissect and model competitive behavior, if it relies on realistic assumptions (Bungert 2012, p. 78). Game theory develops solution concepts to predict which strategies will be applied during a game. A solution concept is a mathematical model of co-operation or conflict between rational decision-makers (Myerson 2013, p. 1). The Nash equilibrium is a common solution concept. It describes a condition in a game, where no player is better off by changing his strategy (cp. van Damme 2012). Another way to anticipate competitors' behavior is to simply predict actions from past behavior. A firm builds reputation by repeating behavior. Once a firm has a certain reputation, it can cause co-operative responses with a certain behavior (Bungert 2012, p. 72).

In a first scenario, competitors try to co-ordinate to optimize each market position without breaking antitrust legislation. One way to achieve co-ordination is competitive market signaling. According to (Mankiw 2014), “*signaling is an action taken by an informed party to reveal private information to an uninformed party (p. 465)*”, therefore signaling is a response to asymmetric information. For example price, advertisements or money-back guarantees could be used as a signal for quality (Bungert 2012, p. 81). Market signaling fosters comprehension of moves and reactions of competitors. Potential aims of market signaling could be to detain new market entrants or to request competitors to adopt the same behavior (Herzog 2015, p. 36). Often, the price leader gives a signal for price changes and competitors will follow suit (Bungert 2012, p. 75). In consequence, every move of a market actor could be interpreted as a signal. But according to Bungert (2012, p. 82), most literature regards only intended actions as signals. If in reverse an uninformed party takes action to reveal information, this is called screening (Mankiw 2014, p. 466).

But rivals’ behavior is not always co-operative as the canonical prisoner’s dilemma exemplifies, even if it appears to be in their best interest. Rivals try to undercut their competition in such a scenario with dumping prices what may lead into actual price wars. The aim of such behavior is to drive out smaller competitors, to gain market shares or to prevent companies from market entry. However, a better alternative as to threaten new market entrance with a potential price war is to make preventative investments. The potential new market participant then knows for sure that his market entry would lead to a price war and resigns such plans (Pindyck/Rubinfeld 2009, pp. 653-654). This is especially true for monopoly markets. Against traditional price war theory, Selim (2010, p. 6) concludes from his game theoretic study that an incumbent firm should not reduce its price even if a competitor offers lower prices. He argued that lowering prices to gain market shares instead of lowering it due to cost advantages is detrimental to profits.

Competition-based pricing sets prices in accordance with competitors. If companies follow such a pricing strategy, they have to consider game theoretic findings to achieve co-ordination with their competitors in an optimum way. However, a competition-based strategy can be disadvantageous if product cost and demand are not taken into account as well.

### **3.3. Demand-based Pricing**

Even though retailers justify higher prices in Switzerland with higher costs there are indications that consumer prices are rather oriented on skimming off higher purchasing power (Price Supervisor, 2014, p. 27). In this case pricing is demand-based. It is assumed that demand-based pricing attains higher profit levels under the condition

that the buyer is willing to pay more for a product than the product's cost (Pride/Hughes/Kapoor 2009, p. 386).

The demand function represents the connection between price and quantity of sales. Price elasticity describes the ratio of how much the quantity of sales reacts to price changes (Simon/Fassnacht 2008, p. 91). Potential customer reactions on price changes are anticipated on the basis of the demand function and price elasticity (Schmidt 2013, p. 54). Interviews and observations are the main tools to figure out the demand function (Simon/Fassnacht 2008, p. 110). Also, historical data can be used to determine the demand function (*ibid.*, p. 144). Once a price-demand curve is specified the demand-based pricing method must be defined in accordance with a company's pricing objectives. There are several different approaches to demand-based pricing.

Customer-driven pricing tries to set the price in accordance with what each customer is willing to pay and therefore charges various prices to different customers. In an optimum way customer-driven pricing yields high volume sales with maximum margins (Raju/Zhang 2010, pp. 8-9). Such a discriminatory pricing tactic runs though the risk of alienating customers with potentially detrimental long-term implications. Raju & Zhang (2010, p. 11) argue that with such a pricing strategy the seller has little incentive to invest in relationships and customer services and it encourages customers to do more comparison shopping or to drive a hard bargain which is why product differentiation declines and price pressure rises. For these reasons, a value-based approach to pricing may be more advisable.

The perceived value of a product is the basis for price determination in value-based pricing. The aim of this pricing strategy is to exceed perceived value of competing products. Best/Vomocil (2014, p. 14) define customer value as the difference between a product's selling price and its fair price. According to them, superior value can be generated through actual or perceived performance of a product, through total cost of ownership or preferences for certain price / performance combinations. In value-based pricing prices are normally set in a way that they are consistent with the benefits the product offers to the consumer (Ferrell/Hartline 2010, p. 249). Other than cost-based pricing, the price of a product is set before the other determinants of the marketing mix in value-based pricing (Kotler/Armstrong 2010, p. 315). The first step in value-based pricing is to assess consumer's needs and to target a price therefrom (Lamb/Hair/McDaniel 2008, p. 494). The outcome of this determines maximum costs and design of the product (Kotler/Armstrong 2010, p. 315). Best/Vomocil (2014) present three approaches to value-based pricing. A price performance strategy assumes that there is a relationship between performance and price that can be managed to gain a value-added price position. The important question to answer with this

strategy then is if the investment required yields a substantial pricing return on investment. Another approach is to consider total cost of ownership (TCO). TCO pays attention to the full lifecycle cost of a product. Value-based TCO does not only take into account actual cost data, but integrates further potentially hard measurable factors, as for example quality, support or technology (Krämer 2008). It is therefore a means to consolidate cost-based and demand-based pricing. Thirdly, trade-off value-based pricing requires the customer to make a trade-off between price and performance. A so called price buyer uses the price as his primary value driver and then chooses the best performance among similar products in price (cp. Best/Vomocil 2014).

In the introduction phase of a new product, the company has to decide whether to skim or penetrate the market. Skimming means that the seller charges a premium price for the product at first to skim off additional profits, before reducing the price to address new customer segments (Griffiths/Ison 2001, p. 100). Skimming is a common strategy for product introduction and often applied in the consumer electronics sector (Blythe 2005). Penetration is the opposite strategy to market skimming. This strategy intends to quickly gain market shares by the means of low initial prices. The intention is to capture market share before competitors can react (cp. Blythe 2005). However, this strategy does not necessarily lead to a sufficient profit rate. If prices are raised after the introductory campaign, customers may switch back to competitors. Kuhn (2007) emphasizes the importance of pricing strategies on the success of a product launch, besides factors such as the degree of innovation or internal commitment to the project.

Dynamic pricing on the other hand is utilized to frequently adjust prices to changes in demand or supply conditions, and to adapt to contextual factors such as seasonality, special events or even the weather (Bodea/Ferguson 2014, p. 168). Dynamic pricing also serves as a means to stimulate short-term demand. This pricing strategy is applied in various industries. First established in the travel and hotel industry, is it now a common strategy in many online retail shops (cp. Cummings 2013). Dynamic prices are calculated by an automated algorithm based on product availability, demand, competition prices or current advertising efforts. Even personal data such as the current location or the internet browser in use were encroached by firms to achieve maximum profits (cp. Cummings 2013). Firms who infringe data privacy in such a way risk displeasing customers, as happened with Amazon. Under the pressure of the public they had to reimburse customers who paid more for the same product only because of their internet browser (cp. Vogel and Rothenberger 2014). Nonetheless, dynamic pricing offers opportunities to companies whereof they have to profit to stay compatible. It is not only a means to better manage demand, but also to control losses and excess inventory (Bodea/Ferguson 2014, p. 169). Dynamic pricing pro-

vides significant benefits to firms. It is a means to maximize profits and to clear out excessive inventory. On the other hand, it may be difficult to plan inventory replenishment because sudden price changes may highly influence demand. For customers, dynamic pricing can be confusing or leave a feeling of inequity what may impinge upon a firm's reputation.

Once a price for a product is set, the way to present it makes big differences. Two-part pricing or payment pricing for example diminishes peoples sensitivity for the total price (Solomon 2009, p. 376). Such psychological pricing strategies stimulate buying decisions based on emotional perceptions rather than rational considerations.

Psychological strategies are mostly used for consumer products and barely in business to business settings (Pride/Hughes/Kapoor 2009, p. 388). Psychological pricing has the power to increase sales, is it by indicating that a product is a bargain or by stirring up feelings of exclusiveness and prestige (Boone/Kurtz 2012, p. 652). There is a great quantity of psychological pricing strategies, as for example bundle pricing, odd pricing and alleged scarcity. In product line pricing, a number of products are grouped together and sold at the same price. Different price levels then help the customer to reflect value differences. Limiting the number of price lines endorses retailers to become specialists for those price lines and buying inventory is simplified. Therefore, line pricing is very common in retail stores (Dunne/Lusch/Carver 2013, p. 413).

Further, consumers are susceptible to reference points, so-called anchors. Psychological pricing often takes use of anchoring effects, particularly if knowledge about quality and the price range of a product is vague. Such price anchors can be pre-scinded from various information sources and are often perceived unconsciously. One anchoring effect is that consumers often choose the middle price out of three choices, for example when selecting a wine in a restaurant (Simon 2015, pp. 32-33). Odd pricing means setting a price just below a round number what is another form of anchoring. Research supports the effectiveness of odd pricing (cp. Anderson/Simester 2003).

## 4. Global Supply Chains

Today's supply chains spread across the world what poses several challenges to companies. The lines between different channel participants from manufacturers over service providers to retailers become increasingly blurred. The bargaining power of each channel participant plays an important role for the end price of a product. Companies entering international markets have to adapt their pricing structures to increased price pressure, global players and rapid technology changes (Büter 2013, p. 156).

The first section of this chapter investigates in the structure of distribution channels and the impacts of bargaining power of channel participants. Secondly, tariff and non-tariff barriers to trade are outlined that companies face when importing or exporting products. The last section then explores opportunities for price discrimination and arbitrage.

### 4.1. Structure of Distribution Channels

The structure of distribution channels and the power of suppliers highly influence the end price of a product. A study by Dent (2014) found that typically, around half the price paid for a product by the end customer is absorbed by activities in the supply chain.

Companies sell their product or service either through a single or multiple distribution channels. Direct sales from manufacturers without any middle engagement are the most straightforward way of a distribution channel. This distribution model potentially leads to higher profit margins with control over pricing, distribution and assortment (Tsay/Agrawal 2004, p. 94). More common though is one- or multiple-tier distribution, since intermediaries offer suppliers cost-effectiveness by providing their assets and infrastructure (Dent 2014, p. 14). A one-tier distribution channel would set one intermediary between the supplier and the customer, such as an overseas agent. Typical intermediaries are distributors, importers, wholesalers, agents or system integrators, and not least retailers. Each intermediary needs a part of the end price charged to consumers to cover its cost and provide some profit. Many companies use a mix of different distribution channels to fully exploit the market potential.

A multi-channel design may enable companies to discriminate prices by serving different customer segments through different channels. A common example of such price discrimination is a product that is cheaper in an online store than in a dedicated retail store (Phillips 2005, p. 79). However, different distribution channels create a risk of channel conflict, especially if a company acts as a competitor to resellers through

direct sales. Also, enterprises have to be aware of potential consultancy theft and a lack of understanding if charging different prices through different channels (Furey/Friedman 2012, p. 181). Diller/Herrmann (2013) noticed rising price resistance in distribution channels that make negotiations an essential issue. Potential drivers of this change are higher expectations of consumers, information technologies, predominant international players and a decreasing profit margin due to higher competition intensity (Wölflle/Leimstoll 2016, p. 19).

Another trend in supply chain structures is increasing disintermediation. Disintermediation describes the abolition of intermediaries and is related to vertical integration of companies which is the internalization of intermediaries. Disintermediation enhances bargaining power of manufacturers and customers against retailers. Manufacturers increasingly supply retailers or even end customers directly, primarily due to growing e-commerce activities (Leimstoll 2009, p. 218). Prestige advertising through an orchestrated customer experience and direct contact to consumers are main goals of such efforts. Similar moves of disintermediation are undertaken by wholesalers (Heng/Slomka 2014, p. 4).

## **4.2. Barriers to International Trade**

Political borders become increasingly irrelevant in finance, trade or industrial businesses (Kotabe/Helsen 2009, p. 4). Instead, regional trade unions such as NAFTA, EU, ASEAN or MERCOSUR gain importance. This globalization process increased the volume of world trade and foreign direct investments (Wittendorff 2010, p. 4). A main driver of these rearrangements is telecommunication and information technology that have changed the nature of business environments tremendously. Boundaries and distances are less of a constraint in global markets nowadays. This increasing information access creates demand that didn't exist before (Kotabe/Helsen 2009, p. 4).

In recent times however there are worldwide tendencies towards stronger protectionism and global disintegration. Far more trade restrictions are imposed by governments than trade facilitation measures mainly due to socioeconomic tensions and political conflicts (Lehmacher 2017, p. 4). A distinction is made between tariff and non-tariff barriers. Tariff barriers to trade are direct protectionist measures taken by governments, such as duties and disposals (Dietl 1998, p. 502). A form of disposals is excise taxes that are imposed on consumption items as for example on electricity, alcohol or tobacco. Furthermore, absorptions such as minimum prices or export subsidies are forms of tariff barriers. The primary aim of tariff barriers is to protect local companies and jobs (Lehmacher 2017, p. 4).

Non-tariff barriers to trade are used in a variety of different forms. There is no clear demarcation for the term non-tariff barrier. It is established practice to use it for all protectionist governmental measures that distort volumes, compositions of goods or regional structures (Adebahr/Maennig 1987, p. 144). Accordingly, Non-tariff barriers are commercial policy measures beyond tariffs and subsidies that restrict access to a market. Underlying causes for non-tariff barriers are various. Technical norms, special provisions regarding packaging and labelling, labor protection laws, bureaucratic hurdles or conformity evaluations are some of them (Swiss Confederation 2016). Different legislation on labor or product directives that have to be respected in each country makes international business more complex. International law suits rise to questions of applicability of law and enforcement of judgements (cp. Iqbal 2015). Legal expenditures need to be considered in calculation when doing business internationally. Also, customs procedures hinder free trade even though no tariff barriers are imposed. Furthermore, government procurement, state-trading and taxes may impose non-tariff barriers to trade (Donnelly/Manifold 2005, p. 5).

Tariff and non-tariff barriers to trade highly influence global markets in that they restrict competition (Simpson 2005, p. 39). If retailers want to import products directly they have to do customs clearance on their own. The border gets a significant hurdle in this case (SECO 2013, p. 54). There are considerable efforts by the World Trade Organization and trade unions to impede tariff and non-tariff barriers to trade imposed by governments. But they still exist in many countries to protect domestic industries what eventually increases the price level of goods (Paul/Kapoor 2008, p. 239).

### **4.3. Price Discrimination and Arbitrage**

Charging varying prices to different customers for similar products is called price discrimination. Price discrimination serves to skim off additional purchasing power. It can be based on geographical, intertemporal or consumer-specific aspects (Pindyck /Rubinfeld 2009, pp. 510-511). The starting point for price discrimination is separated markets. Price discrimination realized with special offers does not need any physical separation but relies on different consumer segments (Hansen 2006, p. 24).

For geographical price discrimination national borders play an important role. Tariff and non-tariff barriers to trade help to segment markets. Furthermore, national borders are an important aspect when it comes to customer loyalty through services. If for example a product has to be repaired abroad there may be additional cost for customs clearance and you are in a different judicial area. Moreover, intellectual property rights potentially facilitate market segmentation (SECO 2013, p. 54).

In general, three pricing strategies can be applied by internationally operating companies: world-wide pricing (or standard pricing), dual pricing and market-differentiated pricing (Boone/Kurtz 2012, p. 642). These strategies primarily differ in their degree of adaptation to local requirements. If companies choose a world-wide pricing strategy they do not differentiate prices among different markets. The primary reason to choose a standard strategy is a globally consistent image of the brand with commercial spill-over effects. However, a global marketing strategy does not take varying market environments into account. Neither culture, taste nor purchasing power or competition is considered with such a strategy. Taxes, duties, currency exchange rates and other environmental factors make it even more difficult to apply an uniform pricing strategy to all markets (Gillespie/Hennessey 2015, p. 387). A dual pricing strategy distinguishes domestic and foreign prices. Such a strategy normally goes along with cost-plus or full-cost pricing why prices may not be competitive (Boone/Kurtz 2012, p. 642).

On the other hand, there are drivers for local responsiveness. Facing such drivers, companies can choose market-differentiated pricing with even more flexible adaption to local markets. Such a price discrimination strategy facilitates higher gains through skimming off surplus purchasing power because of varying price sensitivity among consumers between countries or regions. Price differentiation further supports the adaptation to local competitors, reduces price transparency, helps to occupy niches and maximize profits (cp. Reichwald/Wigand 2008). Strategies of price differentiation are widely used on the Internet, is it by fixing selling prices through auctions, online shopping clubs or group rebates (Zentes et al. 2012, p. 262). As of the reason of blurry market boundaries, anti-dumping laws and diminishing transportation cost and tariffs, it gets more difficult to enforce regional price differentiation (Bogner 2006, p. 101).

Market-differentiated pricing creates the possibility for arbitrage that is capitalizing on a price difference. Grey markets are a specific form of arbitrage (Zentes et al. 2012, p. 371). In grey markets, commodities are traded legally but not through official distribution channels of the exporter. Grey markets normally only occur if prices differ significantly among countries. If transaction and transportation costs don't outweigh the price differences, retailers are able to generate arbitrage profits in grey markets through parallel, lateral or re-imports. As international price transparency has increased, transport cost declined and markets got more liberal, the number of grey markets soared in recent years (Büter 2013, p. 170). A company runs the risk of damaging relationships with their suppliers when procuring on parallel markets (Zentes et al. 2012, p. 371).

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Another factor in product pricing internationally influenced by governments is corporate taxes. Taxation systems highly vary among countries and there is a threat of double taxation. With transfer pricing among associated enterprises, some companies try to circumvent regulations. Furthermore, currency fluctuation is an important issue in international pricing. The exchange rate risks depend on the volatility of the concerned currency. Exchange rates can be fixed, have a certain fluctuation margin set by political or economic players or fluctuate freely (cp. Diller/Herrmann 2013). If the domestic currency is weak companies have the possibility to stress price benefits and exploit export opportunities. If the domestic currency is strong companies should rather invest in non-price competition by improving quality and after-sales services, as well as buying needed services abroad (Keegan/Schlegelmilch 2001, p. 400).

In practice, MNCs rarely dictate identical prices among countries, they rather establish pricing policies for every country (Gillespie/Hennessey 2015, p. 396). With geocentric approaches, the subsidiary is not given full freedom over price setting but still there is no single fixed price (Doole/Lowe 2012, p. 368). For example, a tolerance for country specific adaptations are fixed tariff lists whereof discounts can be granted (Kreutzer 2013, p. 310). Such price lining strategies are able to set prices relative to rivals. Another strategy of global players is to have global brands and local brands at the same time to exploit the full market potential (Calori/Atamer/Nunes, 2000, p. 34).

## II Results

### 5. Research Design and Methodology

The aim of this thesis is to understand the causes that determine the relatively lower price level of consumer electronics in Switzerland compared to EU countries. As price determination is a complex interaction of multidimensional factors, this study needed to focus on some key aspects. This chapter describes the approach that was used to investigate in this topic. It is divided into three sections. First, the research design will be outlined. Then, research instruments will be presented and finally, the analysis of data gathered will be explained.

#### 5.1. Research Design

According to Corbin/Strauss (2008), the research question determines the methodological approach that is used to conduct a study. The main goal of quantitative research is to get a preferably large sample to generate numerical data out of it. These numerical data are able to establish a relationship between an independent variable and an outcome variable. Qualitative research instead rather helps to discover than to test variables. The samples are generally much smaller and reproducibility of results is lower. The aim of qualitative research is to get an in-depth understanding of a phenomenon and the results are rather descriptive than predictive (Hopper 2011). The choice between qualitative or quantitative research is the highest level of methodological decision to be taken. For this thesis a qualitative approach was chosen. Qualitative research facilitates developing a theory during the research and helps to overcome the gap that often occurs between the findings of quantitative research and what is commonly known about the case.

The first step of this research was to elaborate a theoretical background. The aim was to understand price setting mechanisms and to identify the various influence factors on price. As an outcome of the theoretical background section, several areas were detected that possibly influenced the price differences. Different hypotheses were formulated for each area. Therewith a foundation was laid for an extensive literature review that enabled a structured, focused comparison of the two industries. Referring to Collier (1993, p. 105), *“Comparison is routinely used in testing hypotheses, and it can contribute to the inductive discovery of new hypotheses and to theory-building.”* To understand why consumer electronics are so affordable in Switzerland compared to European countries the industry was compared with another Swiss industry. This industry had to be as similar as possible in regards to the market structures but needed to show a higher price level in Switzerland than in European coun-

tries. Therefore, the apparel industry was chosen for comparison. The apparel industry suits well as a control market for several reasons. First and foremost, the price level for apparel is considerably higher in Switzerland than in EU average. This is a prerequisite for a suitable control market. Then, both consumer electronics and apparel are non-food products that are imported to a large extent. Furthermore, both consumer electronics and apparel are lightweight and small what facilitates simple transportation and storage. These circumstances provide similar market structures of the two product categories.

Two different structured, focused methods of comparison are distinguished. The method used in this study is called the method of difference. John Stuart Mill (1843) was the first to distinguish the method of agreement and the method of difference as methods of academic comparison. The method of agreement compares different instances where the phenomenon occurs. The method of difference instead investigates in two similar instances where in one instance the phenomenon occurs and where it does not in the other (Mill 1843, p. 450). That is, if the dependent variable in a pair comparison once occurs and once does not and the independent variables are equal except for one, in that case the independent variable co-varies with the dependent variable and must therefore be the cause for the phenomenon (Jahn 2013, p. 171). A structured, focused comparison is structured because general questions about the research objective are asked of each case so that data collection is standardized; and it is focused in that the comparison only deals with certain aspects of the cases under examination as it is not possible to display the whole complexity of price determination (George/Bennett 2005, p. 67). The comparison performed in this study is based on secondary sources as well as primary data from expert interviews.

## 5.2. Research Instruments

The research instruments describe the means used for gathering and analysing data. Two research instruments were used in this Thesis, namely a literature review and expert interviews. Onwuegbuzie/Leech/Collins (2012, pp. 7.8) strongly recommend to involve sources beyond print and digital information in qualitative research in order to better understand the phenomenon. Legitimation will be enhanced using multiple sources through between-source triangulation what supports higher validity, and between-source initiation to discover paradoxes that potentially lead to a re-framing of syntheses. The comparison of the consumer electronics and the apparel market is based on various sources for these reasons. Theoretical literature was important to identify frameworks and concepts about price mechanisms in a first step. Then, topical literature, also called grey literature was researched. In addition to published books and articles, grey literature encompasses a broad range of sources from

conference papers, dissertations, magazines, to broadcasts and others (cp. Heyvaert/Hannes/Onghena 2016). Naturally, grey literature is harder to review systematically than just academic articles. Even though a broad range of literature was contemplated each source was assessed regarding trustworthiness, objectivity and reliability. This meta-evaluation helped to decide whether or not to use a source at all or what weight was placed on this source.

The literature review was complemented by qualitative expert interviews. Expert interviews are suited to gather in-depth data that are not easily obtained or available through pre-existing literature. During the interview, specific and closed questions were asked to obtain specific information or to confirm a fact or opinion. Six interviews could be conducted in total. Two interviewees were executive managers of leading consumer electronics companies, namely *Digitec* and *Interdiscount*. Two more interviewees had in-depth knowledge of the CE industry. One was from CE sector association *Swico* (interest group consumer electronics) and the other interview partner was from market-research company *GfK*. Furthermore, two interviews could be conducted with experts from the apparel industry. One expert was from the *Swiss Retail Federation*, the other expert from generalist *Manor*. All six interview participants had many years' experience in the field of consumer electronics and were able to provide valuable insights into the industry. This sample of industry experts provided a broad coverage of both the structures of the CE industry as well as the apparel industry. Five interviews were telephone interviews, one interviewee wanted to answer the questions in written form.

Samples are generally much smaller in qualitative studies than in quantitative studies. More data does not necessarily lead to more information throughout a study, as one occurrence of information potentially is as helpful to understand a topic as many mentions of the same information. The sample still should be big enough to gather every important aspect of a topic. With six interviews, the sample in this study is rather small. But still, the most important aspects were covered.

The interviews were semi-structured with several key questions about five areas, while allowing for unplanned follow-up questions and diverging into other details. The areas that were covered by the questionnaire were retail competition, supply chain structures, cost, trade barriers and strategic decisions. The partial standardization of the questionnaire facilitated comparability. However, in each interview only a part of the questions were posed because the questionnaire was too exhaustive for a one hour interview. While elaborating the questionnaire, three major pitfalls had to be avoided: closed questions, unclear or vague question and too complex question (Maykut and Morehouse 2002). Prior to the first interview a pilot test was conducted to reveal such pitfalls and to determine if there are any flaws or weaknesses to the in-

interview guide and to estimate the time frame of an interview. Interviews took around one hour. The interview guide was further refined and some questions were added during the research process, thus the initial guide from the first interview was quite different from the questions asked in the last interview. The full interview guide is available in Appendix A.

### **5.3. Data Analysis**

The first step of data analysis was to collect as much information on a topic as possible from primary and secondary sources. Primary data didn't exist before, in this case the expert interviews that were conducted. Secondary data otherwise have been published in magazines, books, journals, online portals and elsewhere. Methodological triangulation of data from multiple sources enhances confidence in the findings, as was mentioned. Data triangulation however does neither fully preclude that data could be flawed due to a researcher's bias (Lewis-Beck/Bryman/Liao 2004, p. 1142).

Once the interviews were conducted each area of investigation was considered on its own. All primary and secondary statements on this topic were collected. The data were then analyzed in three steps. The basic level analysis focused on a descriptive delineation of the data. That is, the focus was on what was said rather than on speculations on why or how the phenomenon occurred. Thus, a systematic comparison of the CE and the apparel industry on each aspect was the result of this level of analysis. The qualitative study design allowed for new hypotheses throughout the analysis when a new aspect on a topic emerged. The next level of analysis then had a more interpretative account. The aim was to draw conclusions and inferences on the area under investigation. An integrated view on the compilation of all results was taken and the plausibility of results was evaluated in a holistic and comprehensive way.

In a third step, it was then possible to decide whether an aspect has influenced the price difference between consumer electronics and apparel in Switzerland or not. A precise statement about how much a factor contributes to the price difference is not possible with this study design. That is, the result of this study is a list of unweighted causes for the price differences. A qualitative estimate of the importance of each factor was yet discussed.

## 6. An Introduction to the Consumer Electronics Market

In many ways, Switzerland holds its ground as an island in Europe. This is particularly true for the price level that is considerably higher in Switzerland than in all other countries of the European Union (EU). Switzerland even has the highest price level index of all countries belonging to the Organization for Economic Co-operation and Development (OECD) with 48% higher prices than the average (OECD 2016). This is compliant with the findings of the Swiss Federal Assembly that presented a price level of 41.4% above EA-15 countries' average in 2013. A smaller difference of 16.9% resulted when compared to smaller countries such as Austria, the Netherlands or Sweden (Swiss Federal Assembly 2015a). While the price level index of European Free Trade Association (EFTA) member Norway was higher than Switzerland's during the last decade, Norway's index is decreasing and Switzerland's is increasing. Switzerland surpassed Norway's price level by 13% in 2015 (Eurostat, 2016a). The price gap between Switzerland and the EU widened during the last decade. In 2005, Swiss consumer prices were 38% higher than the EU average (Eurostat 2015), while the price gap added up to 63.4% in 2015, mainly caused by an increased appreciation of the Swiss Franc (Eurostat 2016c).

The website *Preisbarometer.ch* is owned by three Swiss consumer organizations and publishes research on Swiss consumer prices compared to neighboring countries. They found distinctive price differences. For example, toys are 35% more expensive in Switzerland than in Germany, clothes 40%, and cosmetics or magazines even up to 70% (Preisbarometer 2015). As well, barriers of trade are imposed on groceries, what makes them 66% more expensive than in EU average (Demuth 2016). Significant differences also exist between goods and services. While services were in average 60% higher in 2014, the price differences for goods were 25% only. The reason for this difference is higher tradability of goods (SECO 2016b). These price-increasing factors do not apply to the sector of consumer electronics (CE) for some reasons.

### 6.1. Definition of Consumer Electronics

According to a study on behalf of the European Commission, "*Consumer electronics can be viewed as a series of products and services resulting from a consumer-oriented value chain as opposed to one which is business-oriented*" (Nauwelaerts et al. 2000, p. 5). There is a broader and a narrower definition of consumer electronics. The broader definition labels both white and brown goods as consumer electronics. White goods are heavy consumer goods used to be painted in white such as refrigerators, stoves or washing machines. They are also referred to as home appliances.

Brown goods on the contrary were presented within wood or imitational wooden cases (Statt 2004, p. 17), and are used for entertainment, information and communication (Nauwelaerts et al. 2000, p. 9). Brown goods would therefore encompass radios, televisions, video games, computers, tablets, cell phones, printers and many more devices. Spokespersons of a broader definition argue most often from a technical standpoint and state that consumer electronics cover all electronic devices that are intended for everyday use and contain an electronic circuit board (Bali, 2007; Chitode, 2007). On the contrary, an even narrower definition of consumer electronics comes from information and communications technology provider associations such as *swico* (Switzerland), *bitkom* (Germany) and *eito* (Europe). They would further subdivide brown goods and specify mobile phones and tablets as telecommunication; terminal equipment and computers, printers and accessories as information technology (IT) hardware (Dirks/Pols 2016). Thus, consumer electronics, after them, are restricted to televisions, cameras, hi-fi devices, car electronics, portables, satellite receivers and accessories.

This study sticks with the broad definition of consumer electronics as brown goods for practical reasons: there is evidence for this range of products to be more affordable in Switzerland than in the European Union, whereas home appliances were 27% more expensive in 2015 (Eurostat 2016f). Consumer electronics will be compared to apparel. Apparel refers to clothing materials, men's, women's, children's and infant's clothing as well as other articles of clothing and clothing accessories (Eurostat 2016f). Shoes are excluded from this analysis because the shoe industry differs from the apparel industry in central aspects and shows significantly smaller price differences.

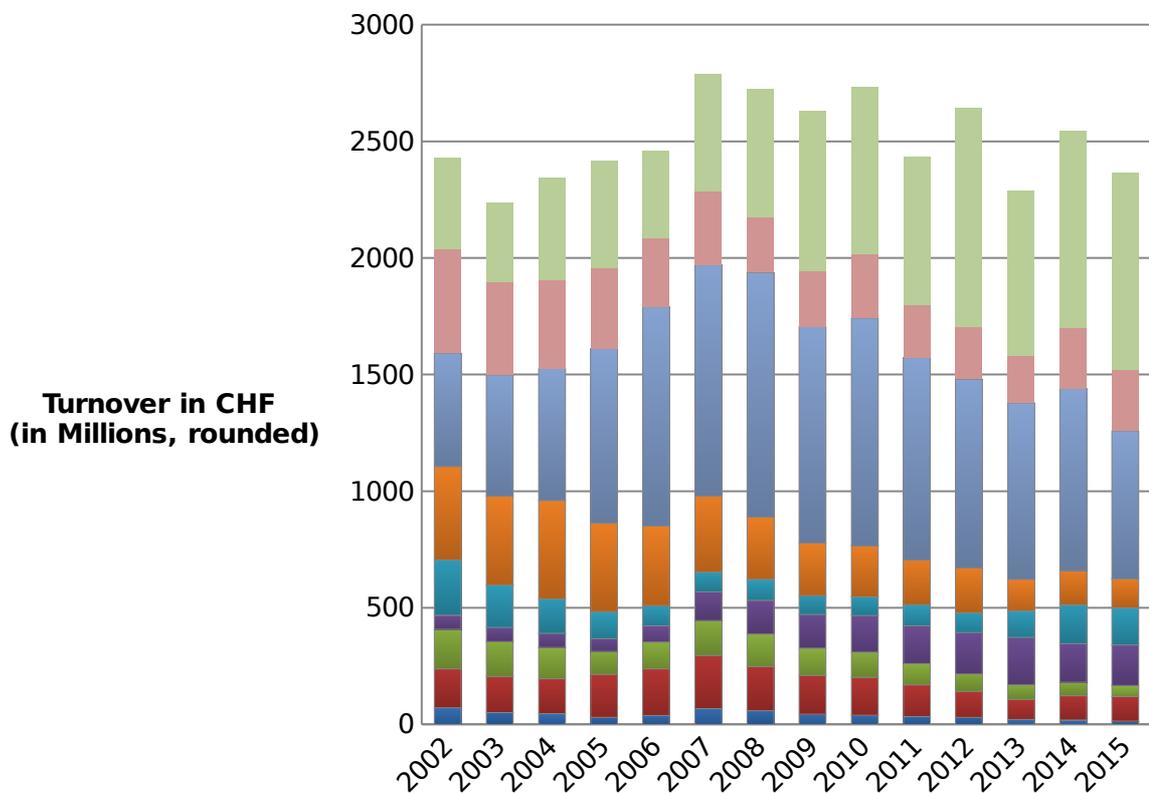
## 6.2. General Price Level, Turnover and Growth Comparison

Generally, price comparisons of consumer electronics are difficult and have to be interpreted with caution. The price of consumer electronics can halve within months due to technological developments, and new products appear frequently. This leads to the fact that price comparisons may represent general trends but have to be understood as a snapshot.

Price comparisons of consumer electronics show clear differences between Switzerland and European countries. The latest numbers from 2014 show that the cheapest Swiss reseller was 12% less expensive than the cheapest German reseller, 21% cheaper than *Pixmania* France and 38% than *Amazon* Italy, the cheapest Italian reseller (Foundation for Consumer Protection 2014). Even retailers with country-specific online shops sell their products cheaper in Switzerland in average (Price Supervisor 2014). This phenomenon is not new. A decade ago, only Bulgaria and Montene-

gro had lower CE prices than Switzerland out of all EU member states (Borchert 2008). The effect seems to truncate in 2015 however. With a CE price level index of 98, Switzerland gets exactly the same score as EA-19, but is still slightly cheaper than in all 28 countries of the EU in average (Eurostat 2016f). With this score, Switzerland ranks above Germany and Austria and equals Italy. Nevertheless, consumer electronics remain the sector with the lowest price level in Switzerland with regard to the observed twelve categories by Eurostat (2016e). Much bigger price differences exist in the apparel industry. The average price level is 34% higher in Switzerland than in EU countries (Eurostat 2016f). Table 1 shows the development of turnover for a selection of consumer electronics.

**Table 1: Development of Turnover in Switzerland**



Sources: SWICO 2015; Wüthrich 2015; Weiss 2014; Weiss 2005; Schnyder 2009; Weiss 2007.

Numbers on personal computers (PC) and notebooks originate from the Weissbuch, an industry analysis performed by Robert Weiss for 26 years until 2014. Since the Weissbuch is proprietary, the data on IT hardware and telecommunication in table 1 are based on secondary sources that cite the Weissbuch. Data on the important CE category of mobile phones were not accessible over the whole period. The data show that the market is saturated in several categories. Particularly large reductions can be observed for televisions. Continuing price deterioration has exacerbated the situation in the industry.

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Exchange rates explain the inflation of Swiss CE products compared to the euro zone: In 2013, the price levels were calculated with an average annual exchange rate of EUR to 1.231 CHF, while for 2015 the exchange rate was 1.067 (Eurostat 2016d), what correlates a price increase of Swiss products and services of 13.8% within two years due to exchange rate fluctuation. Since imports got cheaper from a Swiss point of view, CE retailers reacted with price reductions of -3.7% and restored thus their attractiveness (Feubli, Fuhrer, and Hotz 2016). Since 2010, the turnover with consumer electronics in Switzerland decreased by 1.1 billion CHF (Heim 2017). Similar developments are observed in other European countries (Statista 2017). The market for apparel is likewise significantly decreasing (Häusermann/Wöhlert 2016).

### 6.3. Development of Retail Prices

In the 1970s and 1980s, CE devices were booming in developed countries (Dietrich 2007). Since prices for transistors, microprocessors and integrated circuits dropped rapidly, consumer electronics got affordable to a large number of households. Colored television was invented, PCs got small desktop systems and video games became a mass entertainment medium (Edwards 2012). During these phases of growth, retailers could realize substantial margins on consumer electronics. Even during the 1990s when the Swiss CE market began to be saturated and more competitive, margins were still high (Belz/Schindler 1995, p. 82). Objective price comparisons in the mid-1990s showed that Swiss retailers in the CE sector did not have much higher margins than retailers in other European countries (Larsen 1997, p. 48).

Since then, prices of consumer electronics dropped dramatically. While in 1997 the average price for a PC was 3927 CHF (Steiner 1999), prices experienced a drastic reduction to an average 1563 CHF in 2003 (Weiss 2005), and have now stabilized around 1000 CHF. Another example are tablets, whose prices dropped from 810 CHF in 2012 to 350 CHF in 2014 (Schurter 2015). Between 2008 and 2012, prices of consumer electronics reduced annually by a two-digit percentage in Switzerland (Foundation for Consumer Protection 2014). Since 1995, no other segment decreased prices as much as the CE industry (Federal Statistical Office 2017b). In contrast, the general price level of goods and services for everyday use increased by 11% in the same time period (Rüttimann 2016).

Not only prices of consumer electronics are under pressure. Prices of all non-food sectors including apparel have experienced price reductions in recent years. The price decrease of apparel was strongest in the last seven years with 9.3% (Rüttimann 2016). But still, price-cuttings are most pronounced in the consumer electronics sector with minus 18.6% in the same time period (Jucker et al. 2017, p. 15).

## 7. Intensity of Rivalry among Competitors

The intensity of competitive rivalry has severe impacts on pricing. More competition generally leads to lower prices, more innovation and a greater number of products (Gabaix et al. 2016). Weak competition on the other side is seen as a major cause for high prices in Switzerland (cp. Höhener, 2008). It is disputed why competition is weak in many industries in Switzerland. One argument is that the Swiss market is too small to allow for effective competition. The federalistic political system in Switzerland may divide the Swiss market in even smaller parts.

This chapter will analyze the intensity of rivalry in the Swiss consumer electronics industry and compare them to the apparel industry. Foremost, the amount and relative power of competitors highly influences the intensity of rivalry. Also, the threat of entry is an important factor to be analyzed.

### 7.1. Retail Competition and Market Concentration

A competitive market environment contributes to a large extent to lower retail prices. One aspect of rivalry is the number and relative power of competitors. Several big players compete in the CE market, first and foremost the two biggest Swiss retail companies *Migros* and *Coop*. *Migros* competes in the market with *melectronics* and online market leader *digitec*. *Melectronics* adapts a similar concept as in food stores with cheap private labels. The *M-budget* tablet that sells for only 88 CHF in their online store is an example of such a private label product (Melectronics 2017). *Coop* on the other side competes with *Fust* and *Interdiscount* in stationary retail business and with *microspot.ch* and *nettoshop.ch* in the online market. *Interdiscount* is the biggest pure player in stationary CE business. Furthermore, *Media Markt* is an important player in the Swiss market. For over 10 years, *Media Markt* was market leader in Switzerland until it lost its pole position to *Fust* in 2014 (Filippi 2015). In 1979, the German company opened its first CE store with a large selling space and is today European market leader in CE retailing with 833 stores in 14 countries and sales of over 20 billion euro (Metro Group 2016). The first *Media Markt* in Switzerland opened in the 1990's. In 1990 and 1993, the *Metro / Kaufhof* subsidiary took over *Saturn*. *Media Markt* and *Saturn* were still managed as two separate brands. Even though they remained rivals, *Media Markt* and *Saturn* have many things in common as their aggressive price and advertising strategy (Riekhof 2009, p. 476). *Saturn* also tried to establish itself in Switzerland but was less successful. Their market entry in 2009 took place in a difficult business environment right after the financial crisis hit the economy (Minetti 2011). Only four years later *Media Markt* took over four of six *Saturn* stores after they suffered a loss of up to 20 million Swiss Francs (Parbel 2013).

Not only *Saturn* struggled in the Swiss market, *Media Markt* itself has lost market shares to *Fust*, *Interdiscount* and others in recent years even though they heavily invested in advertising (Rotzinger 2015). In 2016, *Media Markt* realized one third less turnover than in 2010 even though they launched an online shop and opened new stores (Pletter 2014). Therefore, *Media Markt Switzerland* is changing its strategy. They bow out of their vast sales areas of over thousand square meters and rather focus on smaller stores closer to customers (Heim 2017). That is that they want to adapt a similar strategy as *Fust* or *Interdiscount* who both maintain its revenues. This observation is consistent with the tendency in the non-food sector to reduce sales areas (Jucker et al. 2017, p. 26).

Table 2 outlines the turnover and number of stores of the biggest CE and apparel retailers in Switzerland. Where indicated, turnover includes home appliances or other categories beyond consumer electronics.

**Table 2: Turnover of CE and Apparel Companies in Switzerland 2015**

*\*including home appliances, \*\*turnover 2016, \*\*\*turnover 2014.*

| Retail (Consumer Electronics) | Chain   | Number of stores | Turnover in CHF million (2015) | Retail (Apparel)          | Chain | Number of Stores | Turnover in CHF million (2015) |
|-------------------------------|---------|------------------|--------------------------------|---------------------------|-------|------------------|--------------------------------|
| Dip. Ing. Fust AG             |         | 143              | 978*                           | H&M Hennes & Mauritz AG   |       | 66               | 799                            |
| Interdiscount AG              |         | 200              | 945                            | C&A Mode AG               |       | 99               | 521                            |
| Media Markt                   |         | 28               | 888*                           | Zalando                   |       | -                | 424**                          |
| Digitec Galaxus AG            |         | 9                | 640**                          | Charles Vögele Holding AG |       | 163              | 334                            |
| melectronics                  |         | 108              | 577*                           | Brunschwig & Cie.         |       | 17               | 211                            |
| Mobilezone AG                 | Holding | 129              | 388***                         | Schild AG                 |       | 45               | 183                            |
| BRACK.CH AG                   |         | -                | 201*                           | PKZ Burger-Kehl & Co. AG  |       | 39               | 176                            |
| Microspot AG                  |         | 3                | 173**                          | Chicorée Mode AG          |       | 153              | 144                            |
| Steg Electronics AG           |         | 16               | 100                            | Esprit Holdings Limited   |       | 76               | 135                            |
| EP: Electronic Partner        |         | 53               | n/a                            | Mode Bayard AG            |       | 77               | 109                            |
| Data Quest AG                 |         | 21               | n/a                            | Tally Weijl AG            |       | 85               | 90                             |

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Sources: *Retailers' Websites; Statista 2017; Aiolfi 2016; Rotzinger 2016; Carpathia 2016; Kneubühler 2015.*

The market for classic consumer electronics gets further treated successfully by furniture retail chain *Conforama* and generalist *Manor*. A generalist has more than two different assortments whereof none has an assortment share of over 66% in turnover (Kessler/Hochreutener 2014, p. 23). Also, German food retailer *Aldi* shakes up the CE market with bargain buys. They offer only few products but at an aggressively low price (Hediger 2016). In the IT and photographic segment of consumer electronics specialized traders are widespread. *Data Quest, mobilezone* and *Electronic Partner* are main players in this field. Then there is PC assembling specialist *STEG electronics* who serves another market niche. These specialist retailers have a strong local bond with a distinct assortment and are known for extended service offerings as for example individual consultation at home (EP Schweiz 2017). According to Giuriato (cited in Stünzi 2013), the density of trades is as high as scarcely anywhere else in Europe.

The online market for consumer electronics is characterized by big players on the one hand such as *digitec, brack.ch* or *microspot.ch*, and a broad and fragmented field of niche players meanwhile big players grow faster than niche suppliers (Kessler/Hochreutener 2014, p. 22). In recent years, turnovers in the stationary retail sector are descending in favor of online sales. The online share of all CE sales was 26% in 2015. This is by far the highest value of all sectors, followed by apparel with a 15% online market share (Jucker et al. 2017, p. 12). The segment of photographic appliances seems especially under pressure. Two third of specialist shops that existed at the start of the new millennium disappeared in favor of online competitors that have a market share of 50% (Clemenz Berger 2016). Some of the big stationary retail chains do well online but certainly not all of them succeed with their online shop. Online market leader for consumer electronics *digitec* generates 640.1 million CHF in turnover. This is over three times more turnover than the second biggest online retailer generated. *Digitec* was a start-up by 2001. Eleven years later, *Migros* acquired 30% equity in the company for 40 million CHF (Kyora 2014), since 2015 *Migros* is holding 70% of the company (Filippi 2015). The success of *digitec* is based on an early-mover advantage in terms of an unusually user-friendly online shop.

The CE market has experienced strong forces of market concentration. Trigger to this development is on the one hand endogenous growth through further branch expansion and on the other hand exogenous growth through mergers and acquisitions, mainly by *Coop* and *Migros* (Heri, 03.03.2017, para. 11). For example, *Fust* expanded its business quickly since 1998 by acquiring *Service 7000, ElectroPlus, Portable Shop, Rediffusion, Eschenmoser* and *Darty Switzerland*. In 2007 then, *Fust* was

acquired itself by food retailer *Coop* (Fust 2017). However, also in a highly concentrated market, leading actors may fight a price war. Thus, a high concentration of suppliers does not necessarily lead to higher prices (Zentes/Swoboda/Foscht 2012, p. 49). The Swiss CE market shows aspects of price wars. Giuriato (12.05.2017, para. 44) even speaks of ruinous competition where no one makes acceptable profits. Quite likely some competitors offered a part of their assortment below acquisition prices to gain market shares (cp. Bolzli/Castritius 2015).

Interestingly, low prices played an important role in the Swiss CE market before the market entry of Media Markt in 1994. According to Larsen (Larsen 1997), “*Interdiscount, Eschenmoser, Fust and Migros all strove to be the price leader, but all focused on different measures or instruments in order to differentiate themselves*”. Even though the market was yet competitive in the 1990s, margins were not remarkably under pressure until the mid of 2000s. 2004, an industry insider claimed margins to be 30 to 50% for specialist shops (Schneider 2004). Today, the CE sector works with so little markup that participants of the e-commerce Report Switzerland think that they cannot drop any further (Wölfle/Leimstoll 2016, p. 8). Competition is further intensified by the fact that all CE retailers compete in the same product range with little room for differentiation. Many online shops therefore already expanded their assortment to domestic appliances and recreation-oriented products where higher margins are realized.

The Swiss apparel market is dominated by three major retailers in the stationary business, Swedish company *H&M*, German-Belgian company *C&A* and Swiss retailer *Charles Vögele* who was recently taken over by Italian company *OVS*. Alongside there are numerous medium-sized brands such as *Manor*, *Brunschwig*, *PKZ*, *Chicorée*, *Esprit* or *Schild*. Next to them there is a fragmented field of small apparel shops. There are more apparel stores in Switzerland than food stores in Switzerland (Kobler 2014). Furthermore, online market leader *Zalando* gained substantial market shares and currently ranks on third place with regards to turnover. The market entrance of *Zalando* has significantly intensified market pressure and has also led to an increasing share of online sales. There is no Swiss retailer that could yet profit from the online boom; the field was almost completely left to the German company. The next bigger online shops for apparel only constitute a fraction of *Zalando's* market shares. While the CE market is dominated by Swiss companies, foreign competitors play a more important role in the apparel market. Around 60% to 70% of apparel sales are made by foreign companies (Kessler 2016, p. 35). Thus, competition in the Swiss apparel market is international. A Swiss apparel company is in competition with rivals from all over Europe (Jenni, 08.06.2017, para. 51). Foreign competitors have price advantages due to the appreciation of the Swiss Franc and are better able to

profit from economies of scale. This fact has led to an increasingly competitive environment in Switzerland. Prices range 8% lower today than 1995, while average prices for daily goods rose by 11% in the same period (Rüttimann 2016). Regarding to price formats, a polarization between premium shops and discounters occurs (Aiolfi 2012). A large number of retailers sell undifferentiated products to low prices, but there are also high-valued brands that are able to demand premium prices.

Some more factors enhanced competitive rivalry in the Swiss apparel industry. Similar to the CE industry, the apparel market is largely saturated (Aiolfi 2012). Then, the apparel industry suffers from shopping tourism due to lower prices in neighboring countries. It was estimated that sales losses amounted to 1.4 billion CHF in 2015 (Rudolph/Nagengast/Nitsch 2015). This number does not include online sales of foreign competitors, notably *Zalando*. The growing concurrence from e-commerce is further intensifying competition (Rüttimann 2016). Thus, Jenni (08.06.2017, para. 51) describes competition in the Swiss apparel market as more intense than in neighboring countries and margins to be very low. This is why a drastic process of market concentration is in progress. Several retailers already had to close or reduce the number of their shops in Switzerland. *Switcher*, *Blackout*, *Pasito Fricker*, *Bernies* and *Companys* all had to file for bankruptcy (Jucker et al. 2017, p. 23), and *Charles Vögele* was taken over by *OVS* (Schmutz 2017). These crowding-out processes mainly happen at the expense of small boutiques and medium-sized enterprises (Asamer 2012). This market concentration processes have already happened in the CE industry earlier. The apparel market develops in a similar way as the CE market but with a delay of some years. Another sign of harsh competition is a lower seasonality of products (Bloch, 11.06.2017, para. 58). That is, periods of clearance sales are much longer today than some years ago (Jucker et al. 2017, p. 1).

Retail competition in both the CE and apparel industry can be described as very intense. Even though competition is harsh both in the CE and apparel industry, some retailers in the apparel industry are able to set their prices higher in Switzerland than in the EU. For example, while price differences between Switzerland and neighboring countries at *Vero Moda* were 16% in 2014, it were 39.1% at *Zara's* (Foundation for Consumer Protection 2014). What's more, exchange rate related price benefits are not always passed on to consumers by apparel companies (Rüttimann 2016). Lower price transparency in the apparel industry has a negative effect on retail competition, as will be discussed in detail in chapter 9. It is furthermore easier to create a premium brand image for apparel. Consumers are less price sensitive with premium brands. Therefore, the intensity of rivalry is slightly less strong than in the CE industry.

## 7.2. Threat of Market Entry

According to Porter's five forces (Porter 1980), the threat of new entrants to the industry is another force that shapes the competitive environment. New market participants see potential to make profits and often enter a market with considerable financial assets. Therefore, new entrants are able to exert downward pressure on price or to increase cost for established market participants (Porter 2013, p. 41). Low barriers to entry decrease profit potential of existing competitors and thus makes an industry more competitive (Wilkinson 2013). There are several barriers that may threaten an enterprise to enter a market. On the contrary, the absence of barriers attracts new entrants to an industry.

Structural barriers to entry result from efficiency of current competitors. If enterprises have gained cost advantages, economies of scale and scope or could successfully differentiate themselves, they could impose market entry barriers therewith. In general, barriers to entry are higher for stationary retail business than online because of fewer rental and staff cost. Especially for start-ups it is therefore attractive to offer their products online only. This has contributed to a market structure with few big players that dominate stationary business and hundreds of niche suppliers that favor the online retail chain (Langer 2014). A study could show that the entrance rate, that is start-ups divided through the number of enterprises, tends to rise with an increasing share of online sales (Keating et al. 2015, p. 23). From this perspective, market entry barriers should be lowest in the CE sector with the highest online sales shares. Currently, only few foreign retailers compete in the Swiss CE online market. Harsh competition and low margin are possibly the highest threat for a market entry. The failure of *Saturn* to succeed in the Swiss market shows that it is difficult for foreign enterprises to establish themselves. The online market is as well dominated by Swiss companies with a strong local focus (Bolzli/Castritius 2015). Having said this, the market entry of foreign companies, above all *Media Markt*, has intensified competition since the 1990s.

Heri (03.03.2017, para. 13) expects more foreign competition especially in the online market, for example by a market entry of *Amazon* or *Alibaba*. If *Amazon* enters the market, their assortment would be much broader than that of any other retailer. The threat of such a market entry leads retailers to emphasize even more on proximity to customers and service quality (Späni, 10.05.2017, para. 42).

Meanwhile in the Swiss apparel market, stationary as well as the online market are dominated by foreign competitors while Swiss retail chains following behind. The Swiss market is attractive to foreign competitors due to the higher price level in Switzerland. The harsh competitive environment and market saturation alleviate the

attractiveness however. Therefore, the threat of market entry is expected to be similar or higher in the apparel industry than the CE industry. The threat of new entrants therefore does not explain the low price level of consumer electronics in Switzerland.

## 8. Bargaining Power of Suppliers

The bargaining power of suppliers is one of the most important factors when it comes to price determination. Powerful suppliers may threaten the industry to raise prices or to reduce quality (cp. Porter, 1998). Therefore, differences in bargaining power of suppliers potentially explain price differences between the CE and apparel industry.

Hill/Jones (2009, p. 53) resume the influence factors on bargaining power of suppliers: Suppliers are more powerful if their concentration is high, if there are few substitute products and switching costs are high for retailers, if profitability of suppliers is not significantly affected by retailers, and if retailers cannot threaten suppliers by entering their business. This chapter analyzes the market power of supply chain participants on these factors in three sections. The first section describes the supply chain structures, the second analyzes anticompetitive agreements and legal requirements, and finally the threat of substitutes and supplier switching cost are outlined.

### 8.1. Supply Chain Structures

The CE supply chain comprises multiple actors, from manufacturers, logistics service providers to distributors, wholesalers and retailers. Production of consumer electronics takes place throughout the world. A particular high concentration of CE manufacturing activity is found in Japan, South Korea, China and the United States (Kerry et al. 2010, p. 6). Manufacturing and installation increasingly focuses on few companies in aforesaid countries. Gläser (2014, p. 241) describes the structure of CE manufacturing as oligopolistic. There are high market entry barriers imposed by initial investments, short innovation cycles and harsh competition. These circumstances have led to a relocation of production to low-income countries, to rationalization and company mergers. However, big actors on this trade level such as *Samsung*, *Apple*, *Sony* or *LG* were not able to expand their leading position and were subject to major fluctuations (Wulf/Reineke 2012, p. 6). Thus, there are a limited number of manufacturers that act with a high aggressiveness in the market.

Compared to apparel and other industries, the share of multi-national market participants in the CE industry is exceptional. The migration of CE manufacturing companies to low cost countries in Asia has extended supply chain structures with an increasing number of channel participants and with varieties for different product categories (Kerry et al. 2010, p. 9). Products of the IT segment like PCs, notebooks and

tablets traditionally have different supply structures than classic consumer electronics like televisions or DVD players. In the IT segment, broadline distributors are common. They carry a broad variety of products of different manufacturers and have high logistical competences. Such broadline distributors are placed between manufacturers and retailers or specialized shops. The Swiss *Also Holding* is the leading broadline distributor in Switzerland, Germany and five other European countries and has a portfolio of over 16'000 products of 350 different manufacturers (ALSO 2017). In classical CE supply chains it is more common that a manufacturer has a local factory representation agency to distribute their products. Normally, there are one or more general importers per brand. Or products are procured through associated groups with a central warehouse. IT distributors are generally more efficient than such associated groups (Kühn 2006).

In the last decade however, supply chains of the IT segment and classic consumer electronics converged more and more. Indirect channels were able to reduce their cost radically and to boost efficiency (Hugenschmidt 2009). Also procurement is much more international than some years ago, especially for branded products. The market concentration on the level of intermediaries is low (Späni, 10.05.2017, para. 36). That is, CE retailers have a broad variety of different sources for their products. For convenience, retailers consider local subsidiaries in the first place (Heri, 03.03.2017, para. 7) but if they demand much higher prices the goods will be procured on international markets. The biggest part of the assortment is therefore procured abroad where prices are cheaper (Späni, 10.05.2017, para. 35). Low margins force CE retailers to purchase their goods as cheap as possible what consequently enhances the competitive rivalry on the level of distributors.

The supply chain structures in the apparel industry differ from the CE industry. The bargaining power of manufacturers is small since fashion companies mainly source their products from low-income countries which gain only small parts of the profit and that are dispensable. The apparel goods take different supply chains from there on. Brands like *Nike* or *Adidas* have European headquarters and then one or several importers in each country. These importers supply Swiss retailers. Often, several fashion brands are consolidated under one roof to profit from economies of scale. A prominent example is the Spanish company *Inditex*. Furthermore, there are independent importers who assemble own collections under private labels. They order their products directly from the manufacturer. Also, retailers may have own procurements teams as for instance prevalent at *Migros* or *Coop* who would also procure their products from manufacturers (Bloch, 11.06.2017, para. 62). Moreover, there are still around 200 companies that produce apparel in Switzerland. They primarily focus on niches, high quality and design (Swiss Textiles 2017).

A noticeable trend in the CE and as well as in the apparel supply chain is growing disintermediation and activities of direct distribution. Direct distribution is more common in the apparel industry than in the CE industry. The market for direct distribution in both industries is still in developing stages and currently is not cannibalizing retailers but rather complementing them (Feubli/Fuhrer/Hotz 2016, pp. 22-23). Moreover, a trend for vertical integration and progressive advance of chain stores are obvious in the apparel industry. Leading fashion chains want to control preferably the whole supply chain which leaves more margins for themselves and helps to react faster and more cost-efficiently to new fashion trends (Aiolfi 2012). Vertical integration is already at an advanced stage in the apparel industry. Trade associations that reach market power through bundled demand on the other hand have problems to sustain their position because of inert reactions to trends. They also fail to integrate vertically. More than eight trade associations are active in the European apparel industry, and at least five trade associations cope in the CE business (Flögel/Gärtner 2014, p. 22).

## 8.2. Anticompetitive Agreements and Antitrust Law

Many countries implement antitrust law and other measures to limit market power of suppliers. The revision of Swiss antitrust law in 2003 has led to a tighter handling of obstructions to competition. Antitrust law prevents vertical agreements over minimum and fixed prices as well as agreements for territorial protection ever since (SECO 2016b). It was very common to keep prices artificially high in the Swiss CE market before legal regulations were tightened (Späni, 10.05.2017, para. 36). Still, suppliers try to prevent parallel imports with different means. Price discrimination is only possible if suppliers succeed to segment markets.

A much-noticed case where the Swiss competition commission has sentenced a CE company was the fine against *Nikon*, a camera manufacturer. *Nikon* has hindered parallel imports with sanctions against distributors and stipulated import and export bans (Fontana 2016). This sentence had a deterrent effect on other companies in this sector (Späni, 10.05.2017, para. 36). In the apparel industry antitrust legislation has not much impact up to date because a single fashion brand is not market dominating in antitrust sense. Retailers normally follow non-binding price recommendations (Flögel/Gärtner 2014, pp. 45-46). Otherwise they risk to be sanctioned with denials of delivery in the future (Bloch, 11.06.2017, para. 64). Such anticompetitive behavior is in contravention of antitrust law. However, law enforcement in the case of delivery refusal is unsure and in any case complex (SECO 2013, p. 55).

The internet offers new opportunities for consumers to purchase goods directly abroad what is another form of parallel imports. However, such imports are often restricted by geo-blocking and export bans. Some foreign online shops do not serve

Swiss consumers to Switzerland to reinforce higher prices on their Swiss websites. The Swiss competition commission brought a German home electronics retailer to quit this practice. However, there is no strong legislation on geo-blocking yet. The EU commission is currently discussing a stricter legislation concerning geo-blocking, and Switzerland would possibly adopt this legislation (Swiss Federal Assembly 2017, pp. 169-170). Up to now, geo-blocking is a common practice especially in the apparel business. Furthermore, in some cases fashion brands discriminate multi-channel strategies of retailers by not delivering them when they maintain an online shop (van Paesschen/Vis 2015).

But there are also legal frameworks that give an advantage to Swiss businesses. Switzerland applies international exhaustion for trademark law. Other than in the EU, there is no restriction for parallel imports whereas the EU allows parallel imports only in the European Single Market (SECO 2008, p. 207).

### **8.3. Threat of Substitutes and Supplier Switching Cost**

In some industries there is a threat of substitutes that lowers bargaining power of suppliers due to serious alternatives. A similar product from a rival is not a substitute. A substitute is a different product that a consumer could choose instead of the industry's offer (DePersio 2016). The threat of substitutes can be described as low for both the CE and apparel industry. All substitution in the apparel industry is competition. There are alternatives in the CE industry though, like a book could substitute television. However, these are not really alternatives to most consumers. Therefore, substitutes impose no threat on suppliers.

Supplier's power is weak if it is easy for retailers to switch their supplier. CE retailers do not fear any direct sanctions of suppliers when switching supplier but such a step would certainly influence a potential future business relationship in a negative way (Heri, 03.03.2017, para. 8). According to Heri (03.03.2017, para. 8), a supplier switch would be absolutely unproblematic and executed within a short time span. The decisive aspect of such low switching cost is high price transparency in procurement. It was not always the case that price transparency was high however. In a long-lasting process, suppliers were confronted with price differences on comparable products to impose pressure on them. This process has led to transparent supplier prices that are easy to compare (Späni, 10.05.2017, para. 36). Swiss retailers try to find the best purchasing price in the international market place. As mentioned, the greater portion of the assortment is therefore obtained through unofficial trading channels abroad (Heri, 03.03.2017, para. 3-5).

Nevertheless suppliers still try to discriminate prices among different markets. For example, the local subsidiary may grant five years of warranty while in international markets it is only three years. Retailers then usually offer both products, the cheaper product with shorter warranty time from unofficial channels for more price sensitive customers and the product of the official local subsidiary with longer warranty for less price sensitive customers. Another means to support the official trading channel that some suppliers established is cashbacks. Only after selling a product you will get a provision of the supplier as an incentive to use the official trading channel (Späni, 10.05.2017, para. 37). Also, companies like *Samsung* offer cheaper EU models with less functionality and more expensive models customized for a country to impede cross-national trade (Straßburg 2013). Other means of manufacturers to increase switching cost are partner programs that contain certifications and trainings (Sarpong 2012).

Even though suppliers try to discriminate prices in different markets high competitive rivalry among them and high transparency in procurement diminishes their bargaining power. In addition, retailers that are in business throughout Europe like *Media Markt* would have a potential for arbitrage when manufacturers tried to discriminate prices among countries (SECO 2008, p. 206). This would not be tolerated. What further reduces switching cost for retailers is low product differentiation in the CE industry.

Switching costs for retailers in the apparel industry instead are much higher. Parallel imports of branded clothes are difficult to realize. Importers provide important services such as customs clearance, returns handling and customer support. Also, they normally offer turnover bonuses and contributions to advertising cost (Bloch, 11.06.2017, para. 64). Furthermore, trade in this segment is characterized by low price transparency. One reason is that apparel is often distributed without product names. Comparability is therefore not given. Private labels play an important role in this segment. This enables suppliers to differentiate themselves over the assortment. While CE retailers have very similar assortments, apparel retailers address particular customer segments.

Overall, bargaining power of suppliers in the CE business is much weaker than in the apparel business. Therefore, it is much more difficult for CE suppliers to charge a premium in Switzerland or to establish anticompetitive agreements.

## 9. Bargaining Power of Consumers

Bargaining power may not only be played off by suppliers, also consumers may possess bargaining power to lower prices of a product. If bargaining power of consumers is high, they are able to put companies under pressure to reduce their prices. A study by the price supervisor (2014) has found that competition is not sufficient to lower prices in Switzerland. Market characteristics with regard to consumer behavior may have great importance. Thus, higher bargaining power of consumers in the CE sector compared to apparel could possibly explain price level differences.

In Switzerland, demand for consumer electronics is widely saturated and only increases with growth of the general population (Keating et al., 2015, p. 25). The same is true for apparel. While demand for food raised 20% and for health and body care 36% between 2002 and 2012, demand for apparel raised by mere 2% (Aiolfi 2012). Also in more recent days, there were no new impulses to demand for apparel (Möckli 2016). A condition of saturation of consumer demand goes along with an increased pressure on prices.

Not only market saturation influences bargaining power of customers. Four more aspects will be highlighted in this chapter: price transparency, price sensitivity, loyalty as well as service and standards of quality.

### 9.1. Price Transparency

Price transparency indicates how well prices can be compared among different suppliers. Customers have lower search and assessment cost if transparency is higher (Diller/Herrmann 2013, p. 309). Price transparency also reduces price elasticity, that is undercutting prices of competitors has more positive impact on sales (Simon and Fassnacht 2008). Price transparency enhances competition due to lower switching costs of buyers and is therefore able to reduce the price of a good.

Orientation on price is generally higher in online shops than in stationary shops (Keating et al. 2015, p. 22). Due to comparison portals, cheapest retailers are easy to find online and price transparency is enhanced compared to stationary shops. Even small price differences thus generate competitive advantages what especially benefits discounting strategies. The cheapest offer determines the market price (Hofmann 2013). Moreover online prices have a spill-over effect on stationary shops. Their prices generally come under pressure with an increasing online market share (Keating et al. 2015, p. 22). Some customers search the internet for the cheapest price on their mobile phone while shopping in a stationary store to bargain with the seller or to get consultation and then buying the product online (Pöschl 2013). A

quarter of all customers have informed themselves online about prices before shopping stationary (Competition Commission 2011, p. 7).

Consumer electronics are predestined for online trading. Most quality criterions are simple to measure and present, as for example the memory of a hard disk or the resolution of a camera. The quality of a production line is usually stable. A quality control in a stationary shop can therefore be relinquished (Feubli et al. 2015). This is different for apparel. There is a considerable danger that an item of clothing does not fit or does not have the expected quality when shopping online. Comparability is therefore lower in the apparel industry than for consumer electronics. Several more factors influence differences in price transparency. Clothing products are often no-name products what further reduces comparability. Manufacturer's brand orientation of customers is partly low, especially for shoes (Flögel/Gärtner 2014, p. 45). This enables competitors to differentiate themselves with their assortment what facilitates price discrimination. This is different for consumer electronics. There is a significant orientation on manufacturer's brands and almost no no-name products and own labels. Luca Guirriato (para. 49) sees lower price transparency in the apparel industry as an important factor for the price difference. High levels of price transparency of consumer electronics compared to apparel therefore explains to some extent why the price level is lower for consumer electronics.

## 9.2. Price Sensitivity

Price sensitivity of customers is another factor that shapes demand. The higher price sensitivity of customers is, the more pressure is put on prices. This is backed up by the argument that some products that are produced in Switzerland are sold for a cheaper price abroad (Price Supervisor 2014).

Price sensitivity varies substantially among countries and obviously among different customer segments. Generally speaking, price sensitivity is highest in Eastern and Southern Europe and lowest in Scandinavian countries. Western Europe shows heterogeneous consumer behavior. Swiss, Dutch and Belgian consumers have a low orientation towards cheap prices while Germans, French and Austrian consumers are more price sensitive (Krafft et al. 2015, p. 176). Switzerland is considered as a country with relatively many special promotions. This can be interpreted as an attempt of retailers to approach more price sensitive buyers without losing returns from less price sensitive customers (Schöchli 2012). However, Swiss consumers got more price sensitive with the appreciation of the Swiss Franc (Kobler 2014). In 2015, Swiss consumers shopped cross-border for 11 billion CHF due to the devaluation of the euro (Jurinak 2016). Pressure of cross-border shopping is not equal for all product categories. For more expensive products such as cars a price difference of 5% will

already foster cross-border shopping (Pfister 2015). Price differences have to be bigger the cheaper the product is to provide an incentive for cross-border shopping. There are expenses to consumers by geographical distance and by changing the market. Cars excluded, Swiss consumers in particular shop apparel abroad, followed by food and near-food products (Hochreutener 2013). Consumer electronics on the other side are not prone to cross-border shopping thanks to a comparable price level (Spitaleri 2016). Hence, cross-border shopping puts marginal pressure on prices for apparel but barely helps to equalize price differences among neighboring countries and Switzerland.

Another thesis is that Swiss people are more tech-savvy than others and are better able and more willing to hunt for low prices of consumer electronics. A study by the World Economic Forum has ranked Switzerland second on technological readiness (Myers 2015), and almost no other nation spends so much money on technology as Switzerland (Müller 2014). A study by BAK Basel conducted 2011 found that Swiss consumers react very sensitive to price changes for the product category of cameras (BAK Basel 2011). An expert from *digitec* however claims that there is no pressure on prices from price sensitive customers (Heri, 03.03.2017, para. 28). Price sensitivity therefore rather reduces the price gap between consumer electronics and apparel due to the high level of cross-border shopping of apparel.

### 9.3. Brand Loyalty

The creation of a brand loyal customer base might be the only option to maintain or gain market shares in a highly competitive environment (Hill/Schilling/Jones 2016, p. 47). The establishment of appealing brands helps to enhance market power what allows for above-average prices (Brasche 2013, p. 93). On the other hand, the choice for a product is rather determined by price and service when a product is perceived as a commodity. The proposition is therefore that brand loyalty is weaker in the CE industry than for apparel what could explain a part of the price difference.

15 years ago, consumers showed a high affinity for CE brands and a rather distrustful attitude towards own-brand strategies. Specialist shops emphasized on exclusive products (Flögel/Gärtner 2014, p. 41). The brands *Loewe* or *Bang & Olufsen* for example succeeded with a distinguished design and noble packaging for their tube televisions what made them a gem in every living room even though they bought them from mass manufacturers *Philips* or *Thomson*. Consumers were willing to pay double as much for the branded product as for comparable devices (Kerbusk 2004). Also in more recent days, Swiss seem to appreciate high quality products. This is highlighted by the hype around *Apple* products that are positioned in the premium segment. In 2011, there were approximately an equal number of *iPhones* registered in Switzer-

land and in Germany, a country with *nota bene* ten times more inhabitants (Lang/Ebnetter 2012, p. 9). While *Apple* has a reputation for high quality, products from China suffer from reservations with regard to their quality even though this is where their strengths lie (Fritsche 2016). This brand loyalty may impose a barrier to enter the Swiss CE market for some retailers.

But the dominance of *Apple* began to totter. Chinese newcomers show considerable growth rates. However, brand loyalty is still seen as a market entry barrier. Especially consumers that are less comfortable with technology have retentions towards Chinese products as regards quality (Fritsche 2016). Loosli (10.03.2017, para. 30) observes an increasing devaluation of consumer electronics that shifted from status symbols to commodities. He expects no-name products to further gain market shares and associated therewith a stronger focus on low prices. When it comes to retailer loyalty, customers behave more disloyal on CE online shops than with other product categories like apparel due to higher price transparency (Fienert 2013). In the apparel business, polarization between no-name products and premium brands is more accentuated (Aiolfi 2012).

Thus, higher expectations on quality make it possible to create strong premium brand images in Switzerland. On the other hand, there is a low-price segment with disloyal customers in both industries. More in-depth research would be needed to quantify brand loyalty of both industries. From this comparison, brand loyalty is not expected to influence the general price level of consumer electronics compared to apparel significantly.

#### **9.4. Standards of Quality and Service**

In the discussion about the high price level in Switzerland, higher quality is often said to be a factor that justifies an increased price level (Judd 2016). Quality has two aspects: there is service quality and quality of a product itself. Transparency and comparability of quality is an important aspect to prevent market segmentation and price discrimination (Price Supervisor 2014, p. 5).

With regards to quality of a product, consumer electronics are absolutely identical in Switzerland and European countries (Heri, 03.03.2017, para. 18). However, the assortment differs. For example, the average size of a television is much higher in Switzerland than in Spain (Späni, 10.05.2017, para. 38). Generally speaking, the Swiss consumer sets high values on quality. This is equally true for apparel. The Swiss consumer is classified as one of the most demanding customer all over Europe (Guggisberg 2016). Swiss consumers are more sensitive to corporate governance and fair trade products than their European counterparts (Jenni, 08.06.2017,

para. 54). Hard discount concepts that are very popular in Germany and other European countries were not successful in Switzerland (Bloch, 11.06.2017, para. 70).

Also service quality can be used to segment markets or to discriminate prices between different nations. The supply chain for consumer electronics is at an advanced stage when it comes to e-commerce compared to apparel. Other than in the Swiss fashion industry, product availability is high and next-day delivery is an industry standard (Wölfle/Leimstoll 2015, p. 24). Cross-channel strategies are similarly important in both industries (Heinemann/Gehrckens/Wolters 2016, pp. 282-283). Many CE manufacturers offer a higher standard of service quality in Switzerland than in the EU as for example extended warranty (Heri, 03.03.2017, para. 18). When it comes to shipping and return conditions however Swiss retailers have worse conditions than their European counterparts. Swiss apparel retailers invoice shipping costs most often. Returning items was free in only five out of hundred online shops under examination (Kölliker 2016). Furthermore, an erosion of service could be observed in recent years. Especially younger customers are more willing to renounce services. Higher price transparency and decreasing prices have contributed to this fact (Bloch, 11.06.2017, para. 70).

Indeed, Swiss consumers demand for higher quality products. Thus, the assortment of a Swiss CE or apparel company is different in Switzerland than in European countries. It remains unclear, if service quality is higher as well. Since consumer behavior is not different for consumer electronics and apparel, standards of quality and service do not explain the price gap between consumer electronics and apparel.

## 10. Strategic Decisions and Innovation

Company-internal pricing decisions determine if the price of a product is determined by competition, demand, cost or a mix of these factors. Thus, strategic decisions influence the general price level in an industry. Three areas of strategic decisions will be discussed in this chapter. First, innovative drive of the whole industry will be analyzed. Further the use of Switzerland as a test market is discussed, and finally the common pricing strategy of loss-leader offers.

### 10.1. Innovative Drive

In the last decade approximately, a new development was starting to shake up the consumer electronics industry, growing interconnection of IT and consumer electronics. For example, the upcoming MP3 player was a classic IT product that captured the consumer electronics market, and DVD players were equipped with 400 gigabyte drivers and Ethernet-Ports (Schneider 2004). Today, IT hardware and consumer electronics are not dividable anymore. Many traders of consumer electronics feared this development of interconnection for a good reason. Margins in the IT hardware business were 3 to 15% and thus strikingly lower than in the consumer electronics business (Schneider 2004). This convergence therefore resulted in a global downward pressure on margins of consumer electronics. Consolidation of IT hardware and consumer electronics had big impacts on the competitive situation in the consumer electronics market.

The consumer electronics industry is known today as a highly dynamic industry. The speed of new product developments is outstanding. The industry is characterized by high market dynamics and short innovation cycles. This causes a pressure of marketing to refinance development investments. As a consequence, availability of products and variants rises constantly in numbers and prices for consumer electronics decrease constantly at a fast rate. A notebook for example cannot rest longer in a shelf than four to five months until follow-up models appear (Späni, 10.05.2017, para. 39). This early replacement of products results in price drops.

Consumers thus profit from a competitive global marketplace that emphasizes on fast innovations. As a result of an increasing digitalization and increasing productivity, production got less demanding also for no-name manufacturers what has led to overcapacities in some areas (cp. Clausen 2013). At the same time, consumers replace devices that are still working.

Consumer electronics are characterized by fast pace and high interchangeability. Patent legislation therefore plays a tangential role. The apparel industry on the other

hand is similar to consumer electronics in that it also faces constant changes and new trends.

A particularity of the apparel industry is seasonality. Apparel succumbs devaluation through fashion cycles (Flögel/Gärtner 2014). However, seasonality has flattened in recent years. The average price difference between the month with highest prices and the one with lowest prices decreased from 14.6% to 10.4%. The rebate policy of fashion companies is decisive for this trend. Periods of clearance sales are longer than some years ago. This can be attributed on the one hand to intensified competition, on the other hand to shorter product lifecycles. This pressures fashion companies to replace their assortment faster (Jucker et al. 2017, p. 1).

Another driving force in the apparel industry is technical textiles with a primarily functional purpose such as protective clothing or medical textiles. On a world scale, technical textiles make up to a third of total textile production (Bierach/Vorotnikov 2017, p. 4). While the Swiss market for consumer electronics is yet decreasing, technical textiles still are in a former stage of maturity.

Consequently, both consumer electronics and apparel are subject to changing industry dynamics, is it through innovation or seasonality. A conceivable argument for price differences would be that innovations were introduced slightly later to the Swiss market. However, several interview partners deny this arguing that products are even introduced earlier to the Swiss market in some cases (Heri, 03.03.2017, para. 26; Späni, 10.05.2017, para. 39). Thus, innovative drive of the CE industry is responsible for global price decreases and a competitive marketplace but does not explain price differences between Switzerland and the EU.

## **10.2. Switzerland as a Test Market**

Many manufacturers of consumer electronics used Switzerland as a test market for their latest products and services. It is suggested that this has an impact on the low price level of consumer electronics in Switzerland (Stünzi 2013). Switzerland is an interesting market for tests for several reasons. Swiss consumers have a high purchasing power, affinity for technology, and the market has a manageable size and offers different language regions (Lang 2009, p. 32). A dense broadband network has further led to a high mobile phone density and also Swiss consumers are more prone to online shopping than consumers from other European countries (Müller 2017).

In many ways it is the consumer of tomorrow that can be tested in Switzerland. While the most popular television in Spain has a 32 inch screen, there is a tendency towards 64 inch screens in Switzerland. Thus, the development in the Swiss market is

rather ahead of the European market. It is expected that the European market develops in a similar direction as the Swiss market (Späni, 10.05.2017, para. 38).

Manufacturers usually accept smaller margins when using Switzerland as a test market, since small sales numbers would not provide desired information (Price Supervisor 2014). However, Giuriato (12.05.2017, para. 48) doubts that Switzerland is still used as a test market today. Product lifecycles were so short that it is not possible anymore to test a product before releasing it to all markets.

A prominent example of using Switzerland as a test market is also known for the apparel industry. Traditional mail-order catalogue distributor *Neckermann* abolished its catalogue in Switzerland and fully shifted to the online sales channel. Once the strategy was successfully tested in Switzerland, it was expanded to other countries (Lang 2009, p. 32). However, using Switzerland as a test market hardly has an effect on the price level of apparel. Also for the consumer electronics market it is doubtful whether a punctual use of Switzerland as a test market had an impact on the generally low price level since no one is at all times in a testing phase (Stünzi 2013).

### 10.3. Price Pressure of Loss-Leader Offers

Another explanation for cheap consumer electronics are so-called loss-leader offers. *Media Markt* was the first company to pursue such a pricing strategy which is why it is also called Media-Markt-pricing. Today it is used by many retailers in this business. It means that a focus is put on an individual low price article that is highly advertised. Prices might even be set below cost. Such loss-leader offers strongly impact the price image of a retailer even if there exists no price advantage on the rest of the assortment to competitors (Stünzi 2013). The aim of loss-leader offers is to attract customers to the store. Necessary margin is then made on other products, especially on accessories and services. In the end the right margin mix is decisive (Späni, 10.05.2017, para. 40).

According to CE market expert Heinz Beer (cited in Stünzi, 2013), volume-weighted sales prices of electronics might even be above the European average in Switzerland. According to him, Swiss CE retailers have more price setting power than their European counterparts which is why they use loss-leader strategies more intensively. According to him, loss-leader pricing strategies are not pursued in the apparel industry because there are not any comparable focus articles that would attract customers. Loss-leader pricing is therefore a factor that contributes to the lower price level of consumer electronics compared to apparel.

## 11. Trade Barriers

Barriers to trade are an important issue with regard to international price discrimination. Trade restrictions may significantly increase the price of a product or abandon them totally from a market. If there were fewer barriers to trade imposed on consumer electronics than on apparel this could possibly explain a part of the price gap between those product categories. First, the influence of tariff barriers will be analyzed and secondly, non-tariff barriers are researched.

### 11.1. Tariff Barriers to Trade

Tariff barriers have significantly decreased on an international level since the enactment of the General Agreement on Tariffs and Trade (GATT) in 1947. Switzerland joined GATT in 1966 (Swiss Federal Assembly 2003). Over 80% of imports originate from countries with which Switzerland has Free Trade Agreements (FTA). The FTA with the EU is most significant. Consumer electronics as well as apparel imported from the EU are duty-free. However, these imports are only duty-free if they are compliant with origin requirements, otherwise regular tariffs come into effect (Moser/Werner 2016). This is sometimes problematic for apparel companies. A distinct division of labor among the value chain leads to a complicated process to access certificates of origin. Moreover the rules of origin desire some outdated process steps and sometimes it is not possible anymore to reach the origin of a product. Thus, in some cases imports from the EU are subject to regular tariffs instead of preferential tariffs because the certificate of origin is missing. Some companies therefore just pay the regular tariff to circumvent these administrative hurdles. It happens that suppliers do not issue certificates of origin to parallel distributors to impede parallel imports (SECO 2016b, p. 13). Bloch (11.06.2017, para. 67), industry expert of fashion company *Manor*, alleviates the negative effects however, arguing that the importers take care of customs clearance and did not report any problems with certificates of origin.

Regular tariffs for apparel and textiles are higher than those of all other industrial products with an average tariff rate of 5.5% of product value (Moser/Werner 2016, pp. 46-47). In 2016, the Swiss Federal Assembly cancelled duties on 60 tariff numbers restricted to four years to foster competitiveness of local apparel companies. This measure creates comparable competitive conditions with the EU (Swiss Federal Assembly 2015b). A comparative advantage of Switzerland over the EU results from the FTA with China. Apparel imports from China make up to almost a fifth of all apparel imports (Schmutz 2014). The reason why Switzerland still imposes duties on textiles is not primarily to protect the domestic industry but to have something in the bag when negotiating a FTA with India and Vietnam (Städler 2013). Tariffs that are im-

posed on goods from certain countries disqualify the location automatically as a production site (Bloch, 11.06.2017, para. 66). Generally speaking, Swiss fashion companies avoid apparel from countries that are imposed with duties. Thus, the negative effect from tariffs is primarily that they reduce the number of potential suppliers.

Swiss as well as European customs authority distinguish IT goods and consumer electronics. Their interpretation complies with the narrow definition of consumer electronics. Other than in this Thesis, computers, smartphones and other IT related devices are considered as IT goods. Regular tariffs for consumer electronics are up to 14% of the value of the good (Heuser/Samadi 2015). In 1996, Switzerland was amongst the 29 countries that signed the information technology agreement (ITA). Today, this agreement covers 82 participating states and 97% of world trade of IT products. While the agreement covered consumer electronics only partially, it was extended to 200 new products in 2015, and now covers many consumer electronics, inter alia touch-sensitive screens, video cameras, Blu-ray players and navigation devices (cp. SECO, 2016). In Switzerland, the new rules came into force at the beginning of 2017 (Swiss Federal Assembly 2016). Still not covered by this disposal are consumer electronics in the narrow sense such as televisions, projectors and certain monitors (Loets 2016).

With regards to tariffs only, Switzerland has a slight advantage over EU countries due to the FTA with China. However, custom clearance itself brings several disadvantages especially the complicated process of getting certificates of origin. Generally high tariffs on apparel further decrease the number of potential suppliers. But tariffs are also demanded for important categories of consumer electronics. As tariffs were cut for 60 apparel and textiles tariff numbers in 2016, differences in the price level between apparel and consumer electronics caused by duties must have decreased. The impact of duties on price differences is therefore rather negligible.

## 11.2. Non-Tariff Barriers to Trade

Non-tariff barriers are just as detrimental to free trade as tariff barriers to trade and are generally better accepted than tariff barriers. Some non-tariff barriers to trade that affect consumer electronics and apparel are special regulations and provisions, bureaucratic hurdles and diverging technical norms.

Swiss consumers' magazine *saldo* investigated the impact of special provisions on price on a sample of 20 similar products. They could show that imported products with special provisions are in average 45% more expensive in Switzerland than in Germany. On the contrary, the price gap added up to only 25% without trade restric-

tions (Lattmann 2015). That is, import encumbrances may lead to 20 per cent higher prices. A study by the State Secretariat for Economic Affairs (SECO 2013) confirms these findings but found a price difference of only 10% between products with or without technical trade restrictions.

With regards to packaging and labelling consumer electronics are not due to any special regulations. As a member of the European Agency for Standards, Switzerland adapts any new European standards. Products that are compliant with these standards carry the CE label (Santander 2017). Tolerances, permissions, certifications and conformity assessments are identical in Switzerland and the EU (Heri, 03.03.2017, para. 15). This Cassis de Dijon principle generally also applies for textiles. Yet they have to be compliant with additional Swiss legislation regarding flammability, prohibition of short-chain chloroparaffin and octylphenol (SECO, 2016b; SECO 2008, p. 130). CE manuals are preferably but not mandatory written in German or another national language. If the manual does not include an official language this information must be displayed in the offer (Heri, 03.03.2017, para. 16).

Diverging technical norms is another field of non-tariff trade barriers. Such differences exist for some CE categories. Swiss standard plug socket and keyboards are two restrictions to the Swiss market. However, neither is there standardization in the EU on these aspects. Therefore, diverging technical norms cannot explain higher prices in Switzerland. Apart from differing plug sockets and keyboards, there are very little special provisions to the CE industry in Switzerland (Kessler 2016, p. 34). For the apparel industry, norms are compliant with European regulations (Bloch, 11.06.2017, para. 69).

There are some bureaucratic hurdles associated with national borders such as customs clearance costs, value-added tax liabilities or waiting times. The cost resulting from bureaucratic hurdles are estimated to be around 2% of the value of the good (Minsch/Moser 2006). The biggest bureaucratic hurdle for CE retailers according to Späni (10.05.2017, para. 41) is that Switzerland enforces weight duties instead of the more common value duties. This correspondingly applies to apparel. Attention should be paid to the fact that weight duties are a bigger burden for low-priced imports as equivalent value duties what increases the price gap for cheap goods (SECO 2008, p. 132). Some efforts were undertaken to facilitate customs procedures with online tools what counteracts non-tariff barriers to trade (Price Supervisor 2014).

Special provisions, technical norms and bureaucratic hurdles thus make Swiss prices more expensive. Some special provisions exist for consumer electronics but techni-

cal barriers to trade are not considered as significant, neither for consumer electronics nor for apparel. Bureaucratic hurdles are comparable or slightly higher for apparel due to difficulties with certificates of origin. Non-tariff barriers to trade therefore exist but are only a minor factor when it comes to price differences.

## 12. Cost Structures

Economic literature describes a wide behavioral repertoire regarding price formation. However, the lower price limit is normally given by costs that incur with the exception of price wars. Mark-up pricing is still the dominant method for price setting. Eventually, costs are supposed to have a major impact on the high price level in Switzerland.

The first section will analyze cost differences between Switzerland and the EU in general. The second section will then dig specifically into price structures of consumer electronics and apparel retailers.

### 12.1. General Cost Drivers in Switzerland

A commonly held argument for higher prices in Switzerland is the high Swiss income level. Median gross hourly earnings are higher in Switzerland than in every European country, followed by Norway and Denmark (Eurostat 2016e). Labor cost, that include gross wages, social contributions, training and recruitment were 27 euro per hour higher in Switzerland than in the EU average in 2012 (Federal Statistical Office 2016). High wages increase prices of production and distribution in Switzerland, however not as much as often claimed.

To compare competitiveness with regard to price of labor, one has to consider unit labor cost instead of mere labor cost. Unit labor cost are a quotient of labor cost and value added (Arvanitis/Hollenstein/Marmet 2005, p. 94), and are therefore a measure for international price competitiveness. Due to high productivity, Swiss producers managed to keep unit labor costs at a relatively low level from the year 2000 onwards. Switzerland performs well with respect to productivity, ranking only slightly behind Germany and Japan (Reppas/Brandes/Meier 2012, p. 61). The Swiss Federal Assembly (2015a, p. 16) as well as a study by BAKBASEL on behalf of six Swiss retailers (Grass/Stocker/Waldmeier 2010) came to the same conclusion that labor cost are not the reason for the high Swiss price level, arguing that longer working hours and higher productivity allow for a higher wage level. Other impacts on unit labor cost are less ancillary wage costs, public holidays and vacation as well as less strike and sick days in Switzerland. However, Swiss unit labor cost measured in euro rose drastically in recent years due to the steep appreciation of the Swiss Franc. The upvaluation of the Swiss Franc subsequent to the financial crisis pushed unit labor cost up by more than a third. Up to 2008, unit labor cost in Switzerland did not differ significantly if it was measured in Swiss Francs or in euro (Reppas/Brandes/Meier 2012, p. 61). Furthermore, the difference of unit labor cost between Switzerland and the EU is

smaller for high-paying jobs than it is for low-paying jobs (Stölzle/Hofmann/Lampe 2014, p. 42). Retail employees rank at the lower end of the wage scale (Federal Statistical Office 2015). Therefore, with the appreciation of the Swiss Franc and a high share of low-paying jobs in retailing, labor costs have to be considered as a cost driver.

The effect of a strong Swiss Franc is twofold. While the export industry suffers from increased unit labor cost, imports get more affordable (Fischer 2015). Producer and import price index decreased by 9.7% since 2008 (Federal Statistical Office 2017a). Indeed, retail businesses with a focus on imported products such as the consumer electronics or apparel industry can benefit from a strong Swiss Franc by lower import prices depending on the amount of cost that accrue in Switzerland. But another factor is relevant in connection with exchange rates. Consumer electronics are often directly imported from the Far East, which is why the exchange rate to the US Dollar is decisive. Depending on exchange rates, this may cause competitive advantages. While the euro's weakness increases import prices in European countries, a strong Swiss Franc compared to the US Dollar reduces the price on imports from the Far East (Schluep 2013).

Besides, Switzerland has comparative cost advantages in some fields. One of them are low cost of capital due to lower interest rates on credits and mortgages (Feubli,/Fuhrer/Hotz 2016, p. 6). The impact of low capital costs differs depending on the proportion of capital costs on overall costs and debt-financing percentage (Price Supervisor 2014, p. 32). An older study from 2003 found that the price effect of low capital costs in Switzerland should add up to a price advantage of 12% (Iten et al. 2003, p. 14). But due to international capital mobility, capital costs are not considered as relevant to price differences in industrialized countries (Price Supervisor 2014, p. 31).

The third basic cost factor next to labor and capital is land. Property expenses and rents for warehouses and sales areas result from construction cost and demand. Quality-adjusted construction costs were comparable between Germany and Switzerland in 2007 with an exchange rate of then 1.65 CHF per EUR. Prices rose primarily in accordance with the appreciation of the Swiss Franc since then. Building plots are expensive in Switzerland relative to EU countries due to resource scarcity and additional building requirements. Increasing shortage of land especially in urban centers has forced up real estate prices. The rent level in general classifies as high for both private and industrial sites. However, low mortgage interest rates alleviate the effect of high land prices in Switzerland (Price Supervisor 2014, pp. 32-34). New buildings are set up due to the low mortgage rates wherefore a reduction of rents for sales areas could be observed in recent years (Jucker et al. 2017, p.24).

Moreover, higher transportation and logistical costs contribute to higher costs in Switzerland. They consist of warehousing, transportation and cargo handling. The introduction of a distance-related heavy vehicle fee in Switzerland in 2005 increased the cost for transportation significantly (cp. Krebs/Balmer 2015). Higher labor costs are prevalent especially for warehouse staff and dispatchers, but also for chauffeurs (Stölzle/Hofmann/Lampe 2014, p. 43). Customs clearance further increases transportation costs as outlined in the previous chapter. Lower value added taxes (VAT) instead cheapen fuel prices. Overall, it is estimated that logistical costs are 30% to 50% higher in Switzerland than in Germany (Price Supervisor 2014). On a global scale, logistical costs have decreased (Bleuel 2017, p. 5).

Advertising costs are another important cost driver that arises in Swiss Francs. They are often blamed for higher prices in Switzerland. About half of overall production costs of branded products are spent on advertising. The small market size with four different languages is a main driver for higher advertising costs. TV commercials are especially expensive in Switzerland. To reach 1000 people, a company has to spend four times more in Switzerland than in Germany. Pronounced brand affinity of Swiss consumers moreover leads to a higher quantity of advertising activities (Price Supervisor 2014, p. 58).

Another argument to explain higher costs in Switzerland is multilingualism. Operating instructions need to be printed in three different languages and marketing activities need to be adapted. But this argument does not appear particularly pertinent, at least for internationally traded products. All main Swiss languages are common internationally, special translations are not necessary. In the EU, operating instructions have to be printed in far more languages. However, multilingualism may be misused as a tool for price discrimination (Eichenberger 2005, p. 46).

There are also several factors that have a positive effect on cost in Switzerland. Most importantly, Switzerland has considerably lower VAT rates. With a normal rate of 8%, the Swiss rate is 7% lower than the deepest European rate from Luxembourg. The average VAT rate in the EU is 21.5% (European Commission 2017). The fiscal quota compares average tax burden on an aggregated level. The fiscal quota is clearly lower in Switzerland than in the EU where fiscal quotas of 35% and higher are normal (Price Supervisor 2014, p. 40). In consequence, costs imposed by labor, rents, transportation and advertising have potential to increase the general price level in Switzerland. However, the effect to increase prices is lower than generally expected.

## 12.2. Comparison of Cost Efficiency

Consumer electronics and apparel are both sectors with a high share of imports over the value creation stages. Nevertheless, a large part of household expenditures on apparel and consumer electronics goes to Swiss retailers and wholesalers. Over the whole value chain, 43% of apparel expenditures are spent on imported goods and services (Feubli/Fuhrer/Hotz 2016, p. 2). This share must be in a similar range for consumer electronics or slightly higher since there is no local production at all. In the few niches with local production exist in the apparel industry, as for example couture or laces but they carry no weight considering overall turnover of the industry. This means that over the half of overall costs accrue in Switzerland. Thus, also in an industry with mostly imported goods, the lion's share of costs accumulates nationally.

An important difference between the CE and apparel industry is their retail structures. A third of all consumer electronics are sold online, whereas the online share of apparel is only 15% (Jucker et al. 2017, p. 12). The cost structure of an online business is leaner than that of a stationary store. They have cost advantages with regards to fewer fix costs for rents, fewer shop employees and no need for shop equipment (Feubli et al. 2015, p. 22). On the other hand, online shops have higher IT costs what alleviates the effect. The higher online share of consumer electronics still helps to keep costs low.

The share of overall logistical costs is around 5% for retail businesses (Price Supervisor 2014). Consumer electronics and apparel have relatively similar transportation and logistical requirements due to their small size (cp. Kölliker 2016). Jenni (08.06.2017, para. 53) indicates that the CE industry has leaner processes when it comes to inventory management and warehousing. Additional costs arise especially for apparel companies from a high number of returns. The return ratio from goods bought online in Germany 2012 is 20% of consumer electronics purchases and between 30% and 50% of apparel purchases (Hofstetter 2012). While *Zalando* offers shipment and returns for free, most other retailers demand a premium at least for returns. As logistical costs are higher in Switzerland than in the EU, a higher return ratio and costlier warehousing contribute to the price gap between consumer electronics and apparel.

Previous chapters have already given several indications on differences of procurement costs for CE and apparel retailers. A study by BAKBASEL found that Swiss companies had cost disadvantage especially in procurement. The price increase was estimated at 12% against Switzerland's neighbouring countries in 2009 (Grass/ Stocker/Waldmeier 2010, p. 29). Trade barriers, economies of scale as well as bargaining power of suppliers impact procurement costs. Bargaining power of

international fashion companies is higher what allows them to enforce higher list prices for Swiss retailers and to keep higher margins for themselves. This argument is often substantiated with references to lower economies of scale in Switzerland (Bloch, 11.06.2017, para. 63). The order quantity of a German retailer may be up to ten times higher than the quantity of a Swiss retailer. Therefore, European retailers are able to profit from better conditions. On the contrary, it was shown that due to low bargaining power of suppliers, Swiss CE retailers are able to get same acquisition prices as their European counterparts. Therefore, procurement costs are a main driver for higher prices for apparel in Switzerland.

## 13. Discussion

Low prices are beneficial for a national economy. Lower prices strengthen purchasing power of consumers and enhance international competitiveness of the export industry. On the contrary, higher prices forthright reduce available real incomes what leads to weaker demand with negative effects on the economy. Surpluses are shifted from consumers to retailers and producers. This can cause a dissipation of resources. Furthermore, high prices stimulate shopping tourism and an outflow of surpluses (cp. Eichenberger 2005). A complete harmonization of prices is not realistic due to the smallness of the market, topographic conditions, the protection of industries, and steep appreciation of the Swiss Franc. But there are also good reasons for smaller price differences due to lower VAT rates, lower capital costs and higher labor productivity. However, there is considerable evidence that market power on different trade levels is exploited in many industries to demand higher prices in Switzerland.

This study investigated in the CE and apparel industry to find evidence for differences in the market structures that allow for a low price level of consumer electronics in Switzerland. Beforehand to answer this research question, influence factors on prices needed to be detected. This research on influence factors has led to 18 different hypotheses that were tested throughout the analysis. From the tested factors 7 were found to have an impact meanwhile 11 factors had no effect on the price level. Table 3 summarizes the correlations. The pluses in brackets indicate an estimation of the severity of a price enhancing factor. The decisive effects for price differences have various sources. The interplay of supply factors, demand factors, external as well as internal factors have led to the unique structure of the CE market in Switzerland that allows for a low price level.

The intensity of competition is a crucial factor on the supply side to decide whether companies are able to absorb buying power. Market power can exist on all levels of trade, from retailers over suppliers to manufacturers. The market for both consumer electronics and apparel is shrinking what increases the pressure on competitors. With subsidiaries of *Migros* and *Coop* as well as *Media Markt*, three established players compete in the market for consumer electronics. The market is also played by a number of generalists and specialized traders in the IT segment. The online market is separated in major players on the one hand and a vast fragmented field of niche suppliers. This leads to a distinctively high density of retail competitors that compete in the same product range with little potential for differentiation. Low differentiation has then again resulted in a main focus on low prices. There are even signs of a price war with competitors offering parts of their assortment below acquisition prices. Also, loss-leader offers were detected as an influence factor on the low price level of consumer electronics. Loss-leader offers are used more often in Switzerland because re-

tailers have more price-setting power than their European counterparts. However, loss-leader offers are rather a consequence of a high intensity of competitive rivalry than a cause of it.

**Table 3: Effects of different Factors on Price Differences**

Source: Own table

| Influence Factor              | Consumer Electronics | Apparel   | Effect on Price Difference |
|-------------------------------|----------------------|-----------|----------------------------|
| Market growth                 | Negative             | Negative  | No                         |
| Retail competition            | Very high            | High      | Yes (+)                    |
| Threat of entry               | Low                  | Medium    | No                         |
| Bargaining power of suppliers | Low                  | Very high | Yes (+++)                  |
| Anticompetitive agreements    | Low                  | High      | Yes                        |
| Threat of substitutes         | Low                  | Low       | No                         |
| Supplier switching costs      | Low                  | High      | Yes (+)                    |
| Price transparency            | High                 | Low       | Yes (+++)                  |
| Price sensitivity             | Medium               | Medium    | No                         |
| Brand loyalty                 | Low                  | Medium    | No                         |
| Standards of quality          | High                 | High      | No                         |
| Standards of services         | High                 | High      | No                         |
| Tariff barriers to trade      | Low                  | High      | No                         |
| Non-tariff barriers to trade  | Medium               | High      | Yes (+)                    |
| Cost                          | Medium               | High      | Yes (++)                   |
| Innovative drive              | High                 | Medium    | No                         |
| Switzerland as a test market  | No                   | No        | No                         |
| Loss-leader offers            | Yes                  | No        | Yes (+)                    |

could be shown that the same is true for the apparel industry. The apparel industry is dominated by established international fashion companies and numerous medium-sized firms. The density of retailers is higher in the apparel industry in Switzerland than in neighboring countries. Furthermore, there is a broad field of small fashion companies with only few employees. The market entrance of online giant *Zalando* has significantly increased the rivalry in the industry and general expectations of customers towards a fashion company. The seasonality of apparel has decreased due to longer periods of clearance sales. A crowding-out process has started to increase market concentration with some years of delay compared to the CE industry. Thus, the CE industry had more time to adapt to a highly competitive environment than the apparel industry. All these factors have led to a harsh competitive environment of the level of retailers.

With regards to bargaining power of buyers the main difference results from price transparency of retail prices. It is simple to compare prices of consumer electronics online due to uniform product labels what enhances the pressure on retailers. Even small price differences may result in massive competitive advantages. This makes it more difficult for retailers to discriminate prices in Switzerland. Online shopping therefore has a positive effect on the bargaining power of buyers. Price transparency is a reason why rivalry among retail competitors is slightly higher in the consumer electronics industry than in the apparel industry.

Another important factor for price differences is competitive rivalry on the level of suppliers. In the CE industry acquisition prices are very transparent and a broad number of suppliers compete in the market. Supplier switching costs are low due to high price transparency in acquisition and comparability of products. Therefore it is much more difficult for CE suppliers to charge a premium in Switzerland or to establish anticompetitive agreements. Interestingly, Swiss CE retailers profit from identical acquisition prices as their European competitors. Due to the harsh competition on the level of suppliers, no disadvantages accrue from lower economies of scale.

This is different in the apparel business. Lower economies of scale ultimately lead to higher acquisition prices for Swiss apparel retailers. High bargaining power of suppliers probably causes a majority of additional costs on retail prices in the apparel industry in Switzerland. It is very difficult for fashion retailers to use grey markets for parallel imports because dependencies exist to the services of importers. If they would parallel import apparel from brands like *Nike* or *Adidas* for example, they needed to provide customs clearance, customer service and returns handling on their own. They would also abandon bonus payments. As apparel products are more differentiated than consumer electronics, the services of an importer is more important. Also, fashion retailers would run the risk of delivery denials if they would procure some parts of their assortment on grey markets. This increases supplier switching costs massively. What's more, the transparency of prices on the level of suppliers is much lower for apparel. It is therefore more difficult for retailers to put pressure on suppliers. This allows suppliers to charge a premium in Switzerland. The CE industry in Switzerland strongly profits from lower bargaining power of suppliers.

It is problematic that antitrust legislation only applies if a company has a market-dominating position. The lately launched fair pricing initiative attempts to reduce suppliers' market power by tightening antitrust legislation. The CE industry shows eventually that retail prices can be in a similar price range in Switzerland as in the EU if the right conditions are given. The sentence against *Nikon* who violated antitrust legislation had a precautionary effect on other suppliers.

Tariff and non-tariff barriers to trade were further suspected to have an influence on the price differences. Apparel imports generally underlie high tariffs. However, fashion retailers avoid manufacturing in countries where tariffs would be levied. Tariffs also play a tangential role for CE imports. Non-tariff barriers to trade such as border waiting and bureaucratic hurdles slightly increase the price of both consumer electronics and apparel with some more difficulties for apparel businesses due to aggravated accessibility of certificates of origin. Border costs also emerge from another currency and legal area. The interaction of barriers to trade and parallel imports is important in this context. Lower barriers simplify parallel imports that may enhance domestic competition. If a trader wants to import goods through an unofficial channel he has to deal with customs clearance on his own. It is beneficial to a similar price level with the EU that almost no special provisions occur for consumer electronics.

Higher costs in general are frequently used to justify a higher price level of goods in Switzerland. It could be shown that costs in Switzerland are lower than generally expected and that intensive retail competition leads to cost savings. Processes in the CE industry are organized more efficiently and certain cost drivers such as rents and labor costs got reduced. Also, warehousing is designed efficiently to optimize costs. Lean cost structures are therefore a direct cause of a competitive retail environment. It can be assumed that the apparel industry will develop in a similar way but is not there yet. As mentioned, the apparel industry suffers from lower economies of scale and a high bargaining power of suppliers what increases acquisition costs. Even though the market is getting more concentrated, sales areas were still expanded what raises additional costs. Consequently, it is possible to keep costs as low to allow for a similar price level in Switzerland as in the EU. Higher costs are widely compensated by a low VAT rate. The average VAT rate in the EU is 21.5%, while the normal rate in Switzerland is only 8%. The intensity of competition in the CE industry has led to an efficient allocation of resources on the one hand and an erosion of margins on the other. CE companies compensate for those low-margin consumer electronics by offering related products and accessories where higher margins are generated. High retail competition paired with low bargaining power of suppliers is thus the prerequisite for a low price level in Switzerland. These findings suggest that price setting is rather competition-based than cost-based. Import prices have only small explanatory power for retail prices. This argument is supported with reference to products that are produced in Switzerland but sold at a cheaper price abroad (Price Supervisor 2014, p. 21).

The analysis could further demonstrate that some prominent explanations for the low price level of consumer electronics in Switzerland are not plausible. Switzerland is not used anymore as a test market by CE manufacturers because time is too short to

test a product before releasing it everywhere. Furthermore, standards of quality and services are not causing the price differences. Services however help to distinguish more and less price sensitive customers.

Overall it shows that intensive competition on the level of retailers alone does not guarantee for a low price level in Switzerland. Competition needs to be intense on all levels of trade. If this is the case like in the CE industry, prices will not exceed costs by far. A major driver for intensive rivalry is price transparency on all levels. Price transparency in acquisition enhances bargaining power of retailers and transparent retail prices enhance bargaining power of consumers what has positive effects on competition. Price transparency is therefore a main driver to prevent absorption of buying power of consumers.

Online price and quality comparisons are thus an important means to foster price transparency. The rise of online shares in all industries will automatically help to adjust high Swiss price levels.

But also price transparency alone is not sufficient to prevent high prices in Switzerland. Key to low prices is intensive cross-border competition. Maximization of yields is a core essence of a free-market economic system and it is consistent that companies discriminate prices after geographic or other criteria if they have the possibilities to do so. The implementation of the Cassis de Dijon principle that should stimulate competition had less impact than was hoped for. Especially in the food industry retailers do not want to cannibalize their own brands with cheap parallel imports. Cross-border shopping online is another form of parallel imports with which consumers can put pressure on retail prices. The government must create the right boundary conditions that online trade is not unnecessarily restricted. Geo-blocking is such an example of obstruction of online trade that is used by companies to segment different markets. Consumer themselves are able to put pressure on retail prices if they behave sensitive to price differences and actively compare prices. A systematic reduction of tariff and non-tariff trade barriers is another effective way to foster domestic competition. Lower trade barriers would complicate price discrimination among countries.

A main limitation to this study is the lack of available or reliable data on certain aspects of the investigation. Especially with regards to costs interview partners were not willing to provide precise information and literature about this topic is limited. It would be worthwhile to further investigate in cost structures since costs define minimum prices. It was further difficult to find industry experts that were willing to participate. It can be assumed that this research has not reached theoretical saturation and that a higher sample size especially with experts from the apparel industry would have led to more insights into the industry. Also, only some aspects of the two ana-

lyzed industries could be considered. An infinite number of variables exist that influence prices. Market structures and price setting mechanisms are complex and dynamic and there is a threat that not all important factors were covered or not in the needed depth. Moreover, there is a threat of bias when choosing sources and analyzing them. The effect on prices could be over- or underestimated or even misinterpreted. The choice of cases is always a subjective decision. Eventually, contradicting hypotheses could be proven. This threat was mitigated by data triangulation.

This study was able to demonstrate if a variable has an impact on the price difference or not. It would be of value for future research to estimate to what percentage the factors increase the price. Then it would be possible to take appropriate measures where it is mostly needed. Also, to dig deeper into cost structures and the influence of competition on cost would be of great interest. Furthermore, an analysis that considers different industries at the same time could generate more in-depth results.

## 14. Conclusion

Switzerland is a small country staying outside the EU with a high purchasing power and four different languages. These conditions have led to a price level of consumer goods in Switzerland distinctively above the EU average. However, the CE industry shows that high prices are not carved in stone. A fortunate interplay of different factors has resulted in a unique market structure that supports a similar price level in Switzerland as in the EU.

Foremost, the Swiss CE industry is characterized by very intense retail competition. A particularly high density of competitors with similar product ranges, low market growth and high price transparency contribute to this market situation. The assortment of CE retailers is not much differentiated what makes the price often the only argument. Prices of consumer electronics are easy to compare online. But intense retail competition alone does not guarantee for a low price level. Also, bargaining power of suppliers needs to be low at the same time. There are numerous different suppliers competing in the market and price transparency in acquisition is fully given. Low tariff and non-tariff barriers to trade further reduce supplier switching costs for retailers. Therefore, it is not possible for suppliers to discriminate prices and absorb additional purchasing power.

High competition on all levels of trade prevents retailers to retain high margins on consumer electronics. CE companies have allocated their resources efficiently to hold or gain market shares. Resource dissipation was minimized. Together with cost advantages due to a lower VAT rate in Switzerland these particular circumstances allow for a similar price level of consumer electronics in Switzerland and the EU.

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## **List of Interview Partners**

Bloch, Rainer, Merchandising Buying Manager Men's wear, Manor AG, Telephone Interview, June 11, 2017.

Giuriato, Luca, Market Expert Multimedia, GfK, Telephone Interview, May 12, 2017.

Heri, Patrick, Category Manager Consumer Electronics, Digitec Galaxus AG, Zürich, Written Interview, March 03, 2017.

Jenni, Dagmar, Managing Director, Swiss Retail Federation, Bern, Telephone Interview, June 08, 2017.

Loosli, Bernard, Secretariat IG CE, Swico, Zurich, Telephone Interview, March 10, 2017.

Späni, Peter, Category Management and Provisioning, Interdiscount AG / microspot.ch, Jegenstorf, Telephone Interview, May 10, 2017.

## Appendix A: Interview Guide

### A Introductory Questions

1. First, I would be interested in your responsibilities that you have in your company?  
*Als erstes würde mich interessieren, welche Aufgaben und Verantwortungen Sie in ihrem Unternehmen übernehmen?*
2. Consumer electronics are more affordable in Switzerland than in the EU. Could you tell spontaneously tell me the reasons why prices for consumer electronics are so low in Switzerland?  
*In der Schweiz sind Artikel der Unterhaltungselektronik (Consumer Electronics), also etwa Fernseher, Radios oder Smartphones günstiger als in der EU. Können Sie spontan Gründe benennen, warum die Preise von Unterhaltungselektronik in der Schweiz tiefer sind als im Ausland?*
3. Was the price level of consumer electronics always so low? How have price, offer and demand developed in the industry?  
*War Unterhaltungselektronik schon immer günstiger? Wie hat sich die Branche in Bezug auf Preis, Angebot und Nachfrage entwickelt?*

### B Supply Chains

1. What are the supply chains of the products you offer from the manufacturer to the retailer?  
*Wie ist der Vertrieb geregelt vom Produzenten bis zum Detailhändler? Können Sie mir die Wertschöpfungskette für verschiedene Produkte aufzeigen?*
2. Is there a main importer for Switzerland and does he possess sole right of distribution?  
*Gibt es einen Generalimporteur für die Schweiz, und besitzt dieser Alleinvertriebsrechte?*
3. Is it possible for retailers in your industry to buy directly from wholesalers or manufacturers abroad? Do you have to fear any disadvantages if doing so?  
*Kann die Detailhandelsstufe auch selber bei Grosshändlern oder Produzenten im Ausland einkaufen? Steht ein Bezug über verschiedene Grosshändler offen, ohne Nachteile für das Unternehmen befürchten zu müssen?*
4. How saturated is the market on the level of suppliers?  
*Wie gesättigt ist der Markt auf dieser Stufe?*
5. How easy would it be to change distributor?  
*Wie einfach wäre es, den Distributor zu wechseln?*
6. Do lower economies of scale increase acquisition prices?  
*Verteuern tiefere Skaleneffekte den Einkaufspreis?*

## C Competition

1. How would you describe retail competition on the market of consumer electronics?  
*Wie würden sie den Wettbewerb beschreiben auf dem CE Markt?*
2. How many small shops are active on the market? Is the density of retailers higher or smaller than abroad?  
*Wie viele kleine Anbieter gibt es auf dem Markt? Wie hoch ist die Angebotsdichte?*
3. Is there an increase or decrease of market participants? If yes, what are the reasons?  
*Gibt es eine Zunahme an Anbietern? Wenn ja, weshalb, da doch die Margen klein sind?*
4. What leads to the high intensity of competition?  
*Was führt dazu, dass der Schweizer Markt so umkämpft ist?*
5. How important are foreign competitors on the Swiss market?  
*Wie sehr drängen ausländische Wettbewerber auf den Markt?*
6. Is competition more intense in Switzerland or in the EU?  
*Ist der Wettbewerb in der Schweiz noch intensiver als im Ausland oder ist er vergleichbar mit der EU?*
7. When did the first discounters appear in the Swiss market? What influence do they have on the market?  
*Sind Discountketten in der Schweiz früher aufgetaucht als im Ausland? Könnte das einen Einfluss auf den Markt gehabt haben?*

## D Trade Barriers

1. Do you have to pay tariffs? What are the price effect of tariffs?  
*Müssen sie auf ihren Produkten Zölle zahlen? Und um wieviel werden die Produkte dadurch verteuert?*
2. How easy is customs clearance?  
*Wie einfach ist die Zollabwicklung?*
3. Do you depend on importers for customs clearance?  
*Könnten Sie bei einer Direkteinfuhr die Unterlagen für den Zoll/Fiskus selber zusammenstellen?*
4. Are general product requirements and norms on consumer electronics identical in Switzerland and the EU? (Tolerances, Application, Certification, Conformity)  
*Sind die allgemeinen Produkthanforderungen gleichwertig oder hat die Schweiz abweichende Normen (Toleranzen, Zulassung, Zertifizierung, Konformitätsbewertung)?*

5. Are there Switzerland-specific information requirements such as operating instructions?  
*Müssen Schweiz-spezifische Informationsvorschriften beachtet werden?*
6. Are there any quality differences between consumer electronics in Switzerland and the EU or are the products identical?  
*Gibt es Qualitätsunterschiede zwischen Unterhaltungselektronik in der Schweiz und im Ausland oder sind die Produkte und Services identisch?*
7. Do you face any disadvantages that Switzerland is not a member of the EU?  
*Entstehen bei Ihnen irgendwelche Vor- oder Nachteile, dass die Schweiz kein Mitgliedsstaat der EU ist?*

## **E Cost**

1. Are there any surcharges for Swiss retailers?  
*Gibt es Schweiz-Aufschläge irgendwelcher Art?*
2. What advantages / disadvantages do you face related to cost?  
*Ist man als Schweizer Anbieter in irgendeiner Art bevorteilt oder benachteiligt auf Kostenseite?*
3. Can you make a statement to the height of margins? Are they higher or smaller in Switzerland?  
*Können Sie etwas zu der Höhe der Margen sagen? Sind diese höher oder tiefer als im Ausland?*
4. Does the margin vary for different products?  
*Variiert die Marge bei verschiedenen Produkten?*

## **F Demand**

1. Is the assortment smaller in Switzerland?  
*Ist die Sortimentsbreite kleiner in der Schweiz?*
2. Are new products later released in Switzerland and are therefore more affordable?  
*Kommen die neuen Produkte in der Schweiz später auf den Markt und sind deshalb günstiger?*
3. Can you imagine that the Swiss consumer is more price aware and compares prices more than consumers in neighboring countries? Are Swiss more price sensitive in this field?

*Können Sie sich vorstellen, dass sich die Gesellschaft in der Schweiz stärker mit dem Kauf von Unterhaltungselektronik befasst als in Nachbarländern? Sind die Schweizer preissensibler in diesem Bereich?*

4. How loyal do you think customers are in relation to your company or to single brands? Has consumer behavior changed?  
*Wie "treu" schätzen sie die Kunden ein in Bezug auf ihr Unternehmen und einzelne Marken? Hat sich dieser Punkt in der Vergangenheit verändert?*
5. How important is demand when setting prices?  
*Wie wichtig ist der Druck von Kunden bei der Preisfestsetzung?*

## **G Strategy**

1. There are cost-based, demand-based and competition-based pricing strategies. Where does your company set a focus when in price setting?  
*Es gibt kostenorientierte Preisfestlegung, nachfrageorientierte und wettbewerbsorientierte. Worauf legen sie in ihrer Firma bei der Preisfestlegung besonders wert? Wie werden Preisentscheidungen gefällt?*
2. How important are prices of competitors?  
*Wie wichtig ist der Druck von Konkurrenten bei der Preisfestsetzung?*
3. Are there competitors in a premium price segment that position themselves with outstanding quality and service?  
*Gibt es Mitbewerber, die im oberen Preissegment angesiedelt sind, und sich beispielsweise mit Qualität und Service profilieren?*

## **H Conclusions**

1. What are summarized the most important factors to influence the low price level of consumer electronics?  
*Welche der erwähnten preisbestimmenden Faktoren sind zusammengefasst die wichtigsten?*
2. If you compare consumer electronics to washing machines or other home appliances, why are these products more expensive in Switzerland?  
*Wenn Sie Unterhaltungselektronik zum Beispiel mit Waschmaschinen oder Kühlschränken vergleichen, die ja in eine ähnliche Kategorie fallen, weshalb denken Sie, sind diese Produkte wesentlich teurer in der Schweiz?*
3. Is there something else you wanted to mention that could be relevant for my study?  
*Geht Ihnen sonst noch etwas durch den Kopf, das für meine Arbeit relevant sein könnte?*