STRATEGIC MANAGEMENT ACCOUNTING: APPROACHES & TECHNIQUES

Lecture 9_1

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PRESENTATION OUTLINE

A) Review of SMA

B) BSC: Conceptualization

C) Benchmarking

D) Value chain analysis

E) Just in time

F) Total Quality Management

A) INTRODUCTION: SMA (1)

- **WHAT IS SMA?**
- **HOW CAN BE CONCEPUALIZED**

- There is no one single definitions of SMA.
- Many definitions: some emphasize either an *external* or *internal* focus.
- For example: 1) Drury (2008, p. 570) defines SMA as: "*a form of management accounting in which emphasis is placed on* <u>*information*</u> *which relates to* <u>*factors external to the firm*</u>*, as well as* <u>*non-financial information*</u> *and* <u>*internally generated information*</u>" (CIMA, 2005, pag. 54).

A) INTRODUCTION: SMA (2)

- 2) Innes (1998) defines SMA as the "*provision of information to support the <u>strategic decisions</u> in organizations*".
- But an omnibus definition is provided by Hosque (2006), who, in his defition, identifies the key elements to understand SMA:

  i. Nature of SMA: what is it?;

  ii. Role in the decision-making: what role?;

  iii. Orientation: what focus?,

  iv. Purpose: why?

A) STRATEGIC MANAGEMENT ACCOUNTING (3)

SMA IS THE PROCESS OF IDENTIFYING, GATHERING, CHOOSING AND ANALYSING ACCOUNTING DATA FOR HELPING THE MANAGEMENT TEAM TO MAKE STRATEGIC DECISIONS AND TO ASSESS ORGANIZATIONAL EFFECTIVENESS (Hoque, 2006)

A) INTRODUCTION: SMA (4)

CONCEPTUALIZATION

Process	I.e. something that is not static but in a continuous change in relation to the institutional contex
Identifying Gathering Choosing Analysing	Accounting-based information, that could be both financial and non-financial. These have an internal or external focus.
Help Support	Information has a function: i.e. to support management in decision-making.

A) INTRODUCTION: SMA (5)

Strategic choices

Information will be provided for the formulation, implementation and management of organization's strategy .

To promote behaviour that is consistent with an organization's strategy, attention is devoted to designing and implementing accounting-based techniques that can be used to identify, clarify, communicate and manage organizational strategy.

Accounting-techniques ⟷ **Strategy**

A) INTRODUCTION: SMA TECHNIQUES

MANY TECHNIQUES

A) BALANCED SCORECARD

B) VALUE CHAIN ANALYSIS

D) ABC, ABB, ABM

E) BENCHMARKING

F) MAN. ACC. FOR JIT

G) MAN. ACC FOR TQM

B) BSC: CONCEPTUALIZATION (1)

- BSC has been defined as an integrated set of performance indicators, which derive from corporate strategy formulation, that give top management a view of the organization as a whole.
- BSC is a strategic management Accounting technique for communicating, evaluating and monitoring the achievement of the mission and strategy of the organization (Drury 2004, p. 1001).

B) BSC: CONCEPTUALIZATION (2)

To understand BSC we start from its terminology.

SCORECARD → It a system or procedure that is used for checking or testing something (English Dictionary of Advanced Learner's)

BALANCED → It means that indicators should take into account "<u>all</u>" different aspects of organizational life

B) BSC: PERSPECTIVES (3)

BSC is based on the assumption that an organization's vision & strategy is best achieved when organizational operations are seen from 4 balanced perspectives:

A) CUSTOMER PERSPECTIVE: how do customers see the organization?

B) INTERNAL PERSPECTIVE: how well does the organization manage its operational activities?

C) LEARNING and GROWTH PERSPECTIVE: to achieve our vision, how will we sustain our ability to improve?

D) FINANCIAL PERSPECTIVE: how should we appear to our shareholder?

B) BS: PERSPECTIVES (4)

	Goal	Performance indicator
Financial perspective	Increased profitability Retained share dividend	Return on equity Return per share
Customer perspective	Increased customer satisfaction Decrease in complaints and returned products	Customer satisfaction index Number of returned products
Internal business perspective	Decreased cassations Increased productivity	Number of cassations Number of working hours per product/service
Innovation and learning perspective	Increase of new services Better staff policy	New services share of overall sales Employee satisfaction index

C) VALUE CHAIN ANALYSIS: DEFINITION

- Describes the linked set of value-creating activities required to bring a product or service to the customer.
  - Begins with basic raw materials from suppliers, moves to a series of value-added activities involved in producing and marketing a product or service and ends with distributors getting the final products or services into the hands of the ultimate customers.
- Developed by Michael Porter (1980, 1985) as a tool to help businesses to analyse cost structures and identify competitive strategies.
- VCA emphasises that costs occur, not only in manufacturing, but across the activities of a business.
- Provides useful information for cost management and increasing customer value.

C) VALUE CHAIN ANALYSIS (1)

- Activities are classified as *value-added* or *non-value -added*.
- Identify which activities to keep and/or eliminate through an analysis of the value created v/s incurred costs.
- Non value adding activities:
  - preparation time;
  - waiting time;
  - unnecessary process steps;
  - over-production;
  - rejects;
  - set-up times;
  - transportation/distribution;

C) VALUE CHAIN ANALYSIS (2)

- **VCA allows to understand the total value of all operations across the business, as well as the industry.**
  - Where can costs be minimised?
  - Where can customer value be increased?
- **Focus on value-creating activities**
  - from receipt of raw materials from suppliers, and research and development of products and processes,
  - to the sale of the product to the customer and the provision of after-sales customer support.
- **Customer value is the quality of a product or service that a customer finds valuable**.

C) VCA: CO-ORDINATION OF ACTIVITIES

- By co-ordinating linked activities, an organization can
  - Reduce transaction costs
  - Gather better information for control purposes
  - Substitute less costly operations in one activity for more costly ones elsewhere
  - Reduce the combined time required to perform them
- Gaining competitive advantage requires that an enterprise's value chain be managed as a system rather than as a collection of separate parts.

D) BENCHMARKING (1)

1) What does “benchmark” mean?

2) Benchmarking is a SMA technique involving:

- Comparison with “best practices” (sector, market, etc);
- Extended inter-firm comparison/ratio analysis;
- Initiatives to improve the ‘relative position’.

3) Benchmarking requires comparable data

4) Best practices benchmarking: seeks out the leader in a particular process/product for comparison.

5) Difficulties for its application.

D) BENCHMARKING: EXAMPLE (2)

(% of R'n'D expenditure)

	Product x	Best practice
Concept	2%	8%
Specification	3%	10%
Development	42%	40%
Testing/Debugging	45%	32%
Productionisation	8%	10%
Total	100%	100%

Consequences: Slower to market, Higher production costs

E) MANAGEMENT ACCOUNTING FOR JIT

- Just in time (JIT) is a manufacturing approach aimed at reducing non-value added activities (i.e. costs);
- JIT seeks to achieve following goals:
  – Elimination of non-value added activities;
  – Zero-inventory;
  – Zero defects;
  – Zero breakdowns;
  – 100 % on-time delivery
- Difficult to be implemented and unlikely to be fully achieved but offer targets for improvements.

E) MANAGEMENT ACCOUNTING FOR JIT

	Traditional manufacturing	JIT manufacturing
Throughput time	Processing time + inspection time + conveyance time + waiting time	Processing time only
Optimum lot size (production)	More than one	One
Set-up time and costs	Long set-up time and therefore high costs	Zero set-up time and thereby no set-up costs
The need for holding inventory	**A back-up exists to keep production flowing**	**Zero inventory**
Quality management	Provision for waste, scrap, rework etc.	Zero defects; quality environment
Number of suppliers and relationships	**Large number of suppliers and short-run relationships**	**Fewer suppliers and long-term relationships**
Factory layout	More space is needed	Reduces the need for space
Management accounting systems	**Greater emphasis on costing (short-run strategy)**	**Greater emphasize on cost management (long-term strategy)**
Performance evaluation systems	**Greater emphasis on financial indicators (e.g. ROI)**	**Greater emphasize on non-financial indicators (e.g. customer satisfaction)**

E) MANAGEMENT ACCOUNTING FOR JIT

- Installing a JIT system affects:
  - The traceability of costs
  - Enhances product-costing accuracy
  - Diminishes the need for allocation of service-centre costs
  - Changes the behaviour and relative importance of direct labour costs
  - Impacts job-order and process costing systems

F) MAN. ACC. FOR TQM (1)

- Competitive and global environment required businesses to focus on customer demands
- Customer demands **QUALITY** (product and service)
- Quality is not free - costs for quality assurance
- TQM concepts are implemented by firms interested in enhancing their survival prospects

F) MAN. ACC. FOR TQM (2)

- **<u>Quality control</u>**:
  - Specification of what is needed
  - Design the product or service to meet the specification
  - Production or installation to meet the full intent of the specification
  - Inspection to determine conformance to specification
  - Review of usage to provide information for the revision of specifications if needed

F) MAN. ACC. FOR TQM (3)

- **Statistical quality control:**
  - Collection, analysis and interpretation of data
- **Quality assurance:**
  - Determines effectiveness of the quality system
  - Assess the current quality
  - Determines quality problem areas or potential areas
  - Assists in the correction or minimisation of these problem areas

F) MAN. ACC. FOR TQM (4)

- Dimensions of the ‘quality’ of a product:
  - Performance
  - Aesthetics
  - Serviceability
  - Features
  - Reliability
  - Durability
  - Quality of performance
  - Fitness of use

EXAMPLES?

F) MAN. ACC. FOR TQM: THE COSTS OF (NON) QUALITY (5)

A) Prevention costs, e.g.:

- quality engineering
- design and development of equipment,
- quality training,

B) Appraisal costs, e.g.:

- inspection and testing of incoming material,
- product quality audit,
- materials and services consumed,

C) Internal failure costs , e.g.:

- scrap,
- rework,
- faulty supplier

D) External failure costs, e.g.:

- complaints,
- rejects and returns,
- repairs