

Strategic Management Accounting Assignment

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Introduction

The aim of this report is to assess the strategic management accounting techniques and provide a comparison with the traditional management accounting. The report is structured into two parts. Part A provides critical analysis of the costing approaches including marginal costing, absorption costing, and activity-based costing. It evaluates these approaches based on the managerial decision-making situations. Part B aims at addressing strategic management accounting (SMA) in supporting strategic plans and decisions made within the organisation. It compares SMA budgeting approach and traditional approach and justify the effectiveness of SMA.

Part A

1. Marginal or variable costing

Marginal or variable costing is a strategic management accounting technique, which focuses on the changes in the organisational total cost (Cescon, Costantini & Grassetti, 2019). It measures increase or decrease in the total cost of production associated with the change in quantity of the output desired. The emphasis is on the contribution margin per unit, and it helps to distinguish between the fixed and variable cost. Marginal costing is beneficial when implementing short-term decision making. According to Alabdullah (2022), marginal costing mainly focuses on the ease and simplicity in the implementation of short-term decision-making. In this approach, the main variable for costing technique is the variable cost charged to the process and organisation's operations, which leaves the indirect costs being written off on the profits generated.

Marginal costing is effective for the organisation as it is simple and easy to implement. Management accountants can rely on this technique in valuing the closing stock, which prevents the possibility of illogical carrying forward of the organisation's fixed costs (Cescon, Costantini & Grassetti, 2019). For the fixed overhead recovery rates, they can be computed and the over or under recovery can be charged to the reported contribution margin. However, the challenge with this technique is the technical difficulties in separating the fixed cost form the variable costs. The assumption is that all the expenses are separated into fixed and variable expenses, but there are some expenses which are semi-variable (Phornlaphatrachakorn & Na-Kalasinthu, 2020). With the technology development, there has been an increase in fixed expenses, and marginal costing does not consider fixed expenses when computing the total cost for the organisation.

Despite the challenges with marginal costing, organisations rely on it for managerial decision-making situations. Management can implement special order decisions while using marginal costing technique (Phornlaphatrachakorn & Na-Kalasinthu, 2020). In this decision, the management considers the implementation of the one-time occurrences of the special orders, as they are not affected by the fixed costs. The management considers integrating marginal costing where the variable costs will provide accurate information on the variable costs towards fulfilling the order. According to Nikkeh et al. (2022), the marginal costing is appropriate for special orders, as the management relies on the incremental expenses or costs in determining whether to accept or reject the decision.

The second management decision considered with the use of marginal costing is the product mix decision. In this case, marginal costing is valuable in determining optimal product mix to be implemented in the organisation. Mohajan (2022) mentions that insufficient resources within the organisation requires the management to optimise the contribution margin, and they can easily compare the profitability of different products using marginal costing technique. The fixed cost incurred for products in similar product line can be easily assessed, which can be integral in understanding total costs (Phornlaphatrachakorn & Na-Kalasinthu, 2020). As such, the management can benefit in optimizing resource allocation to determine the appropriate product mix to achieve high contribution margin.

2. Full or absorption costing

Absorption costing is a managerial accounting technique used in capturing all the costs associated with the manufacturing of a product. Unlike the marginal costing method, this method captures direct and indirect costs including direct labor, direct materials, overhead costs, insurance, and rent among others. As indicated in Alabdullah (2022), absorption costing is relevant in external reporting of the company's operations. Absorption costing involves the cost each unit, which is essential when determining the effectiveness of managing costs and ensuring that they report information based on the cost of goods, which impact the financial statements.

Organisations can benefit from absorption costing due to its standardized approach in reporting the direct and indirect costs incurred during the manufacturing process. The absorption costing technique complies with the Generally Accepted Accounting Principles (GAAPs), which requires reporting of all expenses reported in the organisation (Cescon, Costantini & Grasseti, 2019). Absorption costing ensures that all the production costs are accounted for, which provides the stakeholders with information on the profitability of the

products manufactured. Using absorption costing is critical and efficient in tackling the profits of the organisation, and it provides the management with the anticipation of the seasonality in increase of revenues. However, the management should consider the challenges with absorption costing in which there is the possibility of the profit and losses being skewed (Mohajan, 2022). This costing technique can show the profit to be better in a given financial period, as the fixed costs are not deducted from the company's revenues until the manufactured products are all sold. There is the challenge of lack of influence on the company's operational efficiency.

The managerial decision-making situations involved in the absorption costing is the external reporting of the company's operations and decisions related to tax (Alabdullah, 2022). Absorption costing is relevant in informing the stakeholders on the financial health of the company. Stakeholders rely on this information, as the costing technique adheres to the accounting standards and provide accurate reflection on the costs associated with the production process (Tran & Thao, 2020). With this in place, a comprehensive costing strategy developed is critical in providing accurate information on the productivity level. Secondly, the management's decision-making process can be aligned with the current strategy in implementing long-term production planning. In the case where strategic decisions undertaken are based on the resource allocation and production capacity, the costing technique used provides an insight into the overall organisation's structure. According to Alabdullah (2022), long-term decision making requires the organisation to understand the cost structure and implement measures towards improving the capacity expansion and increasing the overall production capacity. The organisation should consider the production planning initiatives, which can reveal the changes in the production volume towards accurate decision-making and forecasting.

3. Activity Based costing (ABC)

Unlike the other two costing techniques, ABC involves cost allocation using the overhead cost accounts. There are distinct steps to be followed in allocating the activity cost drives (Elshaer, 2022). First consideration is the identification of the major activities taking place in the organisation. The activities selected should be at a reasonable level of aggregation based on the cost/benefit criteria. It is essential in assigning costs to the cost centre for each activity. It is essential in determining the activity drivers and providing good explanation for the costs of each activity pool (Arenhart, Mendes & Pizzolato, 2020). The cost drivers are easily measurable, and the data can be easily obtained and identified with the respective product.

The benefit of using ABC technique is its ability to provide the management with realistic costs in manufacturing specific products. It allocates the manufacturing overhead costs accurately and identifies processes that are inefficient, which the management can improve (Arenhart, Mendes & Pizzolato, 2020). Through the ABC technique, the profit margin is precisely determined, and the unnecessary costs are mitigated. As such, it offers an understanding of the manufacturing overhead costs, and improve the implementation of policies that will capitalize on the manufacturing costs. However, there is the challenge of time used in preparing reports and analysing the costs associated with the specific manufacturing products (Quesado & Silva, 2021). For the management to undertake a coherent and informative strategy, the costs incurred should be accumulated and information analysed to provides effective measures to improve the quality of the findings generated. The reports from the ABC technique are not always conformed with the GAAPs, and it can be used in external reporting.

The management can rely on this information in decision making process where it is essential in making product diversification decision. Assessment of the different product offerings, and the cost implication on the resources allocation can affect the productivity level in the dynamic industry (Phornlaphatrachakorn & Na-Kalasindhu, 2020). Diversification is essential in accurate allocations of costs to specific activities, which helps in developing pricing decisions aligning with the demand for different products. Secondly, cost reduction measures can be developed with the intention of reducing costs of operations (Cescon, Costantini & Grasseti, 2019). ABC technique is used in identifying specific activities, which contributes to the cost, and this is integral in implementing cost-cutting strategies. As such, ABC technique is superior to the others in providing informed decisions on the cost-cutting mechanisms towards improving competitive edge in the industry.

Part B

a) Establishing mission, vision, and objectives

In modern organisations, strategic management accounting (SMA) supports the strategic plans of the company by providing the management with information in making appropriate decisions (Rashid, Ali & Hossain, 2020). The initial business idea should come from assessing the external environment and internal capabilities in making informed decisions on the policies to be undertaken. Stakeholders should be informed of the vision, mission, and objectives of the organisation. Using the SMA, the objectives of the organisation can be

developed by providing financial and non-financial information regarding the business. However, SMA is appropriate where the business is running, and it can rely on the information on organisation's internal capabilities in developing the objectives and goals (Rashid, Ali & Hossain, 2020). SMA provides guidance on shaping the vision of the company by providing financial information on the current operations of the company and aligning it with non-financial information such as employee motivation. Unlike traditional methods, the vision statement should incorporate the non-financial metrics toward understanding the commitment of the organisation to its overall productivity in the industry. In establishing the mission statement for the organisation, SMA helps to set out the rationale behind the formation of the organisation. This includes communicating the nature of business, and it provides an attainable and realistic mission statement. By considering both the financial and non-financial metrics, the organisation's mission statement can be more realistic unlike when developing it based on financial metrics only.

b) Undertaking a position analysis such as SWOT

Strategic management accounting provides an opportunity to undertake positional analysis such as SWOT analysis. In this case, the assessment of the cost leadership strategies is undertaken in determining the cost-efficient measures to be undertaken (Rashid, Ali & Hossain, 2020). For the traditional budgeting strategy, the interest is in developing mechanisms for improving the productivity level of the organisation. As such, the interest of the management should be on analysing the cost structure of products and services and ensuring that they remain competitive in the industry. SMA facilitates value chain analysis to determine the strengths and weaknesses of the operations of the company. With the value chain analysis, organisations can identify specific activities that can be improved and increase their productivity level. Through activity-based costing (ABC), SMA helps in identifying and allocating costs to efficient activities (Berg & Madsen, 2020). As such, it helps to understand the inefficiencies and weaknesses in some activities and realign its strategy to allocate resources to efficient business processes. The long-term growth and success of the business are based on its ability to capitalise on activities that can maximise its productivity and avoid those inefficient activities. SWOT analysis is used in strategic planning and understanding the opportunities available to the organisation. Using SMA ensures that the management understands the financial and non-financial implications of market expansion.

c) Identifying and assessing strategic options

The management can rely on SMA in identifying and assessing the strategic options available to the organisation (Rashid, Ali & Hossain, 2020). In the use of the cost-plus pricing strategy, the management ensures that it encourages price stability with the assessment of the cost incurred in the manufacturing process (Berg & Madsen, 2020). Unlike traditional budgeting, SMA integrates the demand into the pricing of the products and services (Rashid, Ali & Hossain, 2020). This is done by adjusting the target mark-ups. Interestingly, the profitability of the organisation can be realised where the price setting is concerned with assessing the financial and non-financial elements in understanding the trends in the industry and formulating mechanisms to maximise its productivity in the industry. According to Berg & Madsen (2020), activity-based costing is used in identifying actual costs, by providing a detailed assessment of the cost drivers and the measures to be undertaken to achieve the strategic improvements in the industry. It links the different products and business segments in deciding on the activities that might contribute to the organisation's strategic goals. The management can rely on ABC and cost-plus costing to determine the future implications of the costing strategies, and they should align with the strategic plans and mission of the organisation.

ABC is used to communicate to the management the incremental budgets and the changes reported in certain activities within the organisation (Duci, 2021). The cost management initiatives developed should aim to authorise the supply of the resources and the management to perform activities that meet the required budgeted production and sales volume. With knowledge of the productivity level of the organisation, the emphasis is placed on meeting the budgeted cost, which is integral in understanding the trends in the financial performance levels (Quesado & Silva, 2021). In the case of traditional budgeting, it is inappropriate to be used for those activities in which the consumption of resources does not vary proportionately with the volume (Rashid, Ali & Hossain, 2020). As such, it fails to provide management with detailed information on the trend of the support activities. However, it is worth noting that the SMA cannot be appropriate when applying sophisticated procedures in which the firm has numerous product lines. It can affect the strategic planning of the organisation, as there is limited guidance to setting the price and other factors should be considered in the implementation of the pricing strategy. An understanding of the different measures to implement strategic planning is critical in aligning with the organisational objectives and increasing its competitiveness in the industry.

Strategic management accounting advocates for implementation of different pricing strategies when undertaking strategic plans for the organisation (Bénet, Deville & Naro, 2019). It is integral in realising effective pricing that meets the demands of the consumers. For instance, it facilitates the implementation of price-skimming in which the organisation can charge high initial prices for the consumers and reduce the price over time (Quesado & Silva, 2021). The strategic management accounting provides the management with information on the markets requiring price skimming, which helps to maximise the profitability of the company. The other pricing strategy to be implemented in achieving a strategic plan is penetration pricing, which influences the perspective of the consumers on the products offered to them. In penetration pricing, the organisation sets the prices at the lowest level aiming to reach a wide range of consumers, and this can be increased when the consumers have been loyal to the consumers (Quesado & Silva, 2021). SMA ensures that the pricing policies implemented vary depending on the product's life cycle. However, this is not the case with traditional budgeting where a rigid pricing strategy is employed whether the focus is on market penetration or product diversification. It relies on the forces of demand and supply in determining the prices charged for the products (Berg & Madsen, 2020). The rigidity in the pricing of the products is challenging to the organisation involved in implementing new strategies based on the changing trends in the market.

d) Selection of strategic options and formulation of long- and short-term plans

The selection of the strategic options and formulation of short and long-term plans is facilitated by the SMA. With the use of a sophisticated ABC system, it optimises the operations of the organisation by considering the intensity of competition and implementing short-term and long-term plans to address the competitiveness in the industry (Mariina & Tjahjadi, 2020). The management can use the ABC system to develop high product diversity, which meets the intended objectives of the organisation in maximising its productivity level (Aryani & Setiawan, 2020). However, the simplistic costing system utilises a standardised product range, which is characterised by low product diversity. Emphasis on assessing the competitiveness in the industry helps the management to determine the strategy to employ in the short and long-term.

e) Performance review and control

SMA facilitates performance review and control with the use of a balanced scorecard. The balanced scorecard emphasises non-financial measures and integrates them into a formal

reporting system, unlike the traditional management account where these non-financial terms were not integrated into the management accounting report (Hadid & Al-Sayed, 2021). As such, the financial performance of the company is increased with the organisation linking the performance to its strategy (Bénet, Deville & Naro, 2019). Balance scorecard advocates for integrating four different perspectives into the formal management accounting report – customer perspective, internal business process perspective, learning and growth perspective, and financial perspective (Mio, Costantini & Panfilo, 2022). In implementing the organisation's strategic objectives, these objectives need to be translated into the performance measures for the organisation. The balanced scorecard is characterised by two distinct performance measures including the leading and lagging measures (Killingsworth, Mehany & Kim, 2021). The leading measures assess the drives towards achieving the intended performance including innovation, employee engagement, and quality management. The lagging measures determine the outcomes of the previous actions including the customer satisfaction level, revenue outlay, and profitability level (Killingsworth, Mehany & Kim, 2021). The benefit of using a balanced scorecard is that it brings different perspectives together and influences the company's overall performance. The management can determine the cause-effect of the performance and implement measures to improve it. Also, this is a strategy that provides a comprehensive framework for translating the organisation's strategic goals into performances. As such, it is superior to traditional management accountants.

Conclusion

In this report, the analysis shows that the SMA approaches are superior to the traditional approaches. For costing, the activity-based costing provides the management with cost reduction measures, as it links the costs with the different activities. Organisations interested in product diversification can utilize SMA approach. The findings also suggest that SMA budgeting provides the management with information to conduct performance review, which helps in making decisions on the efficient and inefficient activities within the organisation.

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