Strategic Management Accounting: Strategic Planning Process, Costing And Value-chain

Introduction

The term 'Strategic Management Accounting' is widely accepted to have first been coined by Kenneth Simmonds (1981). Whilst still in its relative infancy, strategic management accounting was given an elementary definition which stated that it is, "… analysis of financial information on the firm's product market and competitors' … cost structures and the monitoring of the enterprise's strategies and those of its competitors" (Bromwich, 1990). Strategic management accounting contains several components such as: how it deals with competitor information; how the firm's strategic position affects their management accounting system; value-chain analysis, in which a firm exploits linkages to gain competitive advantage; and the need for market-oriented information (Lord, 2007). However, strategic management accounting has failed to have the impact that many thought it would, and only leaves behind a trail of "great 'beginnings', 'pilot' projects and 'cameo' appearances" without any real substance (Shank, 2006). Furthermore, Shank notes that of all the firms he worked alongside, trying to implement strategic management accounting techniques, between 1985 and 2005, there are no major success stories. These two points, put forward by Shank, indicate how strategic management accounting has been unable to establish a level of popularity that its early advocates may have expected. It is essential to analyse why this is the case by examining the issues within the practice and concluding with a critical evaluation of strategic management accounting's shortcomings. Analysis of the most prominent components of strategic management accounting and investigation of their flaws will help produce a reductionist view of the concept. Case studies will also be included to understand how strategic management accounting is, or is not, used in real-life practice.

Strategic planning process

As mentioned above, one of the key components of strategic management accounting involves the firm's analysis of their strategic position as well as the implementation of its strategy through the means of strategic planning. There is, however, a lot of literature which underlines a number of criticisms towards this. Firstly, Mintzberg (1978), which is hailed as one of the three works that strategic management originates from (Nixon and Burns, 2012), presents the idea that many of a firm's strategies usually aren't formed during strategic planning. This is regardless of how rigorous the planning process is. It goes on to recognise that strategies tend to arise as a result of exchanges between several of the firm's decision-makers. Strategies are even sometimes only referred to as a strategy due to the benefit of hindsight as they may not have been deliberate at all. It's not a rarity for planned strategies to never come into fruition either (Lord, 2007). This argument calls into question the need for strategic management accounting because it can be said that it's not necessary to spend time creating specific strategies when they will often fall into place themselves. Therefore, it may be better to save valuable resources and avoid the strategic planning process altogether. To add to this criticism of the planning process, Dermer (1990) used the word "teleological" to describe it. This means that they view the process as having its success determined by the effectiveness of how management deals with external events in the environment. Dermer was also a keen advocate of the ecological view as he argued that organisational strategy depends on how individual stakeholders present their personal wants. The strategy that arises, or ‘emergent’ strategy, is then a result of who presents their cases the best. Again, it is hard to view strategies formed in this way as deliberate, it shows that sometimes strategies depend upon the level of power that is held by select decision-makers. Their opinions are then viewed in retrospect and the strategy is formed, without the use of a strategic planning process. Whilst it can’t be denied that some deliberate strategies are ultimately achieved, there is also a lot of reason to question the usefulness of strategic management accounting in cases where emergent strategies are also successful.

Strategic costing and value-chain

Furthering the criticisms of the use of certain components within strategic management accounting, Beverley R. Lord’s (1996) case study of a cycle retailer underlined how the strategic cost management element (Shank and Govindarajan, 1992a) can also be seen as redundant. The cycle manufacturers named, ‘Cyclemakers Group (NZ) Ltd’, were the focus of the case study. Lord’s findings do not reflect well on strategic management accounting practices as Cyclemakers successfully exploited linkages in the value-chain without the need for financial analysis – analysis that would be carried out by accountants. The manufacturers exploited linkages with both suppliers and customers which led to reduced costs, especially compared to competitors, and a relocation of their factory which helped decrease their freight costs from the factory to the retailers who stocked their products. Lord concluded that firms who focus on good relationships with suppliers and customers will already be exploiting linkages in the value-chain deeming the need for its formal analysis unnecessary; a stance that disagrees with Shank and Govindarajan. Despite this criticism levelled towards strategic cost management, the idea of the value-chain analysis is one which has its merits. The idea was first put forward by Porter (1985) who encouraged firms to analyse their value-chain and find linkages that can be exploited to add value to their operations. These linkages can be with suppliers, customers and within the firm itself. As shown by Lord (1996) in the Cyclemakers case, a firm can successfully exploit these linkages in order to reduce their costs and increase their profitability. Whilst many components of strategic management accounting have their weaknesses, it is hard to deny that the value-chain has many strengths when utilised properly within a firm. Value-chain analysis has also managed to make more of an impact than most components of strategic management accounting and still appears in modern literature. As recently as 2018 the value-chain was used to analyse ecosystem service (Rawlins, De Lange and Fraser, 2018). This evidence suggests that strategic management accounting practices have not been completely shunned, but in fact developed to be inclusive of less financially driven uses, and it may have more popularity today than some may think.

Competitor analysis

A third important practice within strategic management accounting is the gathering and analysis of information by a firm regarding the operations of their competitors. Simmonds (1981) saw the importance of a firm’s competitive position over time as he saw that profits would ultimately arise from this. As a result, he advocated the use of competitor information as it would allow a firm to enhance their position. This practice will obviously have its merits as understanding competitor costs, for example, makes it easier to detect if they’re changing their competitive position by changing suppliers to lower costs. However, competitor analysis has been compared to focusing too much on neighbouring, competitor cars on a highway and losing your own concentration on the road ahead (Harari 1994). This analogy was furthered to relay the point that firms who employ this technique usually only manage to match competitors as opposed to being innovative and gaining any sort of advantage themselves (Lord, 2007). Firms who focus on competitor analysis generally miss the opportunity to form alliances with other firms should it be required. Porter (1985) outlines how two firms could potentially form a coalition with one another in order to “attack leaders”. These coalitions pool the resources of the respective firms involved and thus, they are better placed to gain control of the market in place of the original leader. Many firms have probably missed out on such opportunities as they’re too focused on competing with firms in similar positions instead of seeing a potential common goal. This point emphasises a great disadvantage of competitor analysis as a potential increase in profitability can be lost if firms remain too blind to the fact they can work with competitors. Bromwich (1990) also noted how established firms are less likely to require the use of competitor analysis as they have already surpassed the barriers of entry into the economy. Smaller, newer firms, on the other hand, may need to analyse their potential future competitors in order to understand the capital requirements and other costs needed to overcome the barriers to entry (Bromwich 1990). So, although competitor analysis may have its downsides with established firms, it may be more popular within newcomers to the market.

Are accountants required?

Strategic management accounting practices also question whether there is a need for an actual management accountant. Rickwood et al. (1990) is one case where there is a clear role for the accountant as it demonstrates a management accountant acquiring, using his authority, the competitor information that his firm owned. However, there is also a lot of literature to suggest otherwise. Referring back to Lord’s Cyclemakers case study, the firm in question employed a number of strategic management accounting techniques although they were put into practice by alternative departments such as production and marketing. Lord did not see any input from the firm’s management accountant(s) (Lord, 1996). Teijin Seiki, a machine manufacturing firm in Japan who were at the centre of Kawada and Johnson’s 1993 case study, determined that it was not the role of an accountant to carry out strategic management accounting. This role, instead, fell to production and sales and engineering personnel (Kawada and Johnson, 1993). It seems strange that accountants would not be utilised in a practice involving accounting but that could be explained by Coad (1996); he claims that management accountants require “good communication skills and an ability to empathise with others both within and outside the organisation”. This suggests that management accountants are not excluded from strategic management accounting processes for their lack of skill, but their lack of a team player mentality. Therefore, these arguments do not point criticism towards strategic management accounting techniques as such, but more towards management accountants instead. This perhaps illustrates the point, however, of why strategic management accounting has failed to enjoy higher levels of popularity. Management accountants are understandably unlikely to push to use a process within a firm that they would not fit into well themselves. However, this could potentially result in strategic management accounting developing as a concept, only without the input of accountants (Lord, 2007).

Case study analysis

Despite the issues and criticisms discussed so far, it seems that strategic management accounting still has a place in the modern world. Dmitrovi?-Šaponja and Suljovi? (2017) conducted a "large-scale multipurpose survey … on the use of cost systems and SMA practices in large-sized companies" within Serbia. They concluded that, when companies include at least one component of strategic management accounting in their operations, they receive greater quantities of "relevant and timely information compared to companies that do not use these techniques". They also found a strong correlation between the use of strategic management accounting techniques and a positive impact on both cost reduction and control. The fact that these Serbian companies are benefitting from the use of strategic management accounting techniques bodes well for the practice going forward. A lot of the early advocates may be disappointed to see that strategic management accounting isn't overly popular within Western Europe and North America, however, this does not detract from the fact that it can be successfully implemented in other parts of the world. This can also be seen in Lord's case study as the cycle manufacturers were based in New Zealand.

Conclusion

As stated within the introduction, I believed it was best to look at strategic management accounting from a reductionist viewpoint to find some of its deepest-rooted issues. Four major components stood out: competitor analysis; the strategic planning process; the value-chain and strategic costing; and the role of the accountant. Each of these components had significant weaknesses when used in practice which devalues the concept of strategic management accounting. The reductionist view was important as it seems that most firms who employ strategic management accounting do not use more than one component of it within their operations – meaning it becomes difficult to provide a holistic view if there are few examples of companies that implement strategic management accounting fully. Whilst there is a lot of evidence to suggest strategic management accounting is not the best practice within a firm, it can be argued that when utilised effectively it can be successful. This was best shown in the Serbian case study (Dmitrovi?-Šaponja and Suljovi?, 2017). Finally, however, Guilding et al. (2000) put forward the point that there is still no agreement amongst accountants when it comes to what constitutes as strategic management accounting. The early advocates may find that, in its essence, strategic management accounting is popular and well used; as is the case in both Lord's and the Dmitrovi?-Šaponja and Suljovi? case studies. However, the level of confusion that surrounds it may only provide the illusion that it has not established its popularity as much as its advocates would have liked.