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# The Utilization of Target Costing and its Implementation Method in Iran

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## Abstract

Target costing is one of the most effective methods in cost management. As a useful and efficient management tool, it has a comprehensive approach for managing costs, reducing prime cost of products in the initial stage of product planning and design, and achieving long-term profit. The present study attempts to investigate the use of target costing and its implementation method in Iran. For this purpose, the study has been conducted through the methods of field and library studies. The results suggest that identifying competitive price and customers' needs, entering the global competition, reducing prime cost of products, motivation and teamwork of the staff, using value engineering and activity-based costing are necessary for the successful implementation of target costing.

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## 1. Introduction

Today, due to the globalization of markets and the increasing development of issues concerning World Trade Organization and the gradual involvement of countries in this organization and their entrance into the World Trade market, the need for considering new techniques of cost management is felt more than ever. Countries that are willing to join this organization have to work in this competitive environment and in order to survive in such environments, they have to seek those mechanisms and tools that contribute to their economic survival in the global competitive

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market and those that prepare them enough before entering the comprehensive competition. In this regard, cost management can play an important role.

One of the most important techniques of cost management effective in this regard is target costing system. Target costing is a strategic issue in cost management which primarily focuses on cost management and on the future profit planning. Target costing maximizes the control over costs, increases profits and reduces costs of the product life cycle and allows companies to clarify the purpose of cost reduction practically, realistically and objectively. In addition to introducing target costing, the present study investigates the history, utility and purposes, its difference with the traditional approach of cost management, the advantages and disadvantages as well as its relationship with the customer-orientation, teamwork, its method of implementation in Iran according to the findings of the published researches.

## **2. Review of Literature**

Jalali Naini et al., (2010) in an article investigated target costing and cost management strategy in automotive manufacturing companies. They found out that the successful implementation of target costing in automotive manufacturing companies entails the maintenance of the quality and efficacy of their products and paying special attention to this useful issue in reduction of their product price so that they can increase their share and profitability in the market by making their products competitive. Moreover, in addition to protecting the interests of the owners of automotive industries, target costing brings about customer satisfaction and the development of quality.

Ashaghi (2008) in a study examined target costing with a systematic approach in the cost management. The findings suggest that customer and cost play an important role in target costing and that the companies that produce products with long cycle and large investments often use this system because their costs are reduced and they can obtain the prime cost by subtracting target profit margin from the sales price by determining the appropriate sales price, product functions and their desired quality.

In a study, Dastgir and Arab Yarmohammadi (2005) investigated the barriers to applying target costing system in the companies listed in Tehran Stock Exchange. This study seeks to respond to this question: "Given the importance of target costing system and its role in the long-term profitability of a company, what obstacles make the implementation of this system difficult?" For this purpose, five hypotheses have been used and the results suggest that as long as countries have exclusive market, they are not willing to use target costing.

Afonso et al., (2008) in an article examined the impact of time-to-market and target costing on the success of new product development. Their findings indicate that companies can make a profit by using target costing and reducing the time of supplying the products to competitive markets and the companies that can create a time cycle with low cost and high quality by reducing new product development are more successful.

Ellram (2002) in study investigated the involvement of supply management in target costing process. The results suggest that supply management plays a significant role throughout the process of target costing, especially in the early stages when the component level of target costing is developing and when the activities/changes are taking place to achieve the target costing.

## **3. Research Methodology**

The present study has been conducted by descriptive method and through library studies. Library information including books, internal and external journals and searching the databases and also using the experiences of other researchers (studying articles and theses) helped achieving the theoretical foundations and review of literature.

## **4. Theoretical Foundations of Target Costing**

Target costing is a strategic process in the management of a product prime cost to reduce costs which is implemented at the beginning of the product life cycle (early stage of planning and design) to maximize the profitability of products. There are various definitions of target costing, most of which indicate that target costing is a process used in a competitive market to minimize prime costs and achieve the desired profit margin. In a more general definition, it can be said that target costing is a systematic approach to determine at what expense a desired product

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