

# THE RELATIONSHIP BETWEEN COST REDUCTION TECHNIQUES AND PROFITABILITY

## **Abstract**

*The main difficulty encountered by organizations recently is the increase in the cost of operation that could lead to inevitable cost control and reduction scheme which makes it difficult for most organizations to operate at the cost efficient frontier. The main objective of this study is to determine the relationship between Cost reduction technique antecedents and profitability of organizations in a selected manufacturing company, Oyo state, Nigeria.*

*The study adopted a descriptive research design. The targeted population was employees in the selected manufacturing company. The unit of observation was sales managers, salespersons and employees. The sample size was 80. SPSS was used to organize code and generate a quantitative report. The data were analyzed using descriptive and inferential statistics.*

*The study found that fleet management is positively correlated with profitability in selected manufacturing company ( $r = 0.564$ ;  $P\text{-value} = 0.000 < 0.05$ ). The result reviewed that theiris significant relationship between fleet management and profitability in selected manufacturing company. It was also found that there is positive relationship between management control and profitability of the selected manufacturing company. The third hypothesis also shows that there is positive relationship between improved manpower and profitability in selected manufacturing company*

*Moreover, the study concluded that there is relationship between Cost reduction technique antecedents and profitability of organizations in a selected manufacturing company. The study recommended that Cost control and cost reduction scheme must be properly administered in an organization by setting realistic standard*

**Key Words:** *Cost Reduction Techniques, Profitability, Fleet management, Management control and Improved Manpowered.*

## **1.0 Introduction**

The growth of any company is largely determined by how well it can manage its costs. This is partly because to be able to maximize profit, cost must be reduced to the barest minimum. Cost reduction has become a vital tool for companies to constantly stay ahead of the increased competition in the business environment (Alireza & Mahdi, 2012). Indeed, even organizations that are gainful can profit by implementing cost-lessening techniques to make a considerably higher overall revenue on its items or administrations. According to Ogunnaike (2010), the effective and efficient management of cost is not only necessary to meet the profit objective of the company but also the going concern status of the entity. To record growth in terms of increase in profit of an organization, cost reduction mechanism should be put in place.

Asaolu and Nassar (2007) define cost reduction as the term used for planned and positive approach to the improvement of efficiency. It can be viewed in many ways, such as increasing productivity, and elimination of waste. Lucey (2009) refers to cost reduction as a concept which has the aim of reducing cost from a previously accepted norm or standard without reducing the effectiveness or performance of the project or services.

Dury (2007) defines control as the means of ascertaining that the activity of an organization follows the standard plan and that its goal is accomplished. Sikka (2003) discussed that cost control system consists of ways and methods that are used to control the operating cost of a job and ensure that cost does not go beyond a certain amount.

However, the aim of all production is to satisfy peoples wants, however in carrying out this production, certain costs are incurred in order to achieve the stated organizational objective be it to satisfy peoples wants or to maximizes profit. For any business to achieve its set objective there have to be adequate, strong and effective cost reduction measures (formal or informal) which should be adopted. The effectiveness of these measures however may have heaped some of these companies to still remain in business irrespective of the harsh condition like inflation among others. Many Nigerian business establishments presently, especially the manufacturing sectors are in serious profit squeeze. A number of factors account for this into ward condition which include, the increasing cost of running business in Nigeria, drastic fall in Nigerian foreign exchange market did not help matters. The situation is further aggravated by triple digit inflation present in our (Nigeria) economy. To maintain earnings in the face of the conditions, there is the need for these companies to make decision with regard to cost maintenance culture, increase productivity to enhance profitability and diversification into a completely new market area. In addition to these, it will enhance competitive ability and generate reasonable profit margin for survival, growth and expansion of the business.

### **1.1 Statements of the Problem**

The main difficulty encountered by organizations recently is the increase in the cost of operation that could lead to inevitable cost control and reduction scheme which makes it difficult for most organizations to operate at the cost-efficient frontier. Every organization that wants to survive and maintain its consumers must seek to improve on its product. Therefore, in order not to exceed their budget and not to run at loss, as well as not to reduce the quality of their products, organization needs to control costs and reduce their cost to the lowest minimum. For this reason, the study investigates the extent of application of cost control and cost reduction technique and the degree of their impact on the operational efficiency in an organization. The main difficulty encountered by organizations recently is the increase in the cost of operation that could lead to inevitable cost control and reduction scheme which makes it difficult for most organizations to operate at the cost-efficient frontier. Every organization that wants to survive and maintain its consumers must seek to improve on its product. Therefore, in order not to exceed their budget and not to run at loss, as well as not to reduce the quality of their products, organization needs to control costs and reduce their cost to the lowest minimum. For this reason, the study investigates the extent of application of cost control and cost reduction technique and the degree of their impact on the operational efficiency in an organization.

Ban on importation of certain basic raw materials, payment of long excise duties have caused some companies either to have closed indefinitely or produce at high cost, thereby making even the local goods high and sale volume low. This has resulted in poor profit margin payout, retrenchment, compulsory leave and retirement with or without benefit which invariable affects the company as well. Firms therefore are struggling to maintain satisfactory pay-off

because of high costs. So the main difficulty encountered by organizations recently is the increase in the cost of operation that could lead to inevitable cost reduction scheme. This cost reduction schemes makes it difficult for most organizations to operate at the cost-efficient frontier.

However, another problem is that many cost Reduction programs struggle to deliver or fail to stick. No matter how you cut the costs, there are some products where the returns still won't be viable, either because customers don't value them or there is always someone else prepared to offer them cheaper. Although there have been substantial research efforts by different scholars in determining what seems to be the optimal cost reduction strategy for firms and the effect on the reported profit, yet there is no universally accepted theory. Innes, John, Mitchell and Sinclair (2000) assert that the survival triplet today for any company is how to manage product/service cost, quality, and performance. The customers are continuously demanding high quality and better performance products/services and at the same time, they want the price to be reasonably low. The shareholders are also demanding a required rate of return on their investment from the company. Thus, cost has become a residual. The challenge is being able to manufacture products or provide services within the acceptable cost framework. Innes, John, Mitchell and Sinclair (2000) concluded their study with a recommendation that cost management has to be a continuous improvement activity within the company so as to enhance profitability and survival.

### **1.3 Objective of the Study**

The main objective of this study is to determine the relationship between Cost reduction technique antecedents and profitability of organizations in a selected manufacturing company. The specific objectives are:

- 1 Determined the relationship between fleet management and profitability in selected manufacturing company.
- 2 Determine the relationship between management control and profitability in selected manufacturing company
- 3 Determine the relationship improved manpowered and profitability in selected manufacturing company

### **1.4 Significance of the Study**

The significance of the research is to help the organization come up prudent cost control measures to maximize profits. The case study may be of absolute importance to the organization if the recommendation contained is adopted for implementation. The recommendation may help the organization overcome some of its operational and management problems. The researcher stands to benefit from this research in two ways. It is a prerequisite towards the attainment of doctorate degree. It may also propel the researcher to a better height should the organization adopt the contents and recommendation. It may come in handy as a secondary data source for future researchers.

### **1.5 Scope of the Study**

The study assessed the relationship between Cost reduction technique antecedents and profitability of organizations in a selected manufacturing company. The coverage area is limited to a selected manufacturing company in Oyo state. But the study encompasses both the staff in the lower to higher level management. The targeted population is employees and top management of the selected manufacturing company. The study adopted a survey research design and all the respondents were involved. The collected data was analyzed using descriptive statistics method.

## **2.0 Literature Review**

### **2.1 Cost Reduction and Techniques**

Low production costs have become one of the primary ways that organizations compete in a global economy, hence, cost reduction must continually be in the minds of managers of organization (McWatters, Morse, & Zimmerman, 2001). Cost reduction is a planned approach to reduce expenditure. It is a continuous process of examining critically all elements of cost and each aspect of the business with a view to improving business efficiency. Cost reduction is a corrective function. Cost reduction is the process of cutting down costs incurred by an organization for the purpose of making profit. It starts when cost control ends and considers that no cost is at its optimum level. According to Adeniyi (2001), cost reduction starts with an assumption that current cost levels or planned cost levels are too high despite the fact that cost control may be good and organization experiencing high efficiency levels.

### **2.2 Profitability**

Pandey (2010) defines profit as the difference between revenues and expenses over a period of time, (usually one year). Profit is the ultimate output of a company and it will have no future if it fails to make sufficient profit. Therefore, the financial manager should continuously evaluate the efficiency of the company in terms of profit. A company should earn profit to survive and grow over a long period of time. Ezeamama (2010) agrees that profit is the difference between revenues and expenses over a period of time. Therefore, profitability is the ability to make profits from all business activities of the company, organization, firm or an enterprise. It shows how efficiently the management can make profit by using all the resources available in the market. However, the term 'profitability' is an index of efficiency and is regarded as a measure of efficiency and management guide to greater efficiency. The change in operational efficiency is merely one of the factors on which profitability of an enterprise largely depends; moreover, there are many other factors besides efficiency which affects profitability ranging from the degree of competition that a firm faces, market competition, the strength of demand, the state of the demand, the advertising campaign, substitutes, Costing methods to the efficiency of the company. The Companies calculate gross profit by subtracting their manufacturing costs from the revenue generated after sales. Therefore, the money difference between the costs of goods sold and net revenue generated represents the gross profit.

### **2.3 Theoretical review**

#### **Going concern theory**

The going concern principle states that an entity will continue actively in business for the foreseeable future and will not be forced to bring its operations to a stand still or have its assets liquidated (The going concern principle, 2017). Theory of going concern refers to the ability of a company to make enough money to stay afloat without having to go bankrupt. The theory is premised on the assumption that an enterprise will continuously carry out its operating activities for a period of time that is sufficient enough to meet its obligations and commitments as they fall due. In other words, it is presumed that the company would have no reason to liquidate or be forced out of business in the foreseeable future. Since it is assumed that a company will not be

forced to halt operations, then management will have to make provisions to curb anything that will negate such assumption. Rising costs is the major factor that affects the going concern status of a business organization as uncontrolled cost can force a company to halt operations. Uncontrolled costs affect the ability of the company to make profit, thus, without profit company cannot fulfill its obligations, neither can it experience growth.

### **Neo-classical Growth Theory**

Neo classical growth theory summaries how a stable growth rate can be achieved with the proper amount of three powerful forces: labor capital and technology. The theory states that varying the amounts of labor and capital in a production function leads to a state of equilibrium. It emphasizes that three factors influence the growth of an economy (Otekunrin, A.O., Nwanji, T.I., Olowookere, J.K., Egbide, Fakile, S.A., Lawal, A.I., Ajayi, S.A., Falaye, A.J. & Eluyela, D.F., (2018)) .The theory also argues that technological change has a major influence on an economy, and that economic growth cannot continue without advances in technology. In manufacturing companies, three factors affect its capacity to grow; material cost, labour cost and overhead expenses. These factors have a major influence on the profit maximization ability of the firm, thus, hindering its ability to grow. Manufacturing firms will experience growth if these costs can be rightly allocated, controlled and ultimately reduced. In an economy where these costs are greatly affected by inflation, recession and other factors, a strategy must be put in place to ensure that these costs do not exceed the bearable point.

### **2.4 Empirical Review**

Joseph and Joyce (2018) investigated effect of cost reduction strategies on organization performance: a case of Kenya forest service. The study targeted 219 employees of Kenya Forest Service from which a sample size of 33 employees were selected to represent 219 employees from various management levels of Kenya Forest Service. The data was obtained from the respondents by use of structured closed and open-ended questionnaires. The study found out that planned recruitment and training has enhanced the performance of Kenya Forest Service through improved operations and reduction of conflict between the staff and members of the public as well as defining the job holder's position.

Akeem, (2017) study effect of Cost Control and Cost Reduction Techniques in Organizational Performance. A descriptive survey research was adopted. A total number of 50 questionnaires were administered and used for the study. The analysis of data collected was undertaken by applying appropriate statistical tools. Regression analysis was used to test the hypothesis with the use of SPSS. Based on the findings, it was evident that cost control has a positive impact on organizational performance and also the style of management has a positive impact on organizational performance.

Egbide et al (2019) Cost Reduction Strategies and the Growth of Selected Manufacturing Companies in Nigeria. This study examines the relationship between cost reduction strategies and the growth of manufacturing companies in Nigeria using data from annual reports of 40 manufacturing companies quoted on the Nigeria Stock Exchange within the period of 2012-2016. 40 manufacturing companies were sampled purposively for this study. The study took changes in material cost, changes in labour cost and changes in administrative overhead as variables for cost reduction strategies while changes in

turnover as the variable for Growth. Correlation analysis was conducted to determine the association cost reduction strategies and growth while, regression analysis was used to determine the impact of cost reduction strategies on the growth of manufacturing companies. Results showed a positive significant relationship between cost reduction strategies and growth of manufacturing companies in Nigeria.

Sharma, (2017) study Application of Cost Reduction Tools in Manufacturing Organizations at Pokhara. This study aims to evaluate the application of cost reduction tools in Nepalese manufacturing organizations with reference to Pokhara valley. Out of total manufacturing firm, only 10 organizations have been selected at least two samples from each stratum out of the target population. Primary data have been collected through the structured questionnaires by distributing it to the production manager or finance manager of the concerned organization. The information has been collected through unit visits. An empirical investigation has been conducted in order to find out various aspects of cost reduction tools. The major tool used for this purpose is the questionnaire. Nepalese manufacturing organizations are selecting the purchase of raw material, production planning and control as the area of reducing their cost. All of the organizations are conscious about TQM as the technique of cost reduction. Most of the organizations are applying product line rationalization, supply chain management, KAIZEN system, reengineering as the technique of cost reduction.

Aladwan., ALSinglawi and alhawtmeh (2018) study the applicability of target costing in Jordanian hotels industry. To achieve the study objectives the researcher employed a descriptive analytical method using a structured questionnaire addressed to managers in hotels departments such as marketing, accounting, design, research and development. A likert scale and one sample statistical t-test were applied to test the paragraphs and hypothesis of the study. The general findings of the study include the following: (1) Jordanian hotels staffs are highly aware of target costing and its great implementation benefits. (2) The essential requirement for implementing target costing approach is available in Jordanian hotels.

Iliemena and Adinoyi (2019) study Effect of Standard Costing on Profitability of Manufacturing Companies: Study of Edo State Nigeria. Extant literatures were reviewed, and three hypotheses developed and tested. The population of the study consisted of selected manufacturing firms in Benin City. In order to generate the necessary data for this study, primary method of data collection was adopted and applied through the administration of a questionnaire designed in a 5-point Likert scale. The formulated hypotheses were tested using Z-Test statistics at 5% alpha level. Findings generated in this study revealed that there is significant positive effect of standard costing on cost reduction. It was further observed that the more a firm practices standard costing, the more its profit increases.

Rashmi and Yathish (2017) study Analysis of Cost Control Mechanism - Karnataka Soaps and Detergent Limited (KS & DL), Sandal Wood Oil Division, Mysuru. The study is descriptive in nature. During the study, while analyzing the cost sheet investment on material and labour impact in the breakup of the overall cost of production it is observed that the break in the cost of production is creating variations between budgeted cost and

actual cost. Further analyses are carried out with the help of t test to find out the impact on overall performance of the business set between budgeted cost and actual cost. The test reveals a significant difference between the budgeted cost and actual cost and has succeeded in attaining cost control mechanism at KS & DL, as it is evident that in all the year's actual cost is less than budgeted cost.

Lawal (2017), discovered in his study that cost control has a positive impact on organizational performance. He examined the effect of cost control and cost reduction technique on organizational performance with major emphasis on budgetary control as an effective tool of cost reduction and cost control. He viewed the importance of cost reduction scheme as something that cannot be overstated and suggests that companies undertake frequent examination of costs in order to curb excessiveness, thereby, eliminating costs. It was concluded in his study that for an organization to experience more profit growth by producing quality goods and services, there is a need to control and reduce cost to the acceptable limit.

### **3.0 Methodology and Model**

#### **3.1 Research Design**

Descriptive survey was used because it largely focuses on vital facts, beliefs, opinion, demographic information, attitudes, motives and behaviors of correspondent giving responses to the research instrument, its uniqueness and relevance as it concentrates on descriptiveness of the event. (Lim 2013; Mithas, 2011).

#### **3.2 Population of the Study**

The population for the employees both top management and lower management of the selected manufacturing company. The selected manufacturing company was chosen because it is of the largest population in Oyo State. The target population of this study consisted of employees of SUMA manufacturing company.

#### **3.3 Sampling Method**

Convenience sampling is a type of non-probability sampling where members of the target population that meet certain practical criteria, such as easy accessibility, geographical proximity, availability at a given time, or the willingness to participate are included for the purpose of the study. Convenience sampling was used because it is affordable, easy and subject are readily available.

#### **3.4 Sample Size**

A sample size of eighty (80) respondents was selected from the population using Taro Yamane. The desired sample size was selected by use convenience sampling techniques.

#### **3.5 Method of Data Analysis**

The collected data were coded and recoded to accommodate the entire variables that the research measures. It was analysed with the aid of the Statistical Packages for Social Science (SPSS version 23.0). The analysis adopted descriptive statistical methods such as frequency counts and illustrated with tables. Correlations analyses were used to test the the relationship between cost reduction techniques antecedents and profitability.

#### **3.6 Operationalization of Variables**

$Y = F(X)$

Y= Dependent Variable

X=Independent Variable

From this research, the dependent variable = profitability, while independent variable = Cost Reduction Technique

$$Y=F(X)$$

Y= Profitability

X= Cost Reduction Technique

X= FM, MC, IM

P= f (CRT)

$Y_1 = P$

$X_1 =$  Fleet Management (FM)

$X_2 =$  Management Control (MC)

$X_3 =$  Improved Manpower (IM)

$Y_1 = F(X_1, X_2, X_3) \dots \dots \dots (i)$

$P = F(FM, MC, IM) \dots \dots \dots (iii)$

Where  $P = F(FM, MC, IM)$ .

## 4. Findings

### 4.1 Descriptive Analysis of Demographic Profile of the Respondents

The study found it fundamental to find out the broad information of the respondents since it structures the information under which the study can fairly obtain the pertinent information. the background information of the respondents were investigated in the first section of the questionnaire.

**Table 1: Analysis of Demographic Characteristics of Respondents**

Variables	Characteristics	Frequency	Percentages %
Age Distribution	18-25years	22	27.5%
	26-35years	35	43.8%
	36-45years	20	25%
	46-55years	3	3.7%
			100
Gender	Male	48	60%
	Female	32	40%
			100
Marital Status	Single	40	50%



	Married	30	37.5%
	Divorced	4	5%
	Separated	6	7.5%
			100
Educational Qualification	SSCE	10	12.5%
	NCE/OND	24	30%
	BSC/HND/B.E	25	31.3%
	MSC/M. ED/MBA	12	15%
	PhD	5	6.3%
	Others	4	5%
			100

**Data Source: Field Survey 2022**

Results presented in Table 1 depict that most of the respondents 22(27.5%) fall in age bracket of 18-25 years, 35(43.8%) fall in the age bracket of 26-35years, 20(25%) fall in the age bracket of 36-45years while 3(3.7%) fall in the age bracket of 46-55. The table also displayed that majority of the respondents 48(60%) were male while 32(40%) were female respondents. In addition, 40(50%) of the majority were single, 30(37.5%) of the majority were married, 4(5%) of the majority were divorced while 6(7.5%) were separated. With reference to educational qualification 10(12.5%) of the respondent are SSCE holder, 24(30%) of the respondent are NCE/OND holder, 25(31.3%) of the respondent are BSC/HND/B.E holder, 12(15%) of the respondent are MSC/M. ED/MBA holder, 5(6.3%) of the respondent are PhD holder while 4(5%) of the respondents are other educational qualifications.

## **4.2 Testing and Hypothesis**

### **4.3.1 Restatement of Hypothesis**

**Restatement of Hypothesis One ( $H_{01}$ ):** There is no significant relationship between fleet management and profitability in selected manufacturing company. The above hypothesis was tested using correlation analysis.

The results of the correlation analysis are presented in Table 2

Correlations			
		Fleet Management	Profitability
Fleet Management	Pearson Correlation	1	.564**
	Sig. (2-tailed)		.000
	N	80	80
Profitability	Pearson Correlation	.564**	1
	Sig. (2-tailed)	.000	
	N	80	80

**\*\*.** *Correlation is significant at the 0.01 level (2-tailed).*

The result of a bivariate Pearson correlation shows fleet management is positively correlated with profitability in selected manufacturing company. ( $r = 0.564$ ;  $P\text{-value} = 0.000 < 0.05$ ). Based on the result, hypothesis one was supported and conclude that significant relationship between fleet management and profitability in selected manufacturing company.

**Restatement of Hypothesis Two ( $H_{02}$ ):** There is no significant relationship between management control and profitability in selected manufacturing company.

The above hypothesis was tested using correlation analysis. The results of the correlation analysis are presented in the table 3 below.

Correlations			
		Management Control	Profitability
Management Control	Pearson Correlation	1	.111**
	Sig. (2-tailed)		.000
	N	80	80
Profitability	Pearson Correlation	.111**	1
	Sig. (2-tailed)	.000	
	N	80	80

**\*\*.** *Correlation is significant at the 0.01 level (2-tailed).*

The result of a bivariate Pearson correlation shows that management control is positively correlated with profitability in selected manufacturing company. ( $r = 0.111$ ;  $P\text{-value} = 0.000 < 0.05$ ). Based on the result, hypothesis two was supported and conclude that there is significant relationship between management control and profitability in selected manufacturing company. This implies that there is positive relationship between management control and profitability of the selected manufacturing company.

**Restatement of Hypothesis Three ( $H_{03}$ ):** There is no significant relationship between improved manpower and profitability in selected manufacturing company.

The above hypothesis was tested using correlation analysis. The results of the correlation analysis are presented in the table 4 below.

Correlations			
		Improved manpower	Profitability
Improved manpower	Pearson Correlation	1	.777**
	Sig. (2-tailed)		.000
	N	80	80
Profitability	Pearson Correlation	.777**	1
	Sig. (2-tailed)	.000	
	N	80	80

**\*\*.** *Correlation is insignificant at the 0.05 level (2-tailed).*

The result of a bivariate Pearson correlation shows that improved manpower is positively correlated with profitability in selected manufacturing company. ( $r = 0.777$ ;  $P\text{-value} = 0.000 < 0.05$ ). Based on the result, hypothesis three was supported and conclude that there is significant relationship between improved manpower and profitability in selected manufacturing company. This implies that there is positive relationship between improved manpower and profitability in selected manufacturing company

## 5. Discussions

Egbide, Ruth, Adegbola, Bamidele, Sunday, Olufemi, (2019) carried out study on Cost Reduction Strategies and the Growth of Selected Manufacturing Companies in Nigeria. The result shows that a positive significant relationship between cost reduction strategies and growth of manufacturing companies in Nigeria. This finding of Egbide *et al* is in line with the findings of this research work that revealed that there is significant relationship between improved manpower and profitability in selected manufacturing company. This implies that there is positive relationship between improved manpower and profitability of the selected manufacturing company.

## 6. Implication to the findings

The findings of this research work have implications for management of selected manufacturing companies on the importance and benefit of cost reduction technique and how best to manager can applied the cost reduction techniques in other to make profit.

## 7. Conclusions and Recommendations'

Based on the analysis of the study it can be concluded that there is significant relationship between cost reduction and techniques and profitability in selected manufacturing company. Based on the research finding Cost control and cost reduction scheme must be properly administered in an organization by setting realistic standard. Cost control should be operated in every department in an organization especially the production department in other to make sure that the numbers of finished goods are properly accounted for. Target and standard should not be vague set as this will be unrealistic in the course of comprising planned cost in an organization. For effective cost control to be achieved there should be proper data collection, data analysis and control administration. The target fixed cost in an undertaken should not be treated as permanent form. They should be reviewed whenever necessary and should be revised when conditions

change. An organization should have routine recruitment and training programs. This will ensure continuity of the services; improve the skills and knowledge of the staff members which will make them adapt to changing environment of the service points. Organizations should embrace automation since it saves turnaround time of service delivery, increases revenue, some services can be offered on-line saving resources as well as availability of information. Service outsourcing should only be done where the goods and services cannot be adequately provided by the members of the staff or the organization. Otherwise, more capacity building should be conducted to equip them with skills and knowledge.

### **8. Suggestion for Further Study**

From the above conclusion it should be recommended that the researchers can apply more tests on this study. They can use more sample size and add more company rather than this local company selected as a case study. Other variables of cost and reduction techniques should be considered on profitability.

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