BCA 1ST Semester

BCA-102 : FUNDAMENTALS OF MANAGEMENT

UNIT: 5

Controlling

Meaning of Controlling →

Controlling is one of the important functions of a manager. In order to seek planned results from the subordinates, a manager needs to exercise effective control over the activities of the subordinates. In other words, controlling means ensuring that activities in an organisation are performed as per the plans. Controlling also ensures that an organisation's resources are being used effectively and efficiently for the achievement of predetermined goals. Controlling is, thus, a goal-oriented function.

Controlling should not be misunderstood as the last function of management. It is a function that brings back the management cycle back to the planning function. The controlling function finds out how far actual performance deviates from standards, analyses the causes of such deviations and attempts to take corrective actions based on the same.

Importance of Controlling

Control is an indispensable function of management. Without control the best of plans can go awry. A good control system helps an organisation in the following ways:

(i) Accomplishing organisational goals: The controlling function measures progress towards the organisational goals and brings to light the deviations, if any, and indicates corrective action. It, thus, guides the organisation and keeps it on the right track so that organisational goals might be achieved.

(ii) Judging accuracy of standards: A good control system enables management to verify whether the standards set are accurate and objective. An efficient control system keeps a careful check on the changes taking place in the organisation and in the environment and helps to review and revise the standards in light of such changes.

(iii) Making efficient use o f resources: By exercising control, a manager seeks to reduce wastage and spoilage of resources. Each activity is performed in accordance with predetermined standards and norms. This ensures that resources are used in the most effective and efficient manner.

(iv) Improving employee motivation: A good control system ensures that employees know well in advance what they are expected to do and what are the standards of performance on the basis of which they will be appraised. It, thus, motivates them and helps them to give better performance.

(v) Ensuring order and discipline: Controlling creates an atmosphere of order and discipline in the organisation. It helps to minimise dishonest behaviour on the part of the employees by keeping a close check on their activities.

(vi) Facilitating coordination in action: Controlling provides direction to all activities and efforts for achieving organisational goals. Each department and employee is governed by pre‐determined standards which are well coordinated with one another. This ensures that overall organisational objectives are accomplished.

Limitations of Controlling

Although controlling is an important function of management, it suffers from the following limitations.

- **(i) Difficulty in setting quantitative standards**: Control system loses some of its effectiveness when standards cannot be defined in quantitative terms. This makes measurement of performance and their comparison with standards a difficult task. Employee morale, job satisfaction and human behaviour are such areas where this problem might arise.
- **(ii) Little control on external factors**: Generally an enterprise cannot control external factors such as government policies, technologies , competition etc.
- **(iii) Resistance from employees**: Control is often resisted by employees. They see it as a restriction on their freedom. For instance, employees might object when they are kept under a strict watch with the help of Closed Circuit Televisions (CCTVs).
- **(iv) Costly affair**: Control is a costly affair as it involves a lot of expenditure, time and effort. A small enterprise cannot afford to install an expensive control system. It cannot justify the expenses involved. Managers must ensure that the costs of installing and operating a control system should not exceed the benefits derived from it. The box on Control System at FedEx gives an overview of the control system used by FedEx and how it helped FedEx to increase its profits.

Controlling Process

Controlling is a systematic process involving the following steps.

1. Setting performance standards

2. Measurement of actual performance

3. Comparison of actual performance with standards

4. Analysing deviations

5. Taking corrective action

Step 1: Setting Performance Stan�dards: The first step in the controlling process is setting up of performance standards. Standards are the criteria against which actual performance would be measured. Thus, standards serve as benchmarks towards which an organisation strives to work. Standards can be set in both quantitative as well as qualitative terms. For instance, standards set in terms of cost to be incurred, revenue to be earned, product units to be produced and sold, time to be spent in performing a task, all represents quantitative standards. Sometimes standards may also be set in qualitative terms. Improving goodwill and motivation level of employees are examples of qualitative standards. The table in the next page gives a glimpse of standards used in different functional areas of business to gauge performance.

Step 2: Measurement of Actual Performance: Once performance standards are set, the next step is measurement of actual performance. Performance should be measured in an objective and reliable manner. There are several techniques for measurement of performance. These include personal observation, sample checking, performance reports, etc. As far as possible, performance should be measured in the same units in which standards are set as this would make their comparison easier. It is generally believed that measurement should be done after the task is completed. However, wherever possible, measurement of work should be done during the performance. For instance, in case of assembling task, each part produced should be checked before assembling. Similarly, in a manufacturing plant, levels of gas particles in the air could be continuously monitored for safety.

Step 3: Comparing Actual Performance with Standards: This step involves comparison of actual performance with the standard. Such comparison will reveal the deviation between actual and desired results. Comparison becomes easier when standards are set in quantitative terms. For instance, performance of a worker in terms of units produced in a week can be easily measured against the standard output for the week.

Step 4: Analysing Deviations: Some deviation in performance can be expected in all activities. It is, therefore, important to determine the acceptable range of deviations. Also, deviations in key areas of business need to be attended more urgently as compared to deviations in certain insignificant areas. Critical point control and management by exception should be used by a manager in this regard.

Techniques of Managerial Control

The various techniques of managerial control may be classified into two broad categories: traditional techniques, and modern techniques.

Traditional Techniques

Traditional techniques are those which have been used by the companies for a long time now. However, these techniques have not become obsolete and are still being used by companies. These include:

(a) Personal observation

(b) Statistical reports

(c) Breakeven analysis

(d) Budgetary control

Modern Techniques

Modern techniques of controlling are those which are of recent origin and are comparatively new in management literature. These techniques provide a refreshingly new thinking on the ways in which various aspects of an organisation can be controlled. These include:

(a) Return on investment

(b) Ratio analysis

(c) Responsibility accounting

(d) Management audit

(e) PERT and CPM

(f) Management information system

Traditional Techniques →

a) Personal Observation →

This is the most traditional method of control. Personal observation enables the manager to collect first hand information. It also creates a psychological pressure on the employees to perform well as they are aware that they are being observed personally on their job. However, it is a very time-consuming exercise and cannot effectively be used in all kinds of jobs.

b) Statistical Reports

Statistical analysis in the form of averages, percentages, ratios, correlation, etc., present useful information to the managers regarding performance of the organisation in various areas. Such information when presented in the form of charts, graphs, tables, etc., enables the managers to read them more easily and allow a comparison to be made with performance in previous periods and also with the benchmarks.

c) Breakeven Analysis

Breakeven analysis is a technique used by managers to study the relationship between costs, volume and profits. It determines the probable profit and losses at different levels of activity. The sales volume at which there is no profit, no loss is known as breakeven point. It is a useful technique for the managers as it helps in estimating profits at different levels of activities. The figure 1 shows breakeven chart of a firm. Breakeven point is determined by the intersection of Total Revenue and Total Cost curves. The figure shows that the firm will break even at 50,000 units of output. At this point, there is no profit no loss. It is beyond this point that the firm will start earning profits.

Breakeven point can be calculated with the help of the following formula:

$$\textbf{Breakeven Point} = \frac{\textbf{Fixed Costs}}{\textbf{Selling price per unit} - \textbf{Variable cost per unit}}$$

d) Budgetary Control

Budgetary control is a technique of managerial control in which all operations are planned in advance in the form of budgets and actual results are compared with budgetary standards. This comparison reveals the necessary actions to be taken so that organisational objectives are accomplished. A budget is a quantitative statement for a definite future period of time for the purpose of obtaining a given objective. It is also a statement which reflects the policy of that particular period. It will contain figures of forecasts both in terms of time and quantities.

Modern Techniques

a) Return on Investment

Return on Investment (RoI) is a useful technique which provides the basic yardstick for measuring whether or not invested capital has been used effectively for generating reasonable amount of return. RoI can be used to measure overall performance of an organisation or of its individual departments or divisions. It can be calculated as under.

$$\textbf{RoI} = \frac{\text{Net income before interest and tax}}{\text{Capital Employed}}$$

Net Income before or after tax may be used for making comparisons. Total investment includes both working as well as fixed capital invested in business. According to this technique, RoI can be increased either by increasing sales volume proportionately more than total investment or by reducing total investment without having any reductions in sales volume.

RoI provides top management an effective means of control for measuring and comparing performance of different departments. It also permits departmental managers to find out the problem which affects RoI in an adverse manner.

b) Ratio Analysis

Ratio Analysis refers to analysis of financial statements through computation of ratios. The most commonly used ratios used by organisations can be classified into the following categories:

1. Liquidity Ratios: Liquidity ratios are calculated to determine short-term solvency of business. Analysis of current position of liquid funds determines the ability of the business to pay the amount due to its stakeholders.

2. Solvency Ratios: Ratios which are calculated to determine the long-term solvency of business are known as solvency ratios. Thus, these ratios determine the ability of a business to service its indebtedness.

3. Profitability Ratios: These ratios are calculated to analyse the profitability position of a business. Such ratios involve analysis of profits in relation to sales or funds or capital employed.

4. Turnover Ratios: Turnover ratios are calculated to determine the efficiency of operations based on effective utilisation of resources. Higher turnover means better utilisation of resources.

c) Responsibility Accounting

Responsibility accounting is a system of accounting in which different sections, divisions and departments of an organisation are set up as 'Responsibility Centres'. The head of the centre is responsible for achieving the target set for his centre.

Responsibility centres may be of the following types:

1. Cost Centre: A cost or expense centre is a segment of an organisation in which managers are held responsible for the cost incurred in the centre but not for the revenues. For example, in a manufacturing organisation, production department is classified as cost centre.

2. Revenue Centre: A revenue centre is a segment of an organisation which is primarily responsible for generating revenue. For example, marketing department of an organisation may be classified as a revenue center.

3. Profit Centre: A profit centre is a segment of an organisation whose manager is responsible for both revenues and costs. For example, repair and maintenance department of an organisation may be treated as a profit center if it is allowed to bill other production departments for the services provided to them.

4. Investment Centre: An investment centre is responsible not only for profits but also for investments made in the centre in the form of assets.

d) Management Audit

Management audit refers to systematic appraisal of the overall performance of the management of an organisation. The purpose is to review the efficiency and effectiveness of management and to improve its performance in future periods. It is helpful in identifying the deficiencies in the performance of management functions. Thus, management audit may be defined as evaluation of the functioning, performance and effectiveness of management of an organisation.

The main advantages of management audit are as follows.

1. It helps to locate present and potential deficiencies in the performance of management functions.

2. It helps to improve the control system of an organisation by continuously monitoring the performance of management.

3. It improves coordination in the functioning of various departments so that they work together effectively towards the achievement of organisational objective

e) PERT and CPM

PERT (Programme Evaluation and Review Technique) and CPM (Critical Path Method) are important network techniques useful in planning and controlling. These techniques are especially useful for planning, scheduling and implementing time bound projects involving performance of a variety of complex, diverse and interrelated activities. These techniques deals with time scheduling and resource allocation for these activities and aims at effective execution of projects within given time schedule and structure of costs.

The steps involved in using PERT/ CPM are as follows:

1. The project is divided into a number of clearly identifiable activities which are then arranged in a logical sequence.

2. A network diagram is prepared to show the sequence of activities, the starting point and the termination point of the project.

3. Time estimates are prepared for each activity. PERT requires the preparation of three time estimates – optimistic (or shortest time), pessimistic (or longest time) and most likely time. In CPM only one time estimate is prepared. In addition, CPM also requires making cost estimates for completion of project.

4. The longest path in the network is identified as the critical path. It represents the sequence of those activities which are important for timely completion of the project and where no delays can be allowed without delaying the entire project.

f) Management Information System

Management Information System (MIS) is a computer-based information system that provides information and support for effective managerial decision-making. A decision-maker requires up-to-date, accurate and timely information. MIS provides the required information to the managers by systematically processing a massive data generated in an organisation. Thus, MIS is an important communication tool for managers.

MIS also serves as an important control technique. It provides data and information to the managers at the right time so that appropriate corrective action may be taken in case of deviations from standards.

MIS offers the following advantages to the managers:

1. It facilitates collection, management and dissemination of information at different levels of management and across different departments of the organisation.

2. It supports planning, decision‑making and controlling at all levels.

3. It improves the quality of information with which a manager works.

4. It ensures cost effectiveness in managing information.

5. It reduces information overload on the managers as only relevant information is provided to them.

Relationship between Planning and Controlling

Planning and controlling are inseparable twins of management. A system of control presupposes the existence of certain standards. These standards of performance which serve as the basis of controlling are provided by planning. Once a plan becomes operational, controlling is necessary to monitor the progress, measure it, discover deviations and initiate corrective measures to ensure that events conform to plans. Thus, planning without controlling is meaningless. Similarly, controlling is blind without planning. If the standards are not set in advance, managers have nothing to control. When there is no plan, there is no basis of controlling.

Planning is clearly a prerequisite for controlling. It is utterly foolish to think that controlling could be accomplished without planning. Without planning there is no predetermined understanding of the desired performance. Planning seeks consistent, integrated and articulated programmes while controlling seeks to compel events to conform to plans.

Planning is basically an intellectual process involving thinking, articulation and analysis to discover and prescribe an appropriate course of action for achieving objectives. Controlling, on the other hand, checks whether decisions have been translated into desired action. Planning is thus, prescriptive whereas, controlling is evaluative. It is often said that planning is looking ahead while controlling is looking back. However, the statement is only partially correct. Plans are prepared for future and are based on forecasts about future conditions. Therefore, planning involves looking ahead and is called a forward-looking function. On the contrary, controlling is like a postmortem of past activities to find out deviations from the standards. In that sense, controlling is a backward‑looking function.

However, it should be understood that planning is guided by past experiences and the corrective action initiated by control function aims to improve future performance. Thus, planning and controlling are both backward-looking as well as a forward-looking function.

Thus, planning and controlling are interrelated and, in fact, reinforce each other in the sense that

1. Planning based on facts makes controlling easier and effective; and

2. Controlling improves future planning by providing information derived from past experience.