CHAPTER -8
CONTROLLING

Managerial functions commence with planning and end at controlling. Planning involves setting up objectives while controlling seeks to ensure performance as per plan.

MEANING AND DEFINITION OF CONTROLLING

Controlling is the process of ensuring that actual activities conform to planned activities. It is one of the important functions of management .it is the evaluation and correction of the performance of subordinates.

'Controlling is the measuring and correcting of activities of subordinates to assume that events conform to plans' -**Koontz and O 'Donnel**

"control is the process of taking steps to bring actual results and desired results closing together' **– Philip Kotler**

"Management control seeks to compel events to confirm to plans' **- Billy E . Goetz**

"Management control is the process by which managers assume that resources are obtained and used effectively in accomplishment of organisation's objectives"

- **Robert Antony**

Controlling at a glance:

- Controlling is a regulatory function
- It is the end function of management
- It is a dynamic and continuous function
- It is done by all managers at all levels(pervasive)
- It is the evaluation and correction of activities
- Controlling is forward liking

IMPORTANCE OF CONTROLLING

Control is an indispensable function of management .without effective system of control , planned activities cannot be properly implemented . The following are the major advantages of controlling

1. **Accomplishing organizational goals**:- It is through controlling that managers ensure the execution of plans and accomplishment of goals. Controlling is regarded as key to the success of an organization.
2. **Correction of deviation:-** Evaluating performance and correcting deviations are the basic functions of controlling. Thus it prevents mistakes being repeated in future.

3. **Optimum utilization of resources**:- Controlling is essential for securing the best possible use of human, physical and financial resources. A good system of control helps to prevent misuse and wastage of resources. It helps to minimize the cost of operation and to improve quality.
4. **Improve employee motivation and morale:-** A good control system discovers efficient and inefficient employees. Inefficient employees are provided necessary training. Thereby their weakness may be removed and they can contribute their best to the organization.
5. **Ensuring order and discipline**:- Controlling creates an atmosphere of order and discipline in the organization. It helps to minimize dishonest behaviour on the part of employees by keeping close check on their activities
6. **Facilitate Coordination**:- Controlling helps in integration of activities through unity of action. it provides unity of direction
7. **Better Planning:-** A good control system will reveal the shortcomings of a plan. This will facilitate future planning.

LIMITATIONS OF CONTROLLING

The following are the major limitations of control system

1. **Difficulty in setting quantitative standards**:- Control loses its effectiveness when standards of performance cannot be fixed in quantitative term. For eg. It is very difficult to measure human behavior and employee morale.
2. **Little control on external factors**:- An organization cannot control the external factors. These factors may be government policy, technical changes, changes in fashion etc. 3. **Resistance from employees:-** Employees may resist this function of management. They see it as a restriction of their freedom. For eg. Placing of CCTV may resists by employees.
4. **Costly affair (Expensive):-** The exercise of control requires a lot of time and efforts. So it is time consuming and expensive function. A small enterprise cannot afford to install an expensive control system.

RELATION BETWEEN PLANNING AND CONTROLLING

Planning and controlling are inseparable twins of management (Siamese of Management).They are considered the two aspect of the same function. The performance of one function without the other will go in vain.

Without planning, there is no basis for controlling activities and without effective system of control, planned activities cannot be properly implemented. Planning without control is meaningless and control without planning is blind. Therefore it is often said planning leads to controlling, controlling leads to planning.

Planning decides what is to be done in future and controlling makes sure that it is being done as planned. Planning without controlling is ineffective. On the other side , if there is no plan nothing to be controlled. Both planning and controlling are the two sides of the same coin The mutual relationship can be depicted as

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

1. Planning based on facts making controlling easier and effective and
2. Controlling improves future planning by providing information derived from past experience.

CONTROLLING PROCESS

Controlling is a systematic process involving the following steps

1. Establishing standards of performance
2. Measurement of actual performance
3. Comparison of actual performance with standards
4. Analysing deviation
5. Taking corrective action

1. **Establishing standard of performance:**- The first step in the process of control is to set a standard for performance. Standards are determined on the basis of objectives to be attained. Standards serve as benchmarks towards which an organization strives to work. It is the criterion against which actual performance can be compared. Generally standard is expressed in terms of quality, quantity, cost and Time. The standards should be simple, attainable, definite, reasonable, quantitative, and flexible .

2. **Measurement of actual performance**:- Once performance standards are set , the next step is measurement of actual performance. It is the assessment of output both quantitatively and qualitatively. There are several techniques for measurement of performance. These include personal observation. Sample checking, performance report 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.
3. **Compare actual performance with standard**: The third step in control process is the comparison of actual performance with the standard. It reveals the deviations from the standards. If the performance matches the standard, it may assume that everything is under control..

4. **Analysing Deviations:-** At this stage the extent of the deviation and the causes are determined. Deviation means gap between actual performance and standards. Deviation

may be positive or negative. Deviations in key areas of business require urgent attention. Managers can rely on the following in this regard.

CRITICAL POINT CONTROL: It is neither economical nor easy to keep a check on each and every activity in an organization. Control should, therefore focus a key result areas(KRA) which are critical to the success of an organization. These are set as critical points. If anything get wrong at the critical points the entire organization suffers.

MANAGEMENT / CONTROL BY EXCEPTION:-It is based on the belief that an attempt to control everything results in controlling nothing. All deviations need not to be brought to the attention of management. Usually only those deviations which seems exceptionally high and which cannot be solved by lower level management alone, should be reported to top management. This is what is called management by exception.

Advantages of Critical point control and management by exception

a. It saves time and efforts of Top level management as they deal with only significant deviations
b. It focusManagerial attention on important areas.
c. It facilitates delegation of authority and increase morale of the employees
d. It identifies critical problems which need timely action to keep organization in right track.

5. **Taking Corrective action**: The last but most important step in the control process is of taking corrective action. Corrective action consists of curative as well as preventive control measures. Eg

Causes of deviation	Corrective action to be taken
1. Defective Material	- Change the quality specification for material used
2. Defective Machinery	- Repair the existing machine/ replace the machine
3. Defective process	- Modify the existing process

TECHNIQUES OF MANGERIAL CONTROL: Managerial control techniques may broadly be classified into two

1. Traditional Techniques   2. Modern Techinique

TRADITIONAL TECHNIQUES:-
These are techniques used by companies for long time these techniques haven't become obsolete and still being used. These include

- ***Personal Observation***
- ***Statistical Reports***
- ***breakeven analyses***
- ***. Budgetary control***

a. **PERSONAL OBSERVATION**:- This is the most traditional method of control. Personal observation enables the manager to collect firsthand information about the employees.

It creates a psychological pressure on employees to perform well as they are personally observed. But it is time consuming and cannot be employed in all situations.

b. **STATISTICAL REPORTS:** Statistical analysis in the form of averages, ratios, correlations etc. present useful information to the mangers regarding the performance at various areas of the organization. It provides the information for inter firm comparison and future decision making.

c. **BREAK EVEN ANALYSIS:-** Break even analysis is a technique used by managers to study the relationship between costs volume and profit (CVP). It determines the probable profits and losses at different levels of activity. The sales volume at which there is no profit or loss is known as break-even point. ie. Total Revenue = Total cost.

$$\text{Break even point} = \frac{\text{fixed cost}}{\text{selling price per unit} - \text{variable cost per unit}} = \frac{\text{fixed cost}}{\text{contribution per unit}}$$

Break-even point analysis enables the management to have a check on the variable cost and also determine the levels of activity at which firm can make its targeted profit.

d. **BUDGETARY CONTROL:** A budget is a numerical or quantitative statement for a definite period of time for the purpose of obtaining a given objectives. Budgeting means the process of preparing budgets. Budgetary control is a technique of controlling the activities of an organization with the help of budgets. It involves the comparison of actual performance with the budgetary standards. Comparison reveals the reasons for variance to take corrective action to achieve the organizational objective.

Following are the important types of budgets.

Sales Budget*: a statement of what an organization expects to sell in terms of quality as well as value.*
Production Budget*:- a statement of what an organization plans to produce in the budgeted period.*
Material budget*: A statement of estimated quality and cost of materials required for production.*
Cash Budget*:- Anticipated Cash inflows and outflows for the budgeted period.* ***Capital Budget****: Estimated spending on major long term assets like new factory or major equipment.*
Research and Development Budget*: Estimated spending for the development or refinement of products and processes.*

Advantages of Budgetary Control:

1. Budgetary Control guides the management in planning and policy formation
2. It facilitates ‘management by exception’ by identifying areas which require special attention
3. It results the coordinated efforts of all individuals and departments of the organization.
4. It aims maximization of profit through cost control and proper utilization of resources.
5. It is a good guide to the management for making future plan.
6. It minimizes wastages and losses and hence increases productivity.

MODERN TECHNIQUES:-

Modern techniques are of recent origin and new to management literature. It include the following

- Return on Investment (ROI).
- Ratio Analysis
- Responsibility Accounting
- Management Audit
- PERT and CPM
- Management Information system (MIS)

a. **RETURN ON INVESTMENT (ROI):-** Return on investment is a yardstick for measuring the efficiency of the business to earn reasonable amount of return on capital investment. ROI can be used for measuring overall profitability or performance of the organization or its departments.

$$ROI = \frac{\text{Net income}}{\text{Total Investment}} \times 100$$

Net income may be either the profit before tax or after tax. Total investment includes both working as well as fixed capital invested in the business. A high ratio implies better performance of the business.

b. **RATIO ANALYSIS:-** a ratio is an arithmetic expression of relationship between two figures. Ratio analysis refers to analysis of financial statements through computation of ratios. Commonly used accounting ratios are

1. Liquidity Ratios: Liquidity ratios are calculated to determine short term solvency of business. Ie. Ability to meet short term obligation. Eg:- current ratio, quick ratio.

2. Solvency ratios:- Ratios which are calculated to determines the long term solvency of business are known as solvency ratios. Thus these ratios determine the ability of a business to service its indebtedness.
   Eg. Debt- equity ratio, proprietary ratio, Interest coverage ratio.

3. Profitability Ratios:- These ratios are calculated to analyses the profitability in relation to sales or capital investment in business.
   Eg: Gross profit ratio, Net profit ratio, Return on capital employed.

4. Turn over Ratios/ Activity Ratios:- It is calculated to determine the efficiency of operation based on effective utilization of resources. Higher turnover means better utilization of resources.
   Eg: Inventory Turnover Ratios, Stock Turnover ratio, Debtors Turnover Ratios

c. **RESPONSIBILITY ACCOUNTING:-** It is a system of accounting in which different sections/ departments/divisions in an organization are taken as 'Responsibility Centre's'. The person in charge of a Centre is responsible for achieving the target fixed. Responsibility Centres are of the following types:

1. **Cost Centre/Expense Centre**:- Cost Centre is a segment of an organization in which mangers are held responsible for the cost incurred. In the Centre but not for the revenues. Eg. In a manufacturing organization, production department is classified as cost Centre.
2. **Revenue Centre:-** A revenue Centre is a segment of organization which is primary responsible for generating revenue. Eg:- Marketing department of an organization may be classified as a revenue Centre.
3. **Profit Centre:-** A profit Centre is a segment of an organization whose manger is responsible for both revenues and costs. Eg. Repairs and maintenance department may be treated as a profit Centre provided it bills other departments in the organization for the services rendered to them.

4. **Investment Centre:-** This Centre is not only responsible for profit but for investment made in it in the terms of assets. The investment is separately calculated and return on investment is taken as the basis for judging the performance of the Centre

d. **MANGEMENT AUDIT:-** Management Audit refers to systematic appraisal of the overall performance of the management of an organization. The purpose is to review the efficiency and effectiveness of management and to improve its performance in future periods. It is helps in identifying the deficiencies in the performance of the management function. Thus management audit may be defined as evaluation of the functioning , performance and effectiveness of management of an organization.

Advantages of Management Audit:

1. It helps to locate present and potential deficiencies in the performance of management function
2. It suggests the ways and means of increasing managerial efficiency.
3. It improves the coordination in the functioning of various department so that they work together effectively towards the achievement of organizational objectives.
4. It ensures updating of existing managerial policies and strategies in the light of environmental changes.

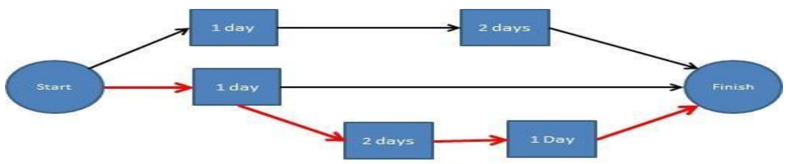
Conducting this kind of audit may create problem as there is no standards for it. Also management audit is not compulsory under the law.

e. NETWORK TECHNIQUES (PERT & 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. Both are decision making tools assisting in project completion. These techniques concentrate on time scheduling and resource allocation and aim at effective project execution within the time frame and costs.

Steps involved in using PERT/CPM

1. Arrange all activities in a logical sequence
2. A network diagram is prepared to show the sequences of activities, the starting point and termination point of the projects.
3. Three time estimates - optimistic, most likely and pessimistic - are made.
4. The Longest path in the network is identified **the critical path.** All activities lying in the critical path are called Critical activities.
5. Plan may be modified for prompt execution and timely completion of the project.



Critical Path = 4 Days

PERT and CPM are used extensively in areas like ship building, construction projects, aircraft manufacture. Etc.

f. **MANGEMENT INFORMATION SYSTEM (MIS**): -

Management Information System is a computer based information system that provides information and support for effective managerial decision making. MIS is an important communication tool for mangers. MIS is also serving as an important control technique. MIS provides the required information to the mangers at the right time so that appropriate corrective action may take in case of deviation from standards.

Advantages of MIS

1. It helps in planning , decision making and controlling in all levels
2. It improves the quality of information with which a manger works
3. It ensures cost effectiveness in managing information.
4. Mangers are free from information overload.
5. It facilitates collection and distribution of information among different levels of management