Class 12

Business Studies

Chapter - 8

Controlling

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Controlling

Controlling is the process through which management ensures that the actual performance conforms to the planned performance

Controlling

Controlling discovers deviation from the results expected

It also identifies the reasons for deviations and suggests suitable action to avoid their recurrence in future

Importance of Controlling

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Importance of Controlling

1. Accomplishing organizational goals

It measures actual performance with standards and making corrective actions on deviations, so that the organization can achieve its goals smoothly

Importance of Controlling

2. Judging accuracy of standards

Controlling helps to check the accuracy of standards in changing environment, which helps to revise the standards if needed

Importance of Controlling

3. Efficient use of resources

Controlling seeks to reduce wastages of resources

Importance of Controlling

4. Improving employee motivation

Controlling ensures employee awareness regarding what is expected to do and what is the standards fixed on him, so that he will be motivated to give better performance

Importance of Controlling

5. Ensures order and discipline

There is a close watch on the activities of all employees

Importance of Controlling

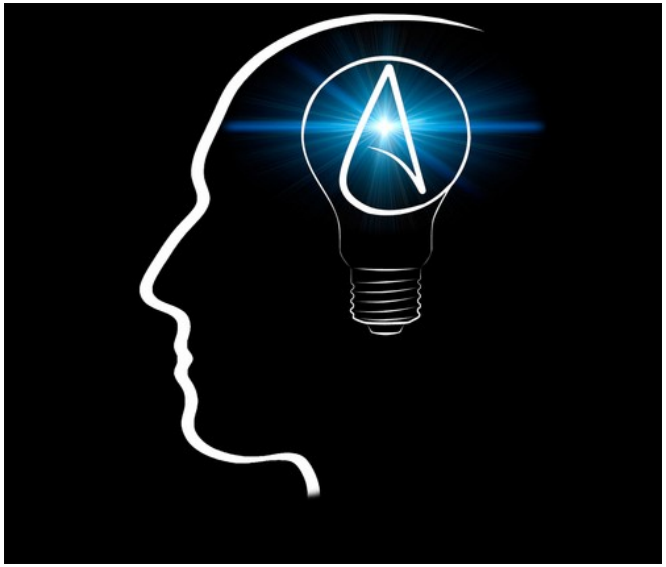
6. Coordination

To coordinate the activities of different persons and departments, an effective system of control is necessary

Importance of Controlling

7. Decision making

The process of control is complete when corrective actions are taken



It will lead to make better decisions in future

Importance of Controlling

1. Accomplishing organizational goals
2. Judging accuracy of standards
3. Efficient use of resources
4. Improving employee motivation
5. Ensures order and discipline
6. Coordination

6. Coordination

Limitations of Controlling

Limitations of Controlling

1. Difficulty in setting standards

Controlling will be effective only when standards are fixed in quantitative terms

Employee Morale

Employee morale, job satisfaction, customer response etc. cannot be expressed quantitatively, so that controlling becomes less effective

Limitations of Controlling

2. Little control on external factors

External factors such as Government policy, technological changes, competition etc. cannot be controlled by the organization

Limitations of Controlling

3. Resistance from employees

Employees may oppose the control measures taken by the firm, because they may feel that it will reduce their freedom

E.g., CCTV, Punching System, Feedback calls to customers etc.

Limitations of Controlling

4. Costly affair

Small organizations cannot afford to install an effective control system as it is very costly

Importance of Controlling

1. Accomplishing organizational goals
2. Judging accuracy of standards
3. Efficient use of resources
4. Improving employee motivation
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6. Coordination

6. Coordination

Relationship between Planning & Controlling

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Planning & Controlling

The entire planning process will turn to be waste unless adequate control measures are exercised

Planning & Controlling

a. Interdependent and inseparable

Planning and control are interdependent and inseparable functions of management.

Without a plan there is nothing to control

Thus planning is useless without control and controlling is useless without plan

Planning & Controlling

b. Interrelated and reinforce each other

i) Planning makes controlling easier and effective

ii) Controlling reveals the shortcomings of plans and calls for improvement in future

Planning & Controlling

c. Looking ahead and looking back

Planning is looking ahead while controlling is looking back

Plans are prepared for future

Controlling is the post mortem of past activities

Relation between Planning & Controlling

a. Interdependent and inseparable

b. Interrelated and reinforce each other

c. Looking ahead and looking back

Controlling Process

(Steps in Controlling)

Controlling Process

5. Taking Corrective Actions 5

4. Analysing Deviations 4

3. Comparison of Actual Performance 3

2. Measurement of Actual Performance 2

1. Setting Standards 1

Controlling Process

1. Setting performance Standards

To achieve the goals, standards of performance have to be determined in planning itself

Controlling Process

a) Quantitative Standards

Standards must be in concrete and tangible forms which will make evaluation process easy

Eg: Cost of production for one unit is Rs.100 etc.

Controlling Process

b) Qualitative Standards

Standards can also be in intangible forms

Eg: The results expected from a training programme, loyalties of workers, Improving motivation level of employees, etc.

Controlling Process

2. Measurement of actual performance

Actual performance of each activity in terms of quality and quantity should be measured

Controlling Process

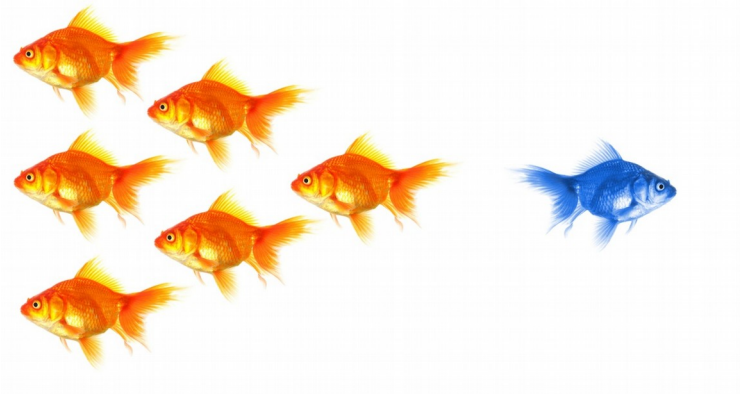
3. Comparison of actual performance with standards

Comparison of actual performance with the standards reveals the deviations between actual and desired results

Controlling Process

4. Analysing deviations

The extent of deviations and causes of such deviations are to be found out



It is important to ascertain whether deviations are within the expected range

Deviations in key areas of business require urgent attention

Methods of Analysing Deviations in Key areas

a) Critical Point Control

The control measures should be focused on **K**ey **R**esult **A**reas (KRAs) which are critical in the success of an organization

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These KRAs are the Critical Points, if anything goes wrong at this critical point, the entire organization will suffer

Eg: 5% increase in labour cost is a serious matter than 20% increase in postal charges

Methods of Analysing Deviations in Key areas

b) Management by Exception (MBE) / Control by Exception

All deviations need not be brought to the attention of top management

Only those deviations which seem exceptionally high and which cannot be easily solved by lower level management alone should be reported to top management

Controlling Process

5. Taking corrective actions

As soon as deviations are reported, it is the duty of the executives to take steps to correct the past action so that deviations may not occur again and the plans are properly executed

If there is no deviation or if the deviation is within the permissible limit, let the situation remains as it is

Controlling Process

1. Setting performance Standards

2. Measurement of actual performance

3. Comparison of actual performance with standards

4. Analysing deviations

5. Taking corrective actions

Controlling Process

Cause of deviation	Corrective action to be taken
Defective material	Change the supplier or quality
Defective machinery	Repair or replace
Obsolete machinery	Undertake technological up gradation
Increase in labour turnover	Improve working conditions and provide better incentives
Defective process	Modify the existing process

Techniques of Managerial Control

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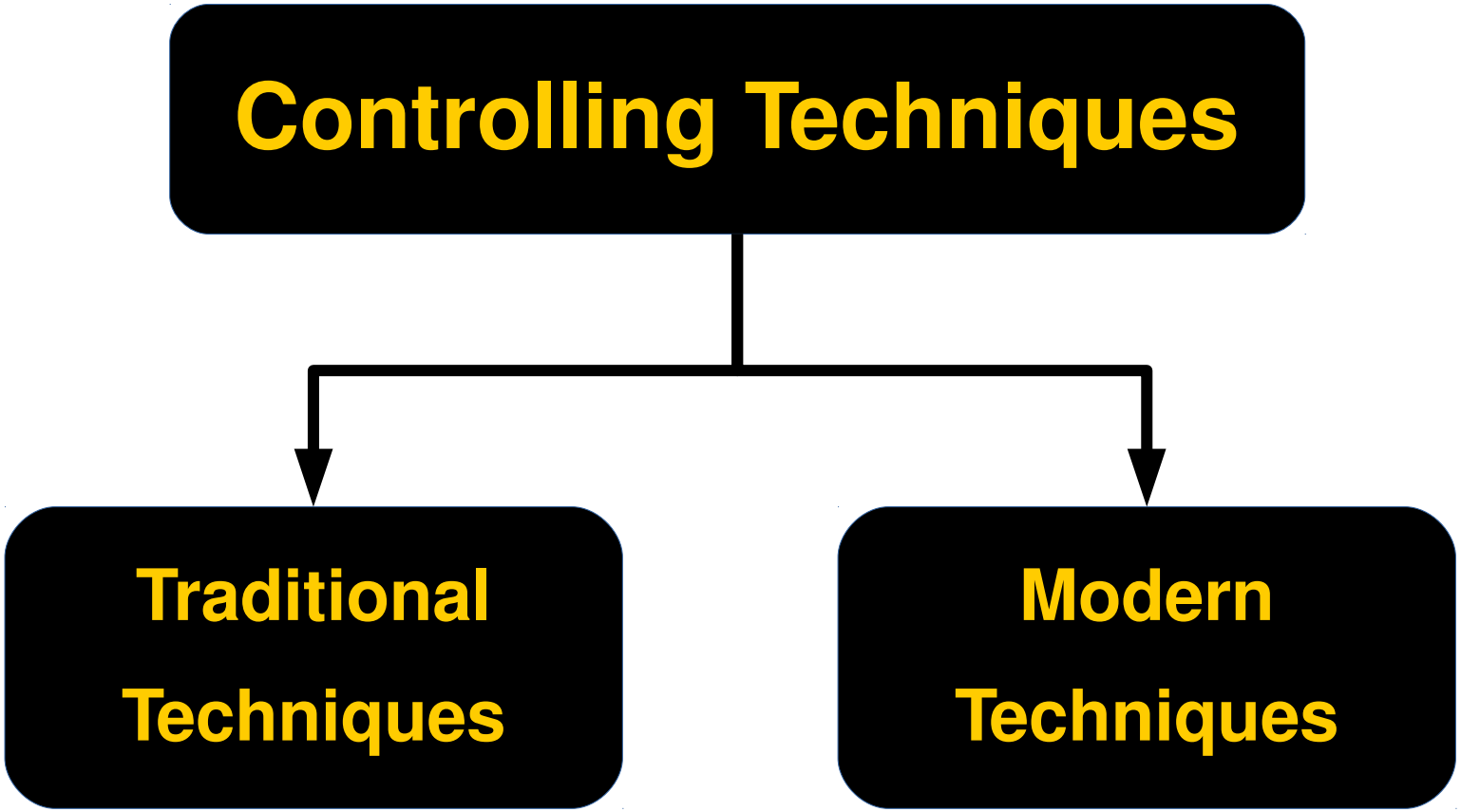

Controlling Techniques
Traditional Techniques
Modern Techniques

Traditional Techniques

1. Personal observation

Personal observation on the employee may create a psychological pressure to perform well

Traditional Techniques

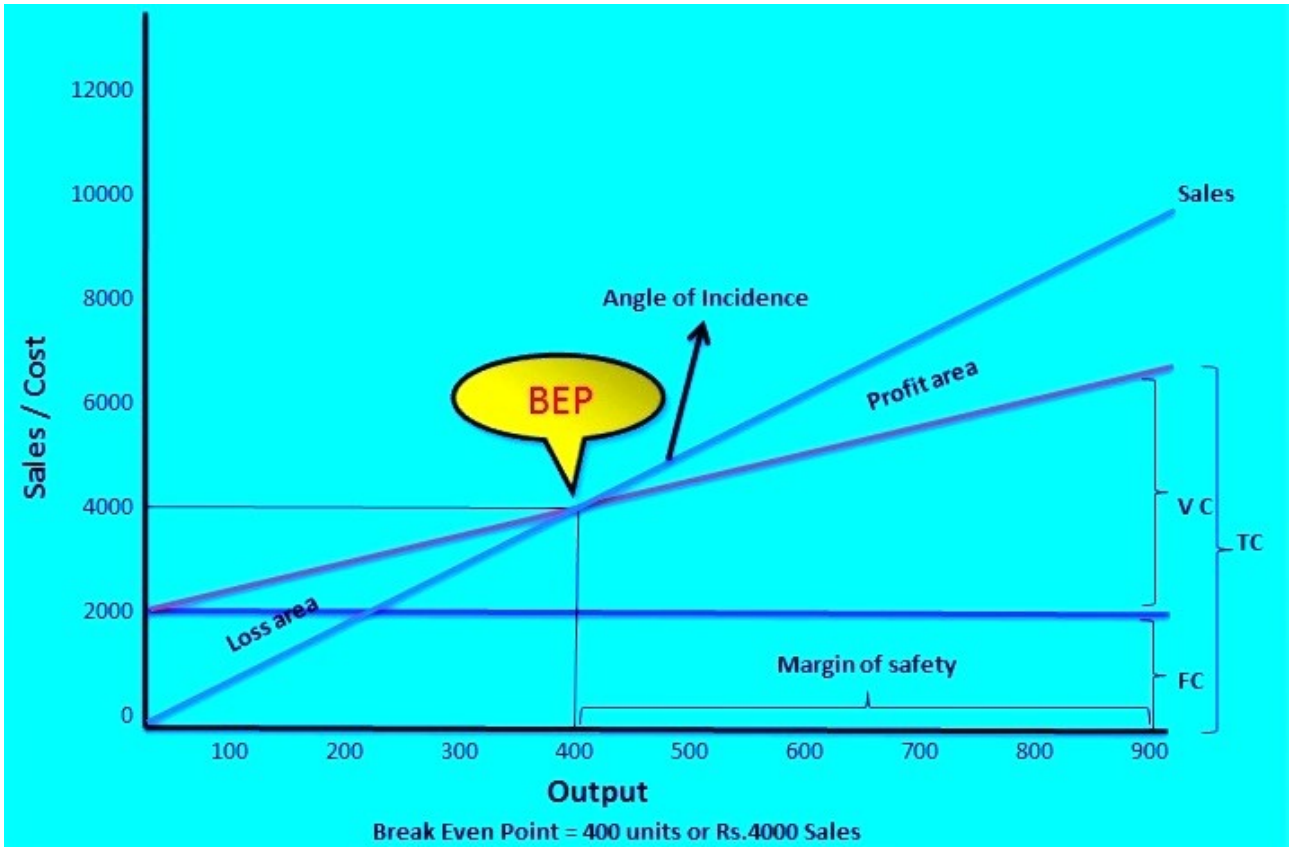
2. Statistical reports

Statistical information regarding performance of employees in the form of charts, graphs, tables etc. enable the managers to interpret them and to make comparison

Traditional Techniques

3. Break-even analysis

The level of operation where total revenue or sales are equal to total cost is called the break-even point



At this point (sales volume) the firm makes no profit no loss

Traditional Techniques

4. Budgetary control

Controlling the activities of an organization with the help of budgets

It involves the comparison of actual performance with the budgetary standards

E.g. Sales budget, production budget, Materials budget etc.

Advantages of budgetary control

1. Budget is a guidance for management in planning and policy formulation.

2. Gives a direction to the organisation by fixing the goals and targets.

Advantages of budgetary control

3. Minimises wastages and losses.

4. Actual performance can be compared with budgetary standards.

5. It motivates the executives to attain targets.

Traditional Techniques

1. Personal observation
2. Statistical reports
3. Break-even analysis
4. Budgetary control

Modern Techniques

1. Return on Investment (ROI)

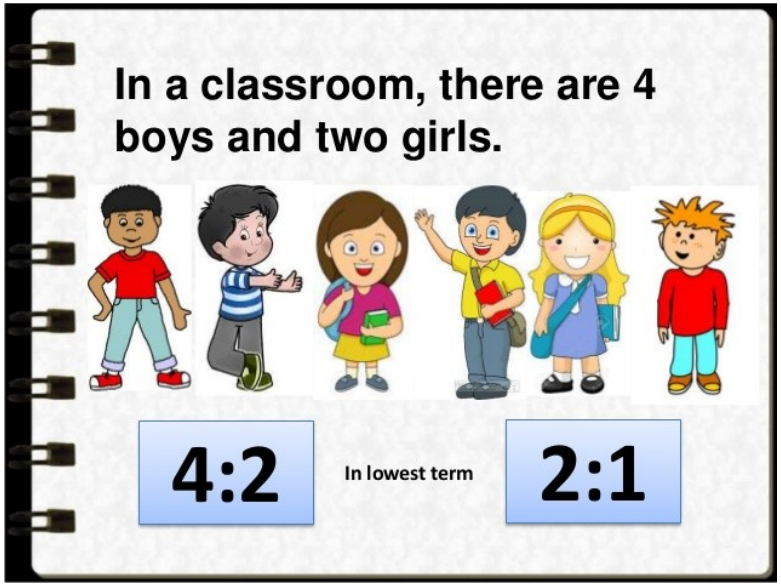
This technique is used to ensure the capital investment is properly utilised or not in order to get a reasonable amount of return (profit)

$$ROI = \frac{NetIncome}{TotalInvestment}$$

Modern Techniques

2. Ratio Analysis

This is a simple technique used for analysing and interpreting data contained in financial statements



This is done through calculating accounting ratios

A ratio is an arithmetic relationship between two figures

Accounting Ratios

a. Liquidity ratio

It is used to ascertain short term solvency of business

It shows the ability of a business to meet its short-term obligations in time

Liquidity Ratios

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

Eg: Current ratio, liquid ratio etc.

Accounting Ratios

b. Solvency ratio

Solvency here means long term solvency which refers to the ability to meet all liabilities in the event of liquidation

$$\text{Debt to Equity Ratio Formula} = \frac{\text{Total Liabilities}}{\text{Total Equity}}$$

Eg: Debt – equity ratio, capital gearing ratio, proprietary ratio etc.

Accounting Ratios

c. Profitability ratio

It is calculated to know the profitability in relation to sales or capital in the business

E.g. Gross profit ratio, Net profit ratio, Return on total sales ratio, Return on capital employed ratio, Return on equity capital ratio etc.

Accounting Ratios

d. Turnover ratio

It reflects the speed at which resources are utilised in effecting sales

A higher turnover ratio means efficient use of resources

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Inventory}} = \frac{1500}{500} = 3$$

E.g. Inventory turnover ratio, Debtors' turnover ratio, Creditors' turnover ratio, working capital turnover ratio etc.

Modern Techniques

3. Responsibility accounting

It is a system of accounting in which different sections or departments in an organisation are taken as “Responsibility Centres”

The person in charge of a centre is responsible for achieving the target fixed

Different Types of Responsibility Centres

a. Cost centre

It is a location, a person, a department or an item of equipment for which the cost is ascertained and used for cost control

Eg: In a manufacturing unit production department is treated as a cost centre and the production manager is responsible for controlling costs in his department

Different Types of Responsibility Centres

b. Revenue centre

A segment of an organization which is primarily responsible for earning revenue is called a revenue centre

E.g. Marketing department is a revenue centre

Different Types of Responsibility Centres

c. Profit centre

It is a segment of activity of an organization which is responsible for making profit

it is a centre responsible for **both revenue and costs** and thereby profit for a particular activity

Repair and maintenance department may be treated as a profit centre provided it bills other departments for their services

Different Types of Responsibility Centres

d. Investment centre

Here the investment is separately calculated and return on investment is taken as the basis for evaluating the performance of that centre

Eg: Investment in Fixed Assets

Modern Techniques

4. Management Audit

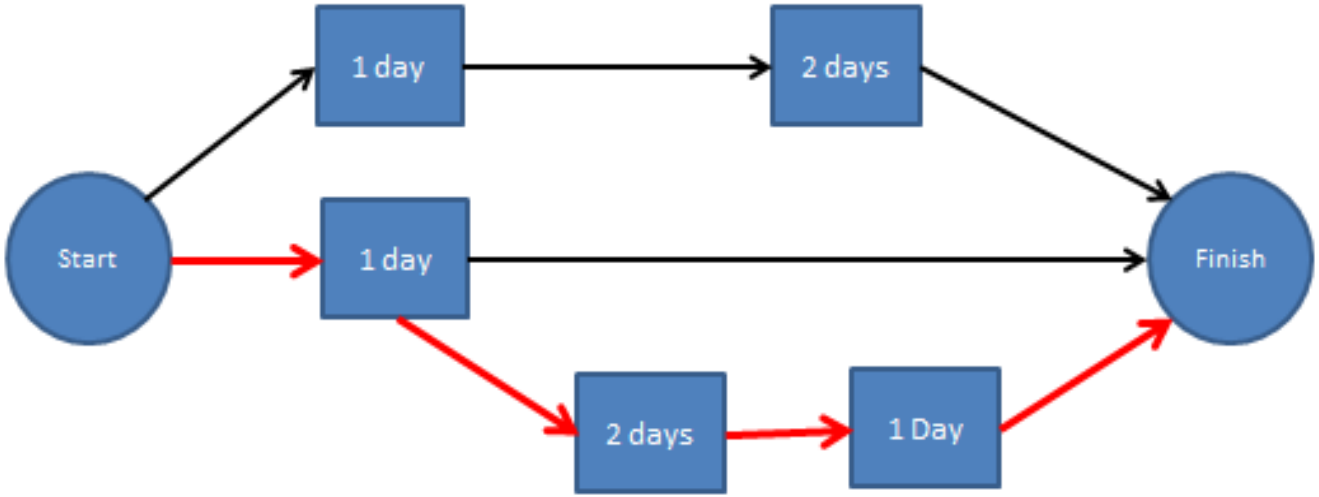
It is necessary to evaluate the efficiency of management to ascertain whether the performance of management is according to expected lines

Management audit reveals the achievements of management against the expected performance and also the weaknesses are pointed out

Modern Techniques

5. PERT and CPM

Program Evaluation and Review Technique and Critical Path Method

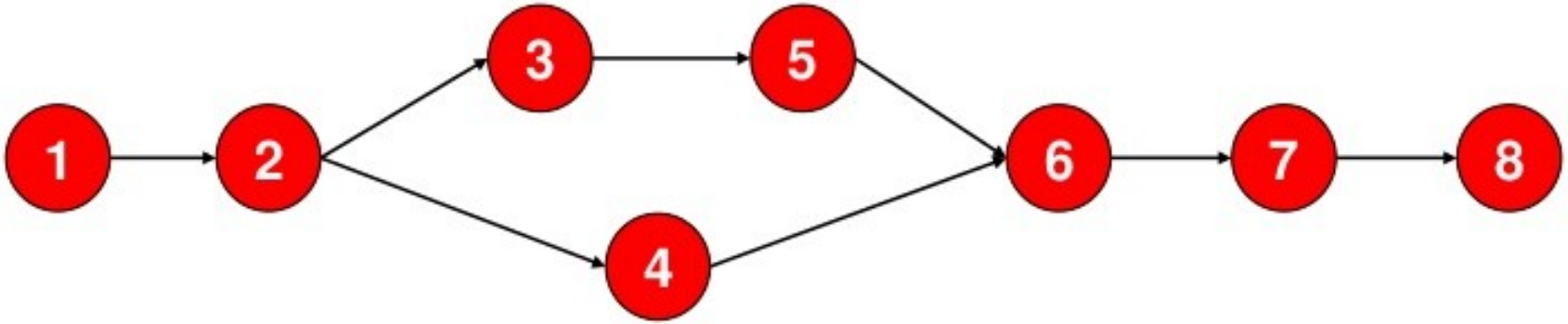


Critical Path = 4 Days

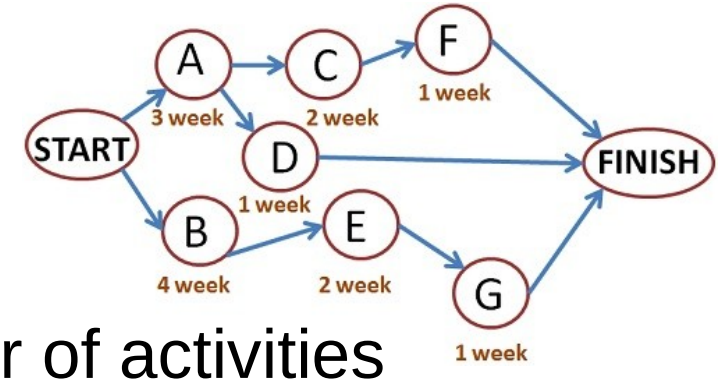
A network analysis technique to determine the time to complete a complex process

Calculation of the Critical Path

- Network approach helps calculate project duration
  - A "***path***" is a sequence of activities that begins at the start of the project and goes to the end of the project
    - 1,2,3,5,6,7,8
    - 1,2,4,6,7,8
  - The "***critical path***" is the path that takes the longest to complete
    - and thus determines the minimum duration of the project



Steps in PERT and CPM



1. The project is divided into a number of activities

2. Develop a network diagram incorporating all activities with a starting point and finishing point

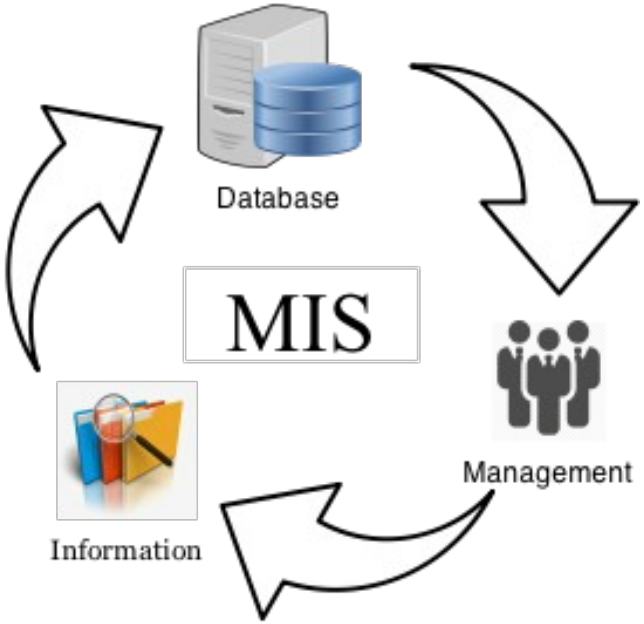
3. Three time estimates – optimistic, most likely and pessimistic are made

4. The longest path in the network is identified as a critical path

5. Plan may be modified for prompt execution and timely completion of the project

Modern Techniques

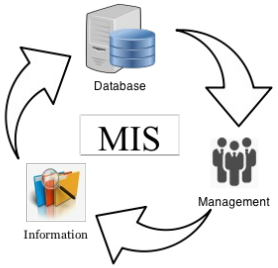
5. Management Information System (MIS)



Computer based information system which provides data and information on a real time basis supports the management for decision making and to take corrective actions on deviations

Advantages of MIS

1. Collection, processing and dissemination of information.
2. Support Planning, decision making and controlling.
3. Quality of information is improved.
4. Cost effectiveness.
5. Managers are not overloaded with too many information.



Modern Techniques

1. Return on Investment (ROI)
2. Ratio Analysis
3. Responsibility accounting
4. Management Audit
5. PERT and CPM

Thanks

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