

IMPACT OF MANAGEMENT ON EFFECTIVENESS AND EFFICIENCY OF ENTERPRISE

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Abstract: The record companies as an economic system depends on the level of economic effectiveness and efficiency of enterprise. Starting from the level of their functional interdependence, the paper points to problems of measuring the effectiveness and efficiency, and measurement of business success as well as their quantitative expression. The paper outlines the development of models for measuring business success that moved through their upgrading and improving to serve as an effective support to the governance process. Selection criteria and models for measuring business success is crucial to the process of governance. Influence of management on the effectiveness and efficiency of the company is viewed through the influence of top management to choose goals of a company stating that the necessity of recognizing the interests of different stakeholders in different contexts, external and internal relations of the enterprise. The same effect is seen through management activities that contribute to achieving the objectives companies.

Key words: effectiveness, efficiency, enterprise goals, stakeholders, business success.

1. EFFECTIVENESS AND EFFICIENCY OF THE ENTERPRISE

One of permanently present requirements within the enterprise today in extremely variable conditions of environment is the requirement for improving the *effectiveness* that refers to the choice of real goals and maximal implementation of selected goals. Achieve as greater as possible economic *efficiency*, i.e. greater range (difference) between the results and investments for obtaining those results represents basic principle in the conduct of enterprise of market economy.

Respecting numerous, even different concept for defining these essential phenomena of the enterprise, we can start from the fact that:

Effectiveness of the enterprise represents the level of achievement of its goals (Haimann T., W. G. Scott). Higher level of achieving the goals of enterprise is an indicator of greater effectiveness of enterprise. Effectiveness is based on comparing the results achieved to the criterion that is determined based on earlier results or results achieved. Therefore, effectivity has always been a dependent variable since it is determined in relation to particular standard. *Efficiency* appears as a requirement for achieving a particular level of goals selected with the least use of resources available, so the efficiency is expressed by the ratio of the results (output) and investments (input), necessary for those results to come true. More precisely, as you achieve higher results by a certain amount of resources, the efficiency of enterprise is higher [1 pp. 123].

P. Drucker points to the difference between efficiency and effectiveness of enterprise. *Efficiency* means to do better what is done “do things in the right way”. Efficiency is measured by the ratio of effects and costs that occurred during their realization. *Effectiveness* means to “do the right things”. It is measured by the realization of gain in the market by adapting the products and services to the requirements of demand [2 pp. 38]. Their view of organizational efficiency and effectiveness is given by Cook S. and Slack N.

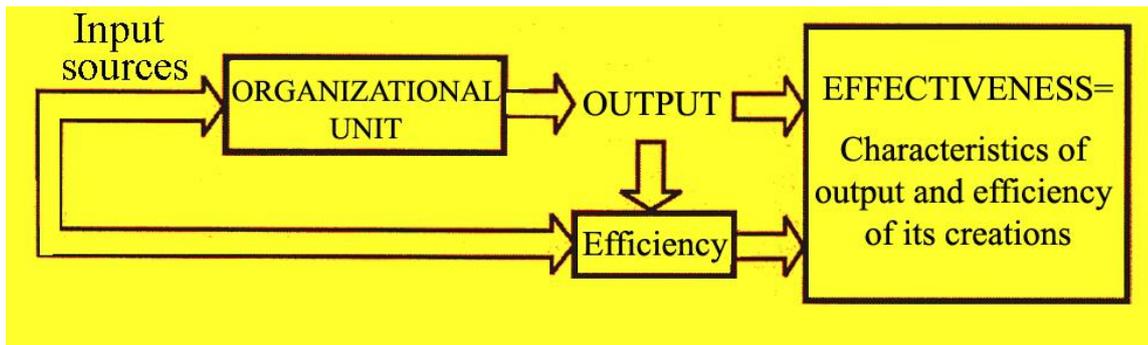


Figure 1. Efficiency and effectiveness of business

Efficiency is a transformational process – it is measured by some function (output) by the unit of used sources (inputs). Measures that are used to point to the efficiency of transformation are: output per employee, level of capacities utilization, costs per product unit, turnover ratio etc. *Effectiveness* includes the characteristics of output, as well as efficiency in their creation. Namely, effectivity of business depends on other factors except costs per unit of output. Characteristics of output are: (1) specification of products and services (what does it contain and how it functions), (2) quality of products and services, (3) reliability of enterprise’s work, (4) availability of products and services, (5) flexibility in performing the activity of enterprise [3 pp. 254].

By the concept of *effectiveness* we imply successful work of enterprise that is based, primarily, on the success in research, identification and projection of flows and relationships in domain of dynamics of market factors that are relevant for market orientation of enterprise’s activities. Understandably, this equally refers to the selection of all resources, goals, work methods, organization etc., by which we contribute to such target orientation of enterprise. *Efficiency* of the enterprise refers to success in achieving selected goals, particularly in domain of production process (production efficiency) [4 pp. 23].

Interdependence of efficiency and effectiveness is more than functional. Effects in domain of effectivity also depend on the effects in domain of production efficiency and vice versa. Product is a result of selection, but also a result of more efficient or less efficient production. In some cases, in the short run, the enterprise can be efficient, without being economically effective (when products are sold by inappropriate prices). Enterprise can be effective even if it is not economically efficient, when in conditions of increased demand sells less rationally produced products.

2. IMPACT OF MANAGEMENT ON SELECTION AND IMPLEMENTATION OF THE GOALS OF ENTERPRISE

Management of each enterprise accesses the formulation of goals that will later serve as secure signposts according to which they will direct diverse business activity of an enterprise. Initial goals come from top management of the enterprise. In the process of goals creation, there has to be coordination of all the main participants in the enterprise. Participation of employees in goals formulation contributes to their rationality and feasibility.

Process of goals selection is searching and determining what is the best to define as state or situation in which the enterprise desires to be in due time. The starting point is the situation analysis and assumptions regarding the factors that will influence the implementation of the intended goals of enterprise.

Modern management recognizes the responsibility of enterprise before numerous interests that belong to different interest groups (owners, consumers, employees, suppliers, social community etc.) which often set different and conflict goals. Starting from the characteristics of enterprise as economic system, it can be seen that target function should include the goals by which the following interests are achieved: interests of consumers, state, owner, manager, employees, survival, i.e. development of enterprise and natural system. Management is chosen and set by the owner, but it cannot carry out the tasks set without cooperation with members of different interest groups of enterprise. Managers have the task to reconcile the interests of different interest groups in the long run. Rationally formulated goals are a significant assumption of minimizing the suboptimization at all levels in organizational structure of enterprise. The more you respect the goals of enterprise, i.e. they more they are accepted, there are more chances for them to be fulfilled.

There needs to be the structure of goals in the enterprise, i.e. enterprise must be able to set priorities regarding the goals. By priority, the achievement of one goal is determined as more important in relation to the achievement of the second goal. Management of enterprise needs to establish priorities if it wants to allocate the sources in a rational way. For that reason, prior to decision on allocation of the sources of enterprise, alternative goals need to be evaluated and ranked [5 pp. 48]. Value system of top managers influences the selection of goals, because their perception of importance of particular goals and selection of priorities depends on the value system.

Management is a precondition for survival, growth and development of enterprise, which is not exhausted only in making business decisions, but it also includes taking actions in their achievement.

Management of the enterprise is a combination of externally and internally oriented management. Management of the enterprise is *externally* oriented, with the help of developed information system it observes the environment and recognizes chances and dangers and, according to that, determines goals and strategic vision. Management of the company *internally* oriented has the impact on rational use of available resources, i.e. reduction of business costs. Operational managers control a wide range of diverse daily activities and they are responsible for the efficiency of spending, work productivity, capacity utilization, stocks control, production schedule, ensuring timely deliveries to customers etc. Management within the enterprise as organization of people, resources and technology improves and discovers new methods of work, combines production factors and finds other innovations for gaining competitive advantage. In common to both components of management is that they do not accept the non-changeability of business environment, both in the aspect of the field of activities and they way of realizing the business of enterprise.

3. MEASUREMENT OF TOTAL EFFECTIVENESS AND EFFICIENCY

Measuring the overall effectiveness and efficiency of enterprise (business success) has primarily interested the owners of enterprises who want to have precise information regarding real economic efficiency of their enterprises and for control of effects of the new investment activities undertaken. Term measurement of overall business success is used as synonym for solving overall economic efficiency of enterprise as business system (which also includes the effects of effectivity). Measurement of business success enables the owners to control the managers in those enterprises where ownership is separated from control. Managers who need adequate economic instrumentarium for successful actions, i.e. more efficient management, are interested in measuring business success.

State expressed the interest for measuring business success of enterprise. By expressing business success through laws of determined schemes regarding balance sheets, income statements and tax balance sheet is a legal requirement without which the enterprise cannot exist.

3.1. BUSINESS SUCCESS AS QUANTITATIVE EXPRESSION OF EFFECTIVENESS AND EFFICIENCY

Changes in effectiveness and efficiency of point to the changes in the quality of economy. Quantitative expression of the quality of economy is expressed by business success.

$$P_U = R(O_u) / U(I_n)$$

Where: P_U – business success, $R(O_u)$ – results (output), $U(I_n)$ – investments (input).

As quality of enterprise's economy as an expression of the level of economic success in achieving goals of enterprise is simultaneously the expression of success in achieving effectiveness and efficiency, the business success is a quantitative expression of effectiveness and efficiency (only economic efficiency often in literature).

3.2. THE ESSENCE AND THEORETICAL-METHODOLOGICAL PROBLEMS OF MEASURING OVERALL BUSINESS SUCCESS

Overall business success of a particular enterprise needs to be an expression of comprehensive economic efficiency of enterprise which further means that it expresses its total allocative ability through the abilities: for selection and procurement of inputs; efficient organization of production as transformational process; as well as selection and realization of products and services as outputs of enterprise. All economic effects that manifest on inputs and outputs of a specific enterprise express its total economic efficiency [1 pp. 475]. Achievement of particular results of reproduction with as lower investments as possible, as basic economic principle of reproduction, is simultaneously the main criterion of the evaluation of achieved business success.

By expressing business success using partial indicators of productivity ($P = Q/L$), cost effectiveness ($E = C / T$) and profitability ($R = D / S$), the level of achieving partial economic principles is expressed, i.e. efficiency of functioning of production-technological exchange and financial subsystem of organizational structure of enterprise. In that way, control and orientation of quality of particular subsystem of specific economy is provided in unique integral goal – achieving the efficiency of entire system.

Analysis of business success is based on research and managing the business factors. Both level and dynamics of business success depend on success in managing relevant business factors.

Research has shown that when expressing and managing the dynamics of total business success, divergence and deficiencies of partial indicators are expressed. Transition from a greater number of partial indicators to one unique indicator of total efficiency requires the resolution of problem of reducing different measures for inputs and outputs of enterprise, as well as development of a complex business-information system which should be in the function of economic instrumentarium developed from a specific model for measuring business success.

Models and indicators (sets of indicators) resulting from previous theory and practice express the deficiencies for expressing overall business success. In such a way that different theoretical models cannot be applied in real economic life of society or that sets of various indicators, indexes and ratio numbers only show the result of business in previous period, according to expressions of partial states and effects, rather than overall business

success. We can agree on the statement that numerous efforts of economic theory and practice of economically the most successful enterprises are the source of valuable ideas in the search for finding adequate solutions.

In finding ways to express overall business success as quantitative expression of overall economic efficiency in economic theory and practice there are many different solutions that can generally be reduced to two groups of models:

- First group consists of different models of business success that use several indicators. Frequently, models are supplemented by new indicators. Summary term is most frequently given in the form of ratings. Attitude on relative significance of particular indicators is based on subjective evaluation and, as a rule, it is not objectivised by some basis.

- Second group of models consists of attempts to reach systematic aggregate expression of business success, with all limitations that come from it [4 pp. 465].

The standpoint that indicators need to be quantitative (financial) and qualitative (non-financial) is generally accepted. Content, whether of the set of indicators or integral model of overall business success, should meet informational, management-control and motivational function [6 pp. 67].

4. TRADITIONAL APPROACH OF BUSINESS SUCCESS MEASUREMENT – SYSTEMS OF FINANCIAL CONTROL

Traditional approach of business success measurement is based on data that can be obtained based on financial and accounting system of enterprise and it is a basis for the system of financial control in enterprise by expressing results of previous activities. Accounting concept of profit is general measure of success/failure of enterprise. Traditional methods of financial control, most frequently used (some of them and dominant even today) include: *financial statements analysis, analysis of ratio number systems, breakpoint analysis, budget and audit*. Evaluation of overall financial success of enterprise implies the interpretation of obtained values of particular indicators and their confrontation and connection having in mind that the information that are sometimes provided by particular indicators can also be mutually contradictory.

Balance theories and accounting indicators have their clear control roles in particular time period. Traditional measurement systems of business success express the results achieved and do not give the overview of factors that influence them. For that reason, they cannot be a basis for proactive control and management in conditions of uncertainty. In addition, lack of traditional system of financial control is inability to include non-material resources of enterprise significant for the creation of competitive position of enterprise in modern business conditions.

5. MODERN APPROACH OF BUSINESS SUCCESS MEASUREMENT – SUPPORT TO MANAGEMENT SYSTEM

In order for the system for measuring overall business success to support efficient control and management in modern conditions of business, it is necessary also to provide measurement of the generator of financial success of enterprise. In addition to extreme financial perspective, it is necessary to observe other dimensions of enterprise's success as well. In modern business conditions, strong requirements for achieving the interests, i.e. goals of different stakeholders of enterprise are expressed. Impacts are expressed in different competitive environment.

As a consequence of striving to meet the above-mentioned requirements, there was a series of attempts to improve financial indicators, or to reach completely new systems of

indicators and models. In that sense, in domestic and foreign literature there was a series of approaches of indicators and models for measuring the performances of enterprise.

In the existing solutions of economic theory and practice, different models and differentiated: *model oriented on stakeholders*, *model oriented on processes*, as well as *integral model* which includes elements of both models.

In the search for the system for success measurement that would simultaneously be the system of performance measures, i.e. database for strategic decisions, one group of researchers was focused on improvement of financial success measures, attempting to increase their relevance for strategic decisions. *Economic value added concept* is a result of such an approach. The second group of researchers improves operational measures (such as, for example, customer satisfaction measures, internal process measures etc.), believing that financial result will not fail. However, the reality finds closer the attitude that decisions regarding the future can be brought based on one set of measures. The decision-makers need balanced structure of financial and operational measures. R. Kaplan and D. Norton have adhered to this idea by developing a concept of so-called „balanced list“ of goals and performance measures (Balanced Scorecard).

Model Balanced Scorecard observes overall success of enterprise from many aspects, i.e. measures overall success of enterprise by combining financial and non-financial indicators. Indicators within financial perspective represent indicators of results (lagging indicators), while the indicators of the other perspectives give early signals (leading indicators) and point to the need of corrective action. The essence of the model is in the attempt to translate visions and missions of enterprise defined by general and immeasurable terms into the system of measurable goals and indicators by particular perspectives through identifying cause and effect connections. Indicators of success can be created based on strategy. It has proven its applicability in practice. It is significant that this concept can be adapted to specific needs of enterprise and conditions in environment, and thus also to the changes in management's requirements in the aspect of characteristics of the system for measuring the performances [7 pp. 210].

Management of the enterprise in modern conditions needs to be aimed at continuous mastering the processes of measurement, compliance of managers' attitudes in order to support the success of enterprise and management process.

Only adequately applied models that provide observation of relevant factors as a cause of changes of business success and selection of managerial actions and measures, can be significant control-managerial instruments of routing the performance of enterprise in the right direction.

6. CONCLUSION

Starting from theoretical understanding of the essence of economic efficiency and its manifestations in economy in general, we obtain the knowledge about the essence of effectiveness and efficiency as economic phenomena at the level of enterprise. Effectiveness is thus considered as a level of achieving the goals of enterprise by pointing to the way in which enterprise satisfies the needs of customers in the market. Efficiency is expressed as a requirement for implementation of a particular level of selected goals with the least resources used. Interdependence of effectiveness and efficiency is obvious and integration of effectiveness and efficiency into a unique expression of overall economic efficiency is in function of measuring overall effects of the success of enterprise and more efficient management of the economy of enterprise.

Theoretical-methodological issues of defining the model for measuring overall business success as quantitative expression of overall effectiveness and efficiency of enterprise are

pointed out in the paper. Direction of development of models (indicators and aggregate models) that can provide timely information and more efficient management in modern business conditions is observed. Balanced Scorecard concept as a system for measuring performances is one of these models.

With the aim to really observe effectiveness and efficiency of enterprise today, we still look for solutions, to which new current paradigm of enterprise and specific practice of the most successful enterprises could provide an answer.

Management of the enterprise faces with a complex, responsible and creative task of choosing the goals, determining the priorities and harmonizing the goals of various interest groups. By its activities, management also contributes to achievement of goals in a decisive way.

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