SELECTING INPUTS AND OUTPUTS IN DATA ENVELOPMENT ANALYSIS BY DESIGNING STATISTICAL EXPERIMENTS

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Abstract  Data envelopment analysis (DEA) is a data oriented, non-parametric method to evaluate relative efficiency based on pre-selected inputs and outputs. In some cases, the performance model is not well defined, so it is critical to select the appropriate inputs and outputs by other means. When we have many potential variables for evaluation, it is difficult to select inputs and outputs from a large number of possible combinations. We propose an input output selection method that uses diagonal layout experiments, which is a statistical approach to find an optimal combination. We demonstrate the proposed method using financial statement data from NIKKEI 500 index.

Keywords: DEA, fractional factorial design, Mahalanobis distance

1. Introduction
Evaluation of performance is an important activity in identifying shortcomings in managerial efficiency and devising goals for improvement. Many activities can be expressed as a translation of inputs to outputs, where it is desirable to produce more outputs with less inputs. Data envelopment analysis (DEA), the most representative method for efficiency evaluation, is a mathematical programming method for evaluating the relative efficiency of decision making units (DMUs) with multiple inputs and multiple outputs.

DEA is a data-oriented non-parametric method. A production possibility set is constructed empirically by enveloping the inputs and outputs data set, where a parametric transformation function is not assumed. The efficient frontier of a production possibility set enables the relative efficiency evaluation. The efficiency score distinguishes between efficient and inefficient DMUs by establishing whether a DMU is located on the efficient frontier or inside the production possibility set. Also, the efficiency score indicates how far a DMU is from the efficient frontier.

DEA empirically identifies the efficient frontier of a set of DMUs based on the input and output variables. Assume that there are \( n \) DMUs, and the \( j \)th DMU, DMU\(_j\), produces \( s \) outputs \((y_{ij}, ..., y_{sj})\) by using \( m \) inputs \((x_{1j}, ..., x_{mj})\). The efficiency score of the observed DMU\(_o\) is given as the optimal value to the following linear programming problem:

\[
\theta^*_o = \min \theta \\
\text{s.t. } \sum_j \lambda_j x_{ij} \leq \theta x_{io}, \ i = 1, ..., m \\
\sum_j \lambda_j y_{rj} \geq y_{ro}, \ r = 1, ..., s \\
\lambda_j \geq 0, \ j = 1, ..., n \tag{1.1}
\]
This is an input oriented constant returns to scale (CRS) model. The efficiency of DMU₀ is determined from efficiency score $\theta^*_o$ and its slack values. If $\theta^*_o = 1$ and there is no slack, DMU₀ is said to be efficient. If $\theta^*_o = 1$ and there are non-zero slacks, DMU₀ is inefficient and is called to be weak-efficient. The weak-efficient DMUs and efficient DMUs comprise the efficient frontier.

Evaluation based on the efficiency score is directly affected by the input and output variables. That is, the inputs and outputs should be selected appropriately so as to express the performance of DMUs. For instance, the selection may be founded on a particular theory, e.g. production versus intermediation approaches to bank behavior. Alternatively, expert knowledge or accepted practices can be useful in determining the variables. For example, when we assess the profit efficiency of banks, two inputs (interest expense and non-interest expense) and two outputs (interest income and non-interest income) are often used as the core variables [6]. However, stakeholders in bank performance would interpret measures differently when it comes to categorizing a variable as an input or an output. This is due to the variety of stakeholders. We normally treat variables considered to be desirable as outputs, and those considered to be undesirable are treated as inputs. For instance, a head office executive would be more interested in running the organization with a smaller number of employees, whereas a branch manager may be interested in having more employees at the disposal of the branch. That is, number of employees is likely to be an undesirable attribute (i.e. an input) for the executive and a desirable attribute (i.e. an output) for the branch manager, which may lead the hesitation to decide input or output to evaluate overall efficiency [10].

Furthermore, in some cases, the performance measure is not always clearly defined. For example, in evaluating baseball players, there are many variables which can be used to capture a player’s performance. Hirotsu and Ueda [7] use seven outputs such as rate of home runs, rate of runs batted in, rate of stolen bases, batting average, slugging percentage, on-base percentage, and batting average in scoring position. But it is possible to use other variables such as at bats, strikeouts, sacrifice bunts, annual salary and so on. Thus, it is necessary to select a parsimonious set of inputs and outputs so as to capture the performance of a DMU’s key activities.

DEA framework identifies the non-dominated efficient DMUs in the data space spanned by inputs and outputs. So, too many inputs and outputs manifest as too many relatively efficient DMUs. Similarly, too few inputs and outputs cannot show the efficient DMUs. Therefore, it is desirable to develop a mathematical approach to selecting input and output variables for performance evaluation that will distinguish between efficient and inefficient DMUs, particularly where appropriate theory or accepted practices are not available.

In a previous study, Morita and Haba [3] select outputs so as to distinguish between two groups based on external information, where a 2-level orthogonal layout experiment is utilized and optimal variables can be found statistically. On the other hand, Edirisinghe and Zhang [4] have proposed a generalized DEA approach to select inputs and outputs by maximizing the correlation between the DEA score and the external performance index. They utilize a two-step heuristic algorithm that combines random sampling and local search to find an optimal combination of inputs and outputs.

In this paper, we consider an input and output selection method based on discriminant analysis using external evaluation. We use a 3-level orthogonal layout experiment to find an appropriate combination of inputs and outputs, where experiments are independent of each other.

The rest of the paper is organized as follows. The next section presents the output...
selection method using the 2-level layout experiment proposed in [3]. Then, the method of variable selection is expanded in section 3 through a 3-level orthogonal layout experiment, where inputs as well as outputs are considered. A case study of management efficiency of ranked Japanese companies is demonstrated in section 4. Section 5 concludes the paper.

2. Selecting Output Variables Using a 2-Level Fractional Factorial Design
We select the appropriate output variables so as to distinguish between two groups, that is, high performers and low performers, on efficiency scores [3]. We assume that external performance criteria on high performers and low performers are available. The distance between the two groups is measured by the Mahalanobis distance. In this study, we consider the distance of one-dimensional variables, where Mahalanobis distance coincides with the Welch statistics. The Welch statistics is given as

\[ d = \frac{\bar{\theta}_h - \bar{\theta}_l}{\sqrt{\frac{V_h}{n_h} + \frac{V_l}{n_l}}} \]  

(2.1)

where the mean and variance of each group are given as \( \bar{\theta}_h, V_h \) for \( n_h \) high performers and \( \bar{\theta}_l, V_l \) for \( n_l \) low performers.

The aim is to find that combination of output variables which maximizes the distance \( d \).

In our first example, for simplicity, we utilize the 2-level factorial design. When there are \( k \) candidates of output variables, the total number of combinations is \( 2^k \). Full factorial designs perform all of \( 2^k \) combinations for \( k \) candidates. On the other hand, we can define a \( 2^{k-p} \) design to be a fractional factorial design with \( k \) candidates, each at two levels, consisting of \( 2^{k-p} \) runs. The first \((k-p)\) candidates are part of \( 2^{k-p} \) combinations as a full factorial design, and the remaining \( p \) candidates can be generated as interactions with the first \((k-p)\) columns. Table 1 shows the example of a fractional factorial design where \( k = 5, p = 2, \) and \( x_i \) is a candidate variable. ‘+’ means that the variable is selected as an output, and ‘−’ means that the variable is not selected as an output. For example, the variables \( x_1, x_3, x_4 \) are selected as outputs in run No. 3.

Based on the fractional factorial design in Table 1, we calculate the efficiency scores by (1.1) and Mahalanobis distance by (2.1) between two groups using the selected output variables. The analysis of variance (ANOVA) for the fractional factorial design appears in Table 2.

The total sum of squares \( S_T \) is given as

\[ S_T = \sum_{i=1}^{8} (d_i - \bar{d})^2 \]  

(2.2)
Table 2: ANOVA table for fractional factorial design of $2^{5-2}$

<table>
<thead>
<tr>
<th>Variables</th>
<th>Sum of Squares</th>
<th>Degrees of Freedom</th>
<th>Mean Squares</th>
<th>$F$ statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>$x_1$</td>
<td>$S_1$</td>
<td>$\phi_1 = 1$</td>
<td>$V_1 = S_1/\phi_1$</td>
<td>$V_1/V_E$</td>
</tr>
<tr>
<td>$x_2$</td>
<td>$S_2$</td>
<td>$\phi_2 = 1$</td>
<td>$V_2 = S_2/\phi_2$</td>
<td>$V_2/V_E$</td>
</tr>
<tr>
<td>$x_3$</td>
<td>$S_3$</td>
<td>$\phi_3 = 1$</td>
<td>$V_3 = S_3/\phi_3$</td>
<td>$V_3/V_E$</td>
</tr>
<tr>
<td>$x_4$</td>
<td>$S_4$</td>
<td>$\phi_4 = 1$</td>
<td>$V_4 = S_4/\phi_4$</td>
<td>$V_4/V_E$</td>
</tr>
<tr>
<td>$x_5$</td>
<td>$S_5$</td>
<td>$\phi_5 = 1$</td>
<td>$V_5 = S_5/\phi_5$</td>
<td>$V_5/V_E$</td>
</tr>
<tr>
<td>Error</td>
<td>$S_E$</td>
<td>$\phi_E = 2$</td>
<td>$V_E = S_E/\phi_E$</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$S_T$</td>
<td>$\phi_T = 7$</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The sum of squares $S_i$ for candidate $i$ reflects the main effect of the variable, which is the difference between ‘+’ and ‘−’ as,

$$S_i = 2\{\bar{d}(x_i+) - \bar{d}(x_i-)^2\} \quad (2.3)$$

where $\bar{d}(x_i+)$ is the mean of the Mahalanobis distances observed when $x_i = +$. The residual sum of squares $S_E$ is given by subtracting the sum of $S_i$ from $S_T$.

$$S_E = S_T - (S_1 + S_2 + S_3 + S_4 + S_5) \quad (2.4)$$

The total degree of freedom is $\phi_T = 7$, which is the number of runs minus 1, and the degree of freedom for each sum of squares is $\phi_i = 1$. Therefore the degree of freedom for the residual is given as,

$$\phi_E = \phi_T - (\phi_1 + \phi_2 + \phi_3 + \phi_4 + \phi_5) = 2 \quad (2.5)$$

The null hypothesis that the candidate has no effect as an output is tested by using the $F$ statistics,

$$F = \frac{S_i/\phi_i}{S_E/\phi_E}. \quad (2.6)$$

The test rejects the null hypothesis at level $\alpha$ if $F$-value exceeds $\alpha$ percentile of $F$ distribution with degrees of freedom $(\phi_i, \phi_E)$.

The negligible variables are pooled into the residual and the remaining variables should be selected as outputs. Then, we can obtain the optimal combination of output variables.

The following summarize the procedure for variable selection.

Step 1. List potential input output variables.

Step 2. Use external criteria to distinguish the performance of two groups, e.g. high and low performers.

Step 3. Assign the variables to an orthogonal layout and determine the combination of selected variables used in the experiments.

Step 4. Calculate the DEA efficiency scores and Mahalanobis distance between the two groups by using the selected variables.

Step 5. Determine the optimal combination of input output variables based on results of analysis of variance.

Step 6. Identify the optimal designation of statistically significant variables as either an input or an output using Mahalanobis distance.
3. Selecting Input and Output Variables Using a 3-Level Fractional Factorial Design

When a variable is considered for DEA, it is necessary to determine whether the variable should act as an input or an output. Some variables can be pre-specified as inputs or outputs based on the production conversion mechanism of a DMU or the expert knowledge of the analyst. When it is difficult to understand the conversion mechanism, inputs and outputs should be determined endogenously. Here, we obtain the efficiency measure to distinguish between high-performing DMUs and low-performing DMUs by selecting an appropriate combination of inputs and outputs that maximizes the distance \( d \) between the two groups. When there are \( k \) candidates of variables in a 3-level design, the total number of possible input and output combinations rises to \( 3^k \). Full factorial designs perform all of \( 3^k \) combinations. We can define a \( 3^k-p \) fractional design with \( k \) candidates, each at three levels, consisting of \( 3^k-p \) runs. Table 3 shows this fractional factorial design when \( k = 3, p = 1 \), where '1' means that the variable is selected as an input, '2' means that the variable is selected as an output, and '3' means that the variable is not selected. For example, in run No. 4, variable \( x_2 \) is selected as an input and variable \( x_1 \) is selected as an output; variable \( x_3 \) is not selected as an input or an output. When no output (input) is selected (e.g. see runs 1 and 6), constant output (input) is assumed, i.e. unity.

Based on the fractional factorial design in Table 3, we calculate the efficiency scores and Mahalanobis distance between the two groups using selected inputs and outputs. The ANOVA table for the fractional factorial design appears in Table 4.

The sum of squares and the degrees of freedom are given as,

\[
\begin{align*}
\text{Table 3: Fractional factorial design for } 3^3-1 \text{ and selected inputs and outputs} \\
\begin{array}{cccccc}
\text{Runs} & x_1 & x_2 & x_3 & \text{Selected Inputs} & \text{Selected Outputs} & \text{Distance} \\
1 & 1 & 1 & 1 & x_1, x_2, x_3 & \text{None} & d_1 \\
2 & 1 & 2 & 2 & x_1 & x_2, x_3 & d_2 \\
3 & 1 & 3 & 3 & x_1 & \text{None} & d_3 \\
4 & 2 & 1 & 3 & x_2 & x_1 & d_4 \\
5 & 2 & 2 & 1 & x_3 & x_1, x_2 & d_5 \\
6 & 2 & 3 & 2 & \text{None} & x_1, x_3 & d_6 \\
7 & 3 & 1 & 2 & x_2 & x_3 & d_7 \\
8 & 3 & 2 & 3 & \text{None} & x_2 & d_8 \\
9 & 3 & 3 & 1 & x_3 & \text{None} & d_9 \\
\end{array}
\end{align*}
\]

\[
\begin{align*}
\text{Table 4: ANOVA table for fractional factorial design of } 3^3-1 \\
\begin{array}{cccc}
\text{Variables} & \text{Sum of Squares} & \text{Degrees of Freedom} & \text{Mean Squares} & F \text{ statistics} \\
& S_1 & \phi_1 = 2 & V_1 = S_1/\phi_1 & V_1/V_E \\
x_2 & S_2 & \phi_2 = 2 & V_2 = S_2/\phi_2 & V_2/V_E \\
x_3 & S_3 & \phi_3 = 2 & V_3 = S_3/\phi_3 & V_3/V_E \\
\text{Error} & S_E & \phi_E = 2 & V_E = S_E/\phi_E \\
\text{Total} & S_T & \phi_T = 8 \\
\end{array}
\end{align*}
\]
\[ S_T = \sum_{i=1}^{9} (d_i - \bar{d})^2, \phi_T = 8 \]  
\[ S_i = 3\{\bar{d}^2(x_i = 1) + \bar{d}^2(x_i = 2) + \bar{d}^2(x_i = 3)\} - 9\bar{d}^2, \phi_i = 2 \]  
\[ S_E = S_T - (S_1 + S_2 + S_3), \phi_E = \phi_T - (\phi_1 + \phi_2 + \phi_3) = 2 \]  

where \( \bar{d}(x_i = 1) \) is the mean of the Mahalanobis distances observed when \( x_i = 1 \). The null hypothesis that the candidate has no effect as an input or output is tested by using the \( F \) statistics.

The negligible variables are pooled into the residual. A statistically significant variable may be considered as an input or an output based on the maximum returned by \( \{\bar{d}(x_i = 1), \bar{d}(x_i = 2), \bar{d}(x_i = 3)\} \). If \( \bar{d}(x_i = 1) \) is the maximum, variable \( x_i \) should be an input. If \( \bar{d}(x_i = 2) \) is the maximum, then variable \( x_i \) should be an output. On the other hand, if \( \bar{d}(x_i = 3) \) is the maximum, variable \( x_i \) should not be an input or an output. This results in the optimal combination of input and output variables.

4. A Case Study of Management Efficiency Using Financial Data

We use the NIKKEI 500 (2007), which is a ranking based on financial data. Ranking is based on the following four dimensions, which are given by fifteen indexes entered into factor analysis, where the result is converted into a score in the range 0-100.

(i) Scale: sales, owners’ equity, number of employees, cash flow

(ii) Profitability: ratio of sales to operating income, return on equity, rate of return on total assets

(iii) Safety: debt-to-asset ratio, interest coverage ratio, net interest expense to sales ratio, liquidity ratio

(iv) Growth: growth rates of total assets, sales, number of employees, and owners’ equity.

In Step 1 (see Section 2), the following twelve variables are collected to evaluate the managerial performance of companies. Table A1 in the Appendix shows a part of the data set. Most of these variables except for (J) and (K) have large coefficients of variation (CV), that is, the standard deviation is greater than the mean.

(A) Issued stocks
(B) Market price
(C) Total assets
(D) Capital
(E) Cash flow
(F) Total sales
(G) Ordinary profits
(H) Net profits
(I) Number of employees
(J) Return of equity
(K) Sales to profits ratio
(L) Debt ratio

In Step 2, we construct two groups, high-performers and low-performers, from the top-ranked 30 and bottom-ranked 30 companies. Table A1 shows the mean and standard deviation for each variable. The variation among the companies is quite large, even though we are focusing on top and bottom performers. When we select the variables to capture the
difference between high-performers and low-performers, we choose a variable with a large difference between these two groups. Mahalanobis distance between the top 30 and bottom 30 for each variable is also shown in Table A1, where we find that (B), (D), (G), (H) and (I) have a large d and may be intuitively selected as inputs or outputs.

In Step 3, we assign twelve factors into a three-level orthogonal layout, where at least twenty-seven runs are required. That is, we utilize the fractional factorial design $3^{12-9}$. Table 5 shows the selected variable combinations for efficiency score calculation. The Mahalanobis distance for each experiment is calculated in Step 4, which is also shown in the last column of Table 5.

Table 6 shows the analysis of variance for the data in Table 5, where we have pooled the negligible variables into the residual (step 5). The level of significance is shown as the $p$ value, where we find four variables (B, G, H and L) significant at the 5% level. The variables (C) and (E) are not significant at the 5% level, but since their $p$ values are not very high, we leave them in the analysis for illustrative purposes.

Step 6, the final step in our procedure, generates Table 7 which shows the means of Mahalanobis distance for each variable at each level. For example, when variable B is selected...
Table 6: Table of ANOVA

<table>
<thead>
<tr>
<th>Variables</th>
<th>Sum of Squares</th>
<th>Degrees of Freedom</th>
<th>Mean Squares</th>
<th>F statistics</th>
<th>p value</th>
</tr>
</thead>
<tbody>
<tr>
<td>B</td>
<td>42.73</td>
<td>2</td>
<td>21.36</td>
<td>7.33**</td>
<td>0.8%</td>
</tr>
<tr>
<td>C</td>
<td>10.65</td>
<td>2</td>
<td>5.32</td>
<td>1.83</td>
<td>20.3%</td>
</tr>
<tr>
<td>E</td>
<td>18.16</td>
<td>2</td>
<td>9.08</td>
<td>3.12</td>
<td>8.1%</td>
</tr>
<tr>
<td>G</td>
<td>28.78</td>
<td>2</td>
<td>14.39</td>
<td>4.94*</td>
<td>2.7%</td>
</tr>
<tr>
<td>H</td>
<td>67.00</td>
<td>2</td>
<td>33.50</td>
<td>11.5**</td>
<td>0.2%</td>
</tr>
<tr>
<td>L</td>
<td>24.00</td>
<td>2</td>
<td>12.00</td>
<td>4.12*</td>
<td>4.3%</td>
</tr>
<tr>
<td>Error</td>
<td>34.97</td>
<td>12</td>
<td>2.91</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>226.29</td>
<td>26</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* 5% level of significance; ** 1% level of significance

as an input, the mean of Mahalanobis distance is $-1.457$, and when variable B is selected as an output, $d$ is $1.491$; when variable B is not selected, $d$ is $-0.760$. Thus, given that the largest $d$ for variable B is 1.491, it should be selected as an output. Maxima are indicated in bold font in Table 7. Thus, we select one input (L) debt ratio, and four outputs, namely, (B) market price, (C) total asset, (G) ordinary profits and (H) net profits. We run the DEA model (1) using this input and output combination, and obtain a Mahalanobis distance of 7.42.

Based on the selected inputs and outputs, we analyze the effectiveness of efficiency evaluation through stratification [5]. Stratification consists of generating a tiered structure of multiple efficient frontiers. That is, Tier 1 represents the original efficient frontier with the full sample. We create Tier 2 when we remove the Tier 1 efficient DMUs and re-run DEA. To create Tier 3, Tier 2 efficient DMUs are removed, and so on. Twenty-two tiers emerge once our sample is exhausted by the stratification procedure. Figure 1 shows the numbers of companies in each tier. The companies in top 30 are categorized into the higher tiers and the companies in bottom 30 are categorized into the lower tiers. We accept this finding as empirical evidence that the selected input output combination effectively distinguishes between the two groups.

When we have many variables to evaluate performance, we may consider using all of them. In this study, there are twelve variables. At face value, the variables (I) and (K) have a ‘smaller-the-better’ characteristic and the others have a ‘larger-the-better’ characteristic. Table 8 summarizes the Mahalanobis distances and average efficiency scores for several combinations. Initially, we demonstrate using all the variables as per earlier prima facie selection of inputs and outputs, i.e. Case (a). For Case (a), there are too many outputs, many companies are evaluated to be efficient and as a result, we cannot distinguish between the two groups. Case (b) represents the combination that returned the maximum distance

```
Table 7: Mahalanobis distance means

<table>
<thead>
<tr>
<th>Variables</th>
<th>Selected as input</th>
<th>Selected as output</th>
<th>Not selected</th>
</tr>
</thead>
<tbody>
<tr>
<td>B</td>
<td>-1.457</td>
<td>1.491</td>
<td>-0.760</td>
</tr>
<tr>
<td>C</td>
<td>-0.951</td>
<td>0.576</td>
<td>-0.350</td>
</tr>
<tr>
<td>E</td>
<td>-1.399</td>
<td>0.269</td>
<td>0.404</td>
</tr>
<tr>
<td>G</td>
<td>-1.357</td>
<td>1.132</td>
<td>-0.501</td>
</tr>
<tr>
<td>H</td>
<td>-1.688</td>
<td>1.949</td>
<td>-0.987</td>
</tr>
<tr>
<td>L</td>
<td>1.010</td>
<td>-1.266</td>
<td>-0.470</td>
</tr>
</tbody>
</table>
```

among the previously calculated twenty-seven runs (see run 13 in Table 5) but it is not optimal either. Finally, the combination to emerge from our proposed method is shown in Case (c), where the Mahalanobis distance is maximized, and the efficiency differences between the two groups are better highlighted.

We apply linear discriminant analysis to the same data set, where seven variables (B, D, E, I, J, K and L) appear in the discriminant function. Based on the sign of coefficients of the linear discriminant function, the company having large values for two variables (E and L) and small values for five variables (B, D, I, J and K) will be classified into the top group. Then, the emerging Mahalanobis distance between the two groups, 6.24, is smaller than 7.42 obtained by our method. The number of misclassifications is 7 companies using discriminant analysis, but Figure 1 shows reversed evaluation for only 2 companies.

### Table 8: Efficiency scores and Mahalanobis distance

<table>
<thead>
<tr>
<th>Case</th>
<th>Inputs</th>
<th>Outputs</th>
<th>Mahalanobis distance</th>
<th>Top 30</th>
<th>Bottom 30</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Ave. s. d.</td>
<td>Ave. s. d.</td>
<td></td>
</tr>
<tr>
<td>(a)</td>
<td>I, K</td>
<td>A, B, C, D, E, F, G, H, J, L</td>
<td>-0.09</td>
<td>0.597 0.312</td>
<td>0.604 0.278</td>
</tr>
<tr>
<td>(b)</td>
<td>D, E, J, L</td>
<td>A, B, F, H</td>
<td>4.37</td>
<td>0.784 0.213</td>
<td>0.480 0.316</td>
</tr>
<tr>
<td>(c)</td>
<td>L</td>
<td>B, C, G, H</td>
<td>7.42</td>
<td>0.394 0.278</td>
<td>0.016 0.013</td>
</tr>
</tbody>
</table>

5. Concluding Remarks

We have considered an input output selection method that utilizes a 3-level fractional factorial design, Mahalanobis distance and ANOVA. The concept of discriminant analysis is used to distinguish between the two groups (Top30 and Bottom30), where the efficiency score is utilized as a one-dimensional measure. Variables are selected from the results of ANOVA to maximize the Mahalanobis distance between two groups. We can find an effective variable combination from a limited number of experiments. We demonstrate the effectiveness of this new approach using a case study with Japanese ranked companies. The selected inputs and outputs measure the performance efficiency that can effectively distinguish between the groups of high and low performers.
The obtained combination is not always optimal when estimated from a limited number of experiments. The orthogonal layout executes fractional combinations of experiments and is assigned selected interactions when necessary. Missing interactions may not lead to a good result, so it is necessary to provide the appropriate interactions. Moreover, the underlying assumptions on error terms such as normality, additivity, and homogeneity may be critical. We acknowledge that results may be unstable in the case of a changed assignment of columns or interactions. If it is essential to have a stronger optimality, combinatorial optimization techniques [9] such as branch and bound methods, or meta-heuristic methods can be applied.

References


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## APPENDIX: Financial data extract

<table>
<thead>
<tr>
<th>Nikkei ranking</th>
<th>Company</th>
<th>(A)</th>
<th>(B)</th>
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<th>(D)</th>
<th>(E)</th>
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