Financial Times, March 31, 2006

Making better choices

Uncertainty can make it hard for executives to take good decisions, says **Michael Useem**. Better preparation, having good advisers and learning from experience can help managers avoid poor choices

Making decisions is what managers do every day. Hundreds are minor, some are significant, such as launching a project or hiring staff, and a few are momentous, such as launching an enterprise or restructuring a company. Decision making is at the heart of virtually all management work and a key driver of organisational performance. And uncertainty is ubiquitous in almost all managerial decisions.

In *The Functions of the Executive*, Chester Barnard describes managerial decisions as a "choice of means to accomplish ends which are not personal". In line with this, I define management decisions as those moments when an individual with organisational responsibility faces a discrete, tangible and realistic opportunity to commit enterprise resources to one course or another on behalf of the enterprise's objectives.

For most managers, the decision-making tools at these moments are pretty sound. We all have a few built-in bugs – design flaws of the mind – that can have big consequences, b[illegible] don't usually follow the lead lemming o[illegible]e cliff. By nature, people are overoptimistic and usually assign zero probability to events that are merely unlikely. During Hurricane Katrina, for instance, the dominant government assumption was that the levees would not rupture. We make choices that justify past decisions and then look for data to support them.

Not only do we make these errors, we make them reliably. But that is the good news. Predictable errors are preventable errors, and preparing well for decision making can help managers steer clear of the most common wrong turns when it is uncertain which way to go.

Low preparation + high stress = less optimal decisions

Underpreparation is a major source of suboptimal managerial decisions. Consider one major barrier to good choices: overconfidence, that is, when a manager believes that an outcome is more certain than the facts would suggest. Business studies have found that executives are more audacious when they have to make decisions on products and markets with which they are least familiar.

In one study, researchers Mark Simon and Susan Houghton examined confidence among product managers of small computer software and hardware companies when they introduced radically new products to the market. The more pioneering the product – and, thus, the less familiar the market – the more the product managers were likely to view the prospects for success through rose-tinted glasses.

Other research confirms that managers under time pressure or performing multiple tasks become reluctant to search out releva[illegible]ata. Studies also demonstrate that the a[illegible] effects of underpreparation on decisi[illegible]aking become most pronounced in the most severe conditions.

Management team + high stress = more optimal decisions

While high stress overwhelms smart decision making, low to modest levels of stress can improve it. This is the famous curvilinear relationship between stress and performance, as shown in figure one (below). To the left of the panic point, the adrenaline feed concentrates the mind, mobilises energies and eliminates distractions. To the right of the panic point, however, we no longer think so clearly and are less able to reason carefully.

Well-formed management teams, however, are better able to insulate themselves against that stress, thereby pushing the panic point to the right. With higher levels of stress, the quality of their decisions improves rather than degrading. That is why the armed forces have long seen camaraderie and teamwork as an essential foundation for their primary fighting units. Equally, it is why so many companies have long invested in building and developing their management teams. When formed into cohesive units, both combat and management groups are better able to make good and timely decisions in challenging and risky environments.

The inner circle: a small band of trusted advisers

In her study of computer hardware and software companies in Silicon Valley, Kathleen Eisenhardt reported that one of the key distinguishing factors between companies that moved swiftly and those that plodded along was whether their managers sought advice from experienced and unbiased advisers before reaching decisions. The advisers served as a sounding board, guidance provider and confidence booster, and when consulting with them, company managers became more comfortable in reaching major decisions in uncertain environments, often in half the time.

The value of such an inner circle was evident at computer equipment manufacturer Cisco Systems as it rode the technology wave during the late 1990s and early 2000s. Much of the company's growth came through acquisitions of companies that had developed new technologies. Because being bought out by Cisco was an end game pursued by many Silicon Valley entrepreneurs, offers arrived by the dozen on the desk of Cisco CEO John Chambers. He chose few – only one in ten in the first decade – but his success rate was high.

How did Mr Chambers manage to make consistently good and timely acquisition decisions? When asked, he referred to the advice provided by John Morgridge, Cisco CEO from 1988 to 1995 and current chairman, and chief financial officer Larry Carter. Both individuals, he argued, offered quick and unbiased evaluations of proposed purchases, they did not need to be briefed on company strategy and they rendered candid advice on whether a proposed acquisition was in Cisco's interest. What's more, because neither man wanted Chambers's job, they could advise without self-interest in mind.

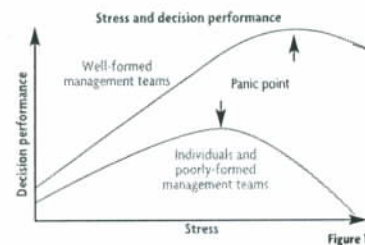
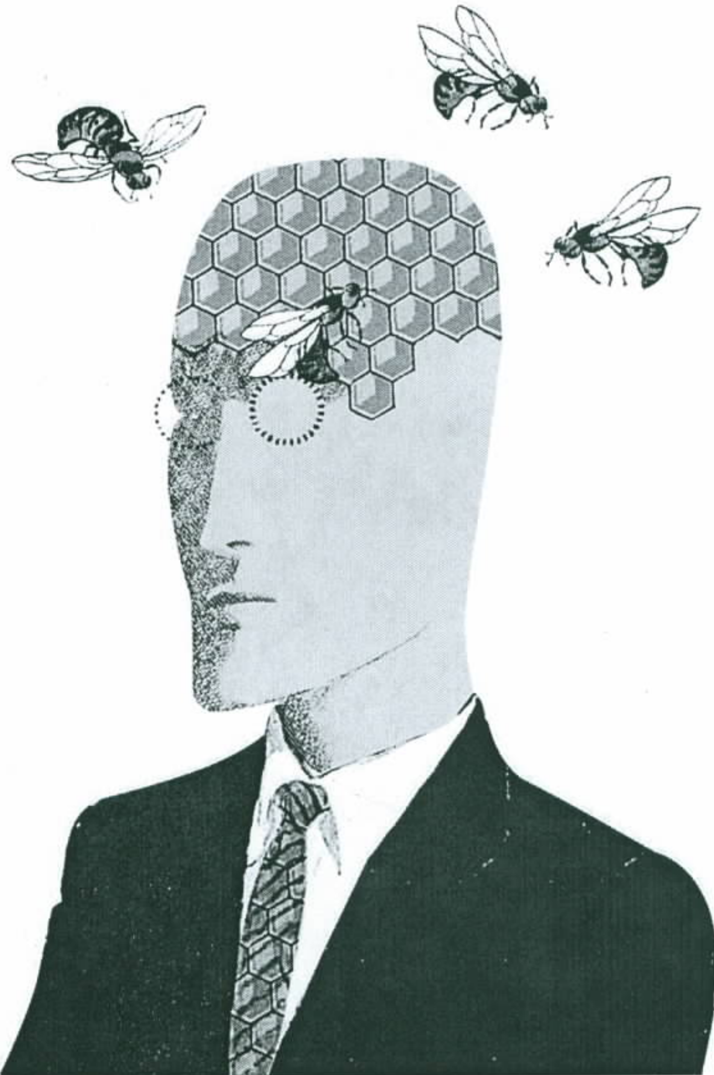


Figure 1



Brett Ryder

The outer circle: a bigger band of more diverse advisers

In his study of engineers, Mark Granovetter discovered that they often developed better leads through their acquaintances than friends. Because the former are more socially remote from the job seeker, they reached further afield and, thus, spotted more openings. As Mr Granovetter's research showed, the job seekers found greater strength in their "weak ties", receiving much from those they knew least well.

The same logic applies to decision making. A manager's weak ties can be more sceptical of a proposed course of action, and the outsiders can help them to see concerns that the inner circle cannot. In other words, the wider and more diverse the manager's outer circle, the better the chance that all stakes are factored into a decision and that "group think" is avoided.

A number of studies have confirmed the importance of expanding the net beyond the inner circle. Mark Mizruchi and Linda Brewster Stearns examined how managers at a large commercial bank closed deals with their corporate customers. Since completing such deals was subject to considerable uncertainty, the researchers hypothesised that the strength of a manager's relations with colleagues would affect the likelihood of successfully doing a deal. They were right, but not exactly in the way that might be anticipated.

When there was a high degree of uncertainty in a deal, the researchers had expected that bankers would more often turn for advice to colleagues with whom they had already established strong working relationships. And they confirmed what they had predicted: the greater the uncertainty in the 137 deals studied, the greater a banker's reliance on trusted colleagues for guidance.

But then the researchers discovered an unexpected twist: the greater the reliance of a banker on their inner circle to the exclusion of the outer circle, the less likely they were to learn what they needed to successfully close the deal. Relying on the inner circle without also turning to the outer circle proved a source of weakness, not strength.

The 70 per cent solution

When managers constantly compile data in pursuit of perfect knowledge – and, thus, perfect certainty – they are edging towards the condition known as "decidophobia", the fear of making a decision.

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Th- "S Marine Corps battles this syndrome v e 70 per cent solution. If an officer ha per cent of the information, has done 70 per cent of the analysis and feels 70 per cent confident, it is time to decide. The logic is simple: a less than ideal action, swiftly executed, stands a chance of success, whereas no action stands no chance. The worst decision is no decision at all.

Analyse, but do not over-analyse. That is much the same message that Hewlett-Packard executive vice-president Ann Livermore sends to the 65,000 employees she oversees in HP's technology services operation. She places primacy on "fast enough" – decision making based on sufficient information, not perfect data.

Decision making as a learned capacity

All organisations have an interest in ensuring that their managers make optimal decisions, but effective decision making is not a natural capacity and companies can do a lot to encourage it.

Predicatable errors are preventable errors, and preparing well for decision making can help managers steer clear of wrong turns

Studies of what researcher Daniel Kahneman terms "systematic biases" – the mental de flaws that separate the choices that n rs actually make from what rational-age... models expect – reveal that such biases can be reduced when managers are trained in decision making and have learned from experience. Company programmes to achieve this would include explicit exposure to decision making under stress and uncertainty, and the fostering of team cohesion, inner and outer circles, and a decision-making culture that emphasises a 70 per cent solution.

A manager's past decisions can serve as a particularly powerful guide for avoiding future mistakes. Consider Liu Chuanzhi, who was working at the Chinese Academy of Sciences in 1984 when his country was embarking on its momentous economic liberalisation process. Mr Liu formed what would become Legend Group, at first distributing a few foreign personal computers and eventually morphing into China's largest PC producer. In 2005, renamed as Lenovo, the company acquired IBM's personal computer unit, making it the third-largest PC producer in the world.

When Mr Liu left the state-sponsored research laboratory, he knew nothing about how to build an enterprise. So, he set about learning to do so by retrospectively studying his own decisions in minute detail. At the end of each week, Mr Liu and his top aides met to review major decisions of the past five days. Many errors were committed, he told me, but the weekly debrief helped "to ensure that we didn't make [the same] mistakes in the future".

Thanks to the reviews and lessons drawn from them, Lenovo was able to weather China's economic gyrations while others faltered. By routinely looking back on his past, Liu Chuanzhi had built his own decision cap--ity for going forward.

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