

DECISION MAKING

DO THE RIGHT THING



MIGUEL Á. ARIÑO
Professor of Managerial Decision Sciences, IESE Business School



PABLO MAELLA
Lecturer in Managing People in Organizations, IESE Business School

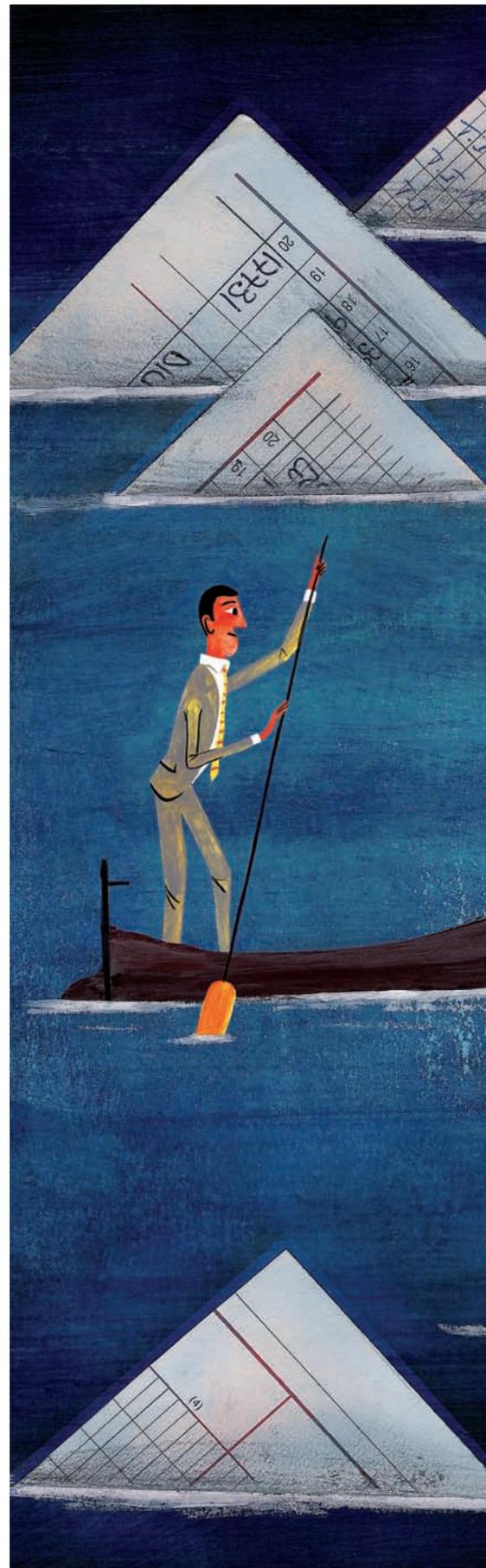
Making decisions and putting them into practice is the key task of management. Many factors come into play, some of them outside your control, such as luck or the effect of decisions taken by third parties, and as a consequence decisions don't always produce the desired results. Nevertheless, in the long term, good decisions will bring better results than bad ones.

DECISION ANALYSIS • STRATEGIC MANAGEMENT

W e learn to walk by walking. We learn to swim by swimming and we learn

to take decisions by... decision making? Not exactly - you can be making decisions all your life and not get any better at it. You know when you can walk or swim and, therefore, whether you've learned how to or not. It's not the same with decisions. It is possible to make a good decision without achieving the desired result, and vice-versa. This means that it is not possible to know if you have decided well by looking at results. This may seem rather surprising, but that's the way it is.

Kenneth Lay, the former CEO of Enron, decided to fiddle the company accounts to show fictitious profits in order to increase his personal wealth. By doing so, he boosted both the share value and his personal wealth, as he received a large part of his compensation in the form of stock options. Given that at the beginning he achieved his objectives, it could be concluded that he had made a good decision. However, it was not. It wasn't a bad decision because he ended up in jail; on the contrary, he





ended up in jail because it was a bad decision. The opposite also applies: sometimes we make good decisions without achieving the desired result. To demonstrate this in class we offer students the chance to take part in a game. The game consists of showing them a container in which there are 99 white balls and one black one. You take out a ball, and if it is white you win €1,000 and if it is black, you lose one euro. Naturally, everyone agrees to take part in the game. Someone takes out a ball and it's black. They have not achieved their objective (the €1,000 that were up for grabs) and yet everyone agrees that they've made the right decision and that they would take part again under the same conditions.

MAKING GOOD AND BAD DECISIONS IS NOT THE SAME AS BEING CERTAIN

● Evaluating whether we are making good or bad decisions, or if we are learning to make better decisions, is not easy. It's not possible to know simply by looking at the consequences of our decisions. This is because the consequences of our decisions depend on many factors, one of which is our decision. But there is also the question of luck, decisions made by other people that also affect us, and decisions that we ourselves made some months ago without realizing that they would affect us now as well. The consequences of our decisions are also affected by external factors beyond our control. Often these factors cannot be anticipated. We usually can't predict that a war will be declared in our principal market or that it will be struck by a devastating hurricane.

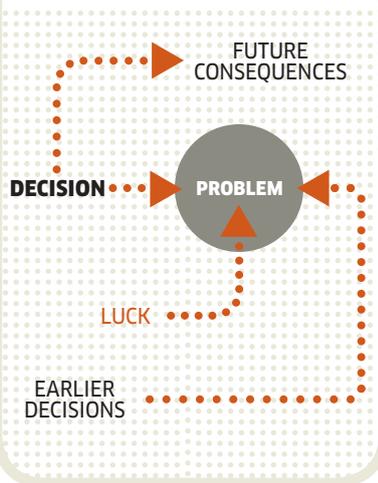
On the other hand, decisions that we make now will also have long-term consequences, and we may be happy with a decision we have taken because the immediate consequences are satisfactory but which may have disastrous consequences in the medium term.

BELIEVING THAT GOOD DECISION MAKING CONSISTS IN BRINGING ABOUT THE DESIRED RESULTS IS TO RAISE DECISIONS TO THE LEVEL OF MAGIC.

THE PRINCIPLES OF DECISION MAKING

- **Identify your objectives**
- Assess the problem realistically
- Do not kid ourselves, thinking that things are as we would like them to be instead of how they really are
- **Be clear about what is the relevant** information in each situation
- Recognize that uncertainty exists and know how to manage it
- **Be creative** about alternatives
- Bear in mind that our decisions may also bring about undesirable or unforeseen consequences
- **Be convinced** that what we have decided must be acted upon, bearing in mind that not everything is rational and that **emotion and intuition** also play a part - for better or worse - in our decisions

These principles must be followed in order to guarantee that we are deciding well, without forgetting that no decision-making process infallibly guarantees the desired results.



IS IT POSSIBLE TO LEARN TO MAKE BETTER DECISIONS?

● Decision making is complex and observing the results of our decisions doesn't allow us to judge whether we are deciding well or not. In these circumstances, what can we do? How can we improve our decisions? There are a number of things to say in this respect. Firstly, stay calm. People worry too much. They think that good decision making leads to good results and when that doesn't happen, they think they have done something wrong. On the contrary. Believing that good decision making consists in bringing about the desired results is to raise decisions to the level of magic, divination or tarot.

MANAGING UNCERTAINTY AND UNDERSTANDING OTHERS' DECISIONS

● With any decision there is uncertainty, and if there wasn't, there wouldn't be a problem. But that's the way uncertainty is: uncertain. It's not knowing what will happen, and therefore when we make decisions we cannot know what is not known because it is uncertain. Coming to terms with this in our daily lives, both personal and professional, is very important, as it frees us from much tension and anguish, and from the need and the responsibility of knowing what cannot be known. We are responsible for the factors under our control and those that we may possibly influence, but that is all. We have to free ourselves from an unjustified sense of responsibility. Being conscious of the fact that the consequences of our decisions are affected by luck, by external circumstances beyond our control and by decisions taken by third parties helps us keep things in perspective.

Internalizing this fundamental principle will also help us to avoid being unfair to our subordinates or people who work with us. Often things don't turn out as planned for reasons beyond an individual's control. In such cases it is unfair to blame subordinates for something that is not their fault. A paradigm of incompetent

management is to judge the actions of others using information that was only available *a posteriori*, which the person who took the decision did not know was going to happen. In hindsight, everyone knows what should have been done. That is why you have to bet on football games before the matches have been played.

The fact that decisions cannot be judged by whether the consequences are positive or negative doesn't mean that it doesn't matter what you do. Even though we cannot establish a direct line between results and good decisions, taking together all of the decisions made in the long term, good decisions lead to better results than bad ones.

Furthermore, if the criteria for evaluating whether we are making good or bad decisions are the results, we still cannot know if we are making good decisions or not until we have acted upon them and seen what happens. That is to say, we can't judge whether the decision is correct until we have seen the consequences. But it is management's responsibility to know if a decision is good or not before execution. Knowing this *after* the decision has been made is too late.

WHAT IS GOOD DECISION MAKING?

● So, what is good decision making? Deciding is a process, and there are both good and bad processes for making decisions. And it is possible to assess whether a decision-making process is effective or defective.

There is a series of principles for correct decision-making. While it is never possible to guarantee that any one decision will bring good results, following these principles will guarantee that you are making decisions well, that you are learning to make them better each time and that over the long term you will get better results than you would using a faulty process.