

How do I make good decisions?

- 1.** What are the steps in the decision-making process?
- 2.** What factors affect how decisions are made?
- 3.** How can managers make more effective decisions?

▶▶▶ Peter Brown, chair and CEO of Vancouver-based Canaccord Capital faced a very big decision in spring 2004.¹ Canaccord is Canada's largest independent investment firm, with a specialty in small-, mid-, and large-size capitalization companies. Brown wondered whether the company should file for an initial public offering (IPO) in June. An IPO would allow Canaccord to raise money by letting people purchase shares in the company. Firms often raise between \$20 million and \$40 million in an IPO. Brown had weighed the issue for quite some time, and had originally decided that 2005 would be a better time to file for an IPO. But recent gains in North American stock markets led him to reconsider the decision.

Brown's decision is complicated by his feelings about Canaccord: "We enjoy

being a private company now and I hate the thought of being public. But having said that, the landscape has changed."²

By selling its shares on the stock market, Canaccord would become a public company and be put under greater media spotlight, something Brown does not really look forward to. Three of Canaccord's competitors in Toronto—Griffiths McBurney, First Associates, and Dundee—have gone public recently, fuelling speculation that Canaccord will follow suit. "Canaccord has reached a size now where going public would be an expected development," says Tony Hepburn, president of Vancouver-based Odlum Brown. "It has been talked about before and I have definitely had the impression that this was something on their calendar."³

Think About It

How do CEOs make important decisions? Put yourself in Peter Brown's shoes. What steps would you take to determine whether Canaccord should go public or remain a private corporation? How could he evaluate the effectiveness of a decision to go public? What decision criteria might he use?

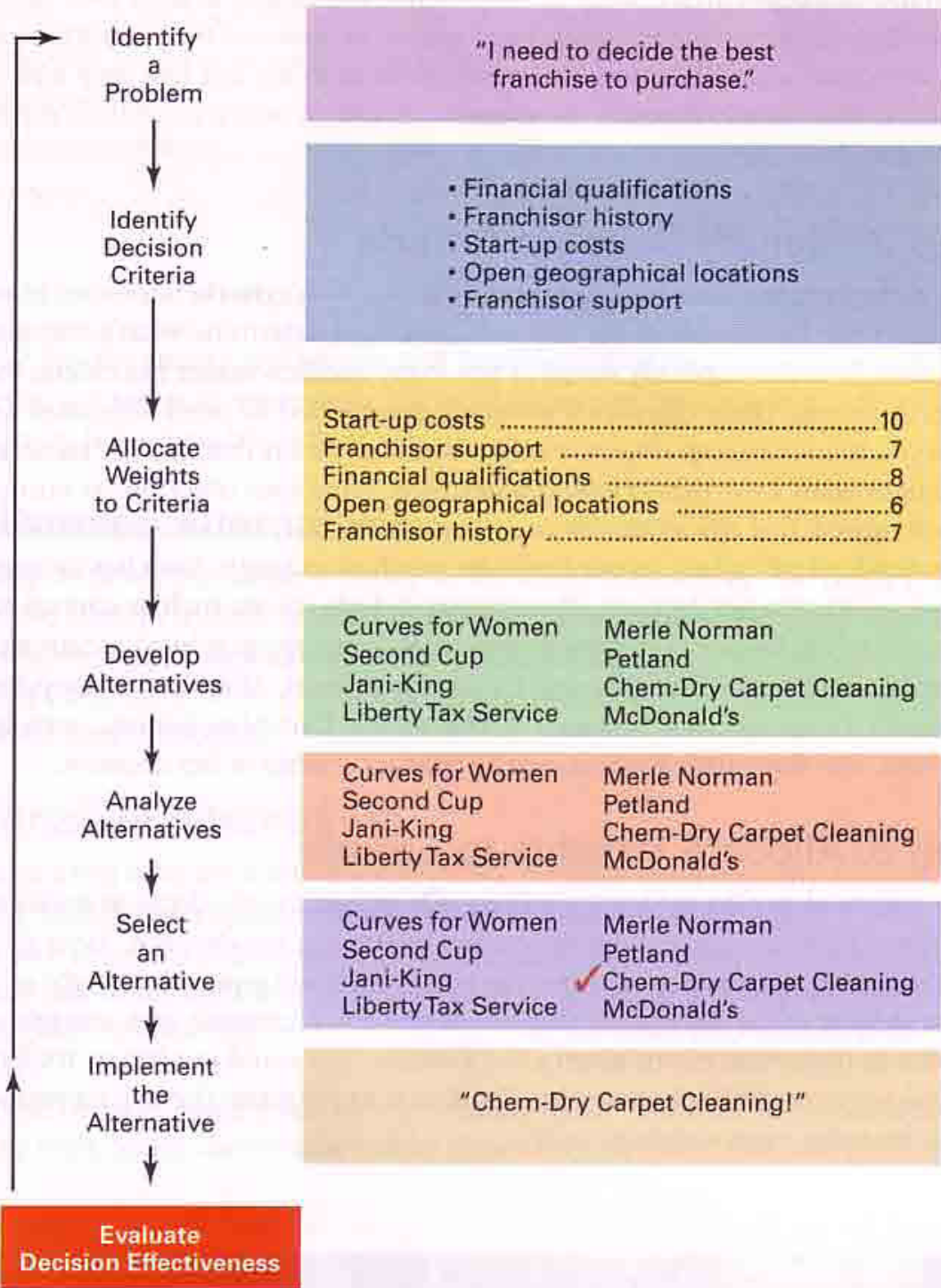
The decision-making process

Individuals are continually faced with making **decisions**. That is, they make choices from two or more alternatives. For instance, you have made decisions about what post-secondary institution to attend, and what your likely major will be. Top managers make decisions about their organization's goals, where to locate manufacturing facilities, what new markets to move into, and what products or services to offer. Middle and first-line managers make decisions about weekly or monthly production schedules, problems that arise, pay raises, and disciplining employees. Individual employees make decisions about how well they will do their job, whether or not they will go to work, even whether they will look for another job. How do people make their decisions?

Although decision making is typically described as "choosing among alternatives," that view is simplistic. Why? Because decision making is a comprehensive process, not just a simple act of choosing among alternatives.⁵ Even for something as straightforward as deciding where to go for lunch, you do more than just choose burgers or pizza. You may consider various restaurants, how you will get there, who might go with you. Granted, you may not spend a lot of time contemplating a lunch decision, but you still go through a process when making that decision. What *does* the decision-making process involve?

Exhibit 5-1 illustrates the **decision-making process**, a set of eight steps that begins with identifying a problem and decision criteria and allocating weights to those criteria; moves to developing, analyzing, and selecting an alternative that can resolve the problem; then moves to implementing the alternative; and concludes with evaluating the decision's effectiveness. This process is as relevant to your personal decision about what movie to see on a Friday night as it is to a corporate action such as a decision to use technology in managing client relationships. The process also can be used to describe both individual and group decisions. Let's take a closer look at the process in order to understand what each step involves. We'll use an example—deciding what is the best franchise to purchase—to illustrate.

The Decision-Making Process



Step 1: Identify a Problem

The decision-making process begins with the existence of a **problem** or, more specifically, a discrepancy between an existing and a desired state of affairs.⁶ Take Joan, a laid-off sales manager who has been out of work for six months. She's decided she wants to become an entrepreneur rather than return to a corporate job. For simplicity's sake, assume that Joan doesn't want to purchase an existing small business and instead has decided to look at possible franchises to purchase. Now we have a problem. There's a disparity between where Joan is now (unemployed) and where she wants to be (an entrepreneur and franchise owner). She has a decision to make about the best franchise to purchase.

One thing our example doesn't do is tell us how managers identify problems. In the real world, most problems don't come with neon signs flashing "problem." For example, if sales representatives complain to their manager that their computers are inadequate to do their jobs effectively, that might be a clear signal to the manager that new computers need to be purchased. But the real problem may not be the computers at all. It could be problems with the software, or it could be that employees have not been trained to use the computer (or the software) correctly. Managers should be careful not to confuse problems with the symptoms of the problem. Is a 5 percent drop in sales a problem? Or are declining sales merely a symptom of the *real* problem, such as unsatisfactory products, high prices, poor advertising, or poor customer service? Also, keep in mind that problem iden-

tification is subjective. What one manager considers a problem might not be considered a problem by another manager. Furthermore, a manager who mistakenly resolves the wrong problem perfectly is likely to perform just as poorly as the manager who doesn't identify the right problem and does nothing.

As you can see, effectively identifying a problem isn't simple or trivial.⁷ Managers can be better at it if they understand the three characteristics of a problem: They have to be aware of it; they have to be under pressure to act; and they must have the authority, information, and resources needed to take action.⁸

Managers become aware of a problem by seeing where things stand currently versus where they should be or where they want them to be. If they're not where they want them to be or if things aren't going as they should, then a discrepancy exists. But that's not enough to make it a problem.

A discrepancy without pressure to act is a problem that can be postponed. To initiate the decision process, the problem must put pressure on the manager to act. Pressure might come from, for example, organizational policies, deadlines, financial crises, competitor actions, customer complaints, expectations from the manager, or an upcoming performance evaluation.

Finally, managers aren't likely to characterize something as their own problem if they believe they don't have the authority, information, or resources necessary to act on it. If managers recognize a problem and are under pressure to act but feel they have inadequate resources, they usually describe the situation as one in which unrealistic expectations are being placed on them.

Step 2: Identify Decision Criteria

Once a manager has identified a problem, the **decision criteria** important to resolving the problem must be identified. That is, managers must determine what's relevant in making a decision. Whether explicitly stated or not, every decision maker has criteria that guide his or her decisions. These criteria are generally determined by one's objectives. For instance, when you buy a car, your objective might be to have a car that shouts "status symbol." Or you might want a car that is low maintenance. With your objective in mind, you might consider speed, fuel efficiency, colour, manufacturer, size, and so on as criteria on which to evaluate which car to buy. In our franchise purchase example, Joan has to assess what factors are relevant to her decision. These might include criteria such as start-up costs, financing availability, failure rate, growth potential, open geographical locations, franchisor history, financial qualifications, and franchisor support. After careful consideration, Joan decides that start-up costs, financial qualifications, franchisor history, open geographical locations, and franchisor support are the relevant criteria in her decision.

Step 3: Allocate Weights to Criteria

If the criteria identified in Step 2 aren't equally important, the decision maker must weight the items in order to give them the correct priority in the decision. How do you weight criteria? A simple approach is to give the most important criterion a weight of 10 and then assign weights to the rest against that standard. Thus, a criterion with a weight of 10 would be twice as important as one given a 5. Of course, you could use 100 or 1000 or any number you select as the highest weight. The idea is to prioritize the criteria you identified in Step 2 by assigning a weight to each.

Criteria and Weights for Franchise Decision

Criterion	Weight
Start-up costs.....	10
Franchisor support	8
Financial qualifications	6
Open geographical locations	4
Franchisor history	3

Exhibit 5-2 lists the criteria and weights that Joan developed for her franchise purchase decision. As you can see, start-up costs are the most important criteria in her decision, and franchisor history is the least important.

Step 4: Develop Alternatives

The fourth step requires the decision maker to list viable alternatives that could resolve the problem. No attempt is made to evaluate the alternatives, only to list them. Joan identified eight potential franchises as viable choices including Curves for Women, Second Cup, Jani-King Cleaning Service, Liberty Tax Service, Merle Norman, Petland, Chem-Dry Carpet Cleaning, and McDonald's.

Step 5: Analyze Alternatives

Once the alternatives have been identified, a decision maker must critically analyze each one. How? By appraising it against the criteria established in Steps 2 and 3. From this comparison, the strengths and weaknesses of each alternative become evident. Exhibit 5-3 shows the assessed values that Joan gave each of her eight alternatives after extensively studying the franchise opportunities and reading the latest information from business magazines.

Keep in mind that the ratings given the eight franchises are based on the personal assessment made by Joan. Some assessments can be done objectively. For instance, the start-up

Assessed Values of Franchise Opportunities Using Decision Criteria

	Start-Up Costs	Franchise Support	Financial Qualifications	Open Locations	Franchisor History
Franchise					
Curves for Women	10	3	10	8	5
Second Cup	8	7	7	8	7
Jani-King	8	5	7	10	10
Liberty Tax Service	8	7	7	8	7
Merle Norman	7	8	7	8	7
Petland	8	3	6	10	8
Chem-Dry Carpet Cleaning	10	7	8	6	7
McDonald's	4	10	4	8	10

Evaluation of Franchise Alternatives Against Weighted Criteria

	Start-Up Costs	Franchise Support	Financial Qualifications	Open Locations	Franchisor History	Total
Franchise						
Curves for Women	100	24	60	32	15	231
Second Cup	80	56	42	32	21	231
Jani-King	80	40	42	40	30	232
Liberty Tax Service	80	56	42	32	21	231
Merle Norman	70	64	42	32	21	229
Petland	80	24	36	40	24	204
Chem-Dry Carpet Cleaning	100	56	48	24	21	249
McDonald's	40	80	24	32	30	206

costs reflect the total investment required by each franchisor, and financial qualifications are the amounts set by each franchisor. However, the assessment of franchisor support is more of a personal judgment. The point is that most decisions by managers involve judgments—the criteria chosen in Step 2, the weights given to the criteria in Step 3, and the analysis of alternatives in Step 5. This explains why two franchise buyers with the same amount of money may look at two totally different sets of alternatives or even rate the same alternatives differently.

Exhibit 5-3 represents only an assessment of the eight alternatives against the decision criteria. It doesn't reflect the weighting done in Step 3. If you multiply each alternative (Exhibit 5-3) by its weight (Exhibit 5-2), you get Exhibit 5-4 (see below). The sum of these scores represents an evaluation of each alternative against both the established criteria and weights. There are times when a decision maker might not have to do this step. If one choice had scored 10 on every criterion, you wouldn't need to consider the weights. Similarly, if the weights were all equal, you could evaluate each alternative merely by summing up the appropriate lines in Exhibit 5-3. In this instance, the score for Curves for Women would be 36 and Petland's score would be 35.

Step 6: Select an Alternative

What does it mean if the "best" alternative doesn't feel right to you after going through the decision-making steps?

Step 6 is choosing the best alternative from among those considered. Once all the pertinent criteria in the decision have been weighted and viable alternatives analyzed, we merely choose the alternative that generated the highest total in Step 5. In our example (Exhibit 5-4), Joan would choose Chem-Dry Carpet Cleaning since it scored highest on the basis of the criteria identified, the weights given to the criteria, and her assessment of each franchise's ranking on the criteria. It's the "best" alternative and the one she should choose.

Step 7: Implement the Alternative

Step 7 is concerned with putting the decision into action. This involves conveying the decision to those affected by it and getting their commitment to it. Managers often fail to get buy-in from those around them before making a decision, even though successful implementation requires participation. One study found that managers used participa-

tion in only 20 percent of decisions, even though broad participation in decisions led to successful implementation 80 percent of the time. The same study found that managers most commonly tried to implement decisions through power or persuasion (used in 60 percent of decisions). These tactics were successful in only one of three decisions, however.⁹ If the people who must carry out a decision participate in the process, they're more likely to enthusiastically support the outcome than if you just tell them what to do. Parts 3, 4, and 5 of this book discuss how decisions are implemented by effective planning, organizing, and leading.

Step 8: Evaluate Decision Effectiveness

The last step in the decision-making process involves evaluating the outcome of the decision to see if the problem has been resolved. Did the alternative chosen in Step 6 and implemented in Step 7 accomplish the desired result? In Part 5 of this book, where we look at the controlling function, we will see how to evaluate the results of decisions.

What if the evaluation shows the problem still exists? The manager would need to assess what went wrong. Was the problem incorrectly defined? Were errors made in the evaluation of the various alternatives? Was the right alternative selected but poorly implemented? Answers to questions like these might send the manager back to one of the earlier steps. It might even require re-doing the whole decision process.

Decision-Making Styles

Suppose that you were a new manager at Sony or at the local YMCA. How would you make decisions? Decision-making styles differ along two dimensions.²¹ The first dimension is an individual's *way of thinking*. Some of us are more rational and logical in the way we process information. A rational type processes information in order and makes sure that it's logical and consistent before making a decision. Others tend to be creative and intuitive. An intuitive type doesn't have to process information in a certain order and is comfortable looking at it as a whole.

The other dimension is an individual's *tolerance for ambiguity*. Some of us have a low tolerance for ambiguity. These types need consistency and order in the way they structure information so that ambiguity is minimized. On the other hand, some of us can tolerate high levels of ambiguity and are able to process many thoughts at the same time. (To assess your tolerance for ambiguity, see *Self-Assessment—How Well Do I Handle Ambiguity?*, pages 203–204, in Chapter 7.) When we diagram these two dimensions, four decision-making styles are evident: directive, analytic, conceptual, and behavioural (see Exhibit 5–11 on page 142). Let's look more closely at each style.

- *Directive style*. Individuals with a **directive style** have low tolerance for ambiguity and are rational in their way of thinking. They're efficient and logical. Directive types make fast decisions and focus on the short run. Their efficiency and speed in making decisions often result in their making decisions with minimal information and assessing few alternatives.
- *Analytic style*. Individuals with an **analytic style** have much greater tolerance for ambiguity than do directive types. They want more information before making a decision and consider more alternatives than directive-style decision makers do. Analytic-style decision makers are characterized as careful decision makers with the ability to adapt to or cope with unique situations.
- *Conceptual style*. Individuals with a **conceptual style** tend to be very broad in their outlook and look at many alternatives. They are intuitive, focus on the long run, and are very good at finding creative solutions to problems.
- *Behavioural style*. Individuals with a **behavioural style** have a low tolerance for ambiguity and an intuitive way of thinking. They work well with others, are concerned about the achievements of those around them, and are receptive to suggestions from others. They often use meetings to communicate, although they try to avoid conflict. Acceptance by others is important to this decision-making style.

Decision-Making Biases and Errors

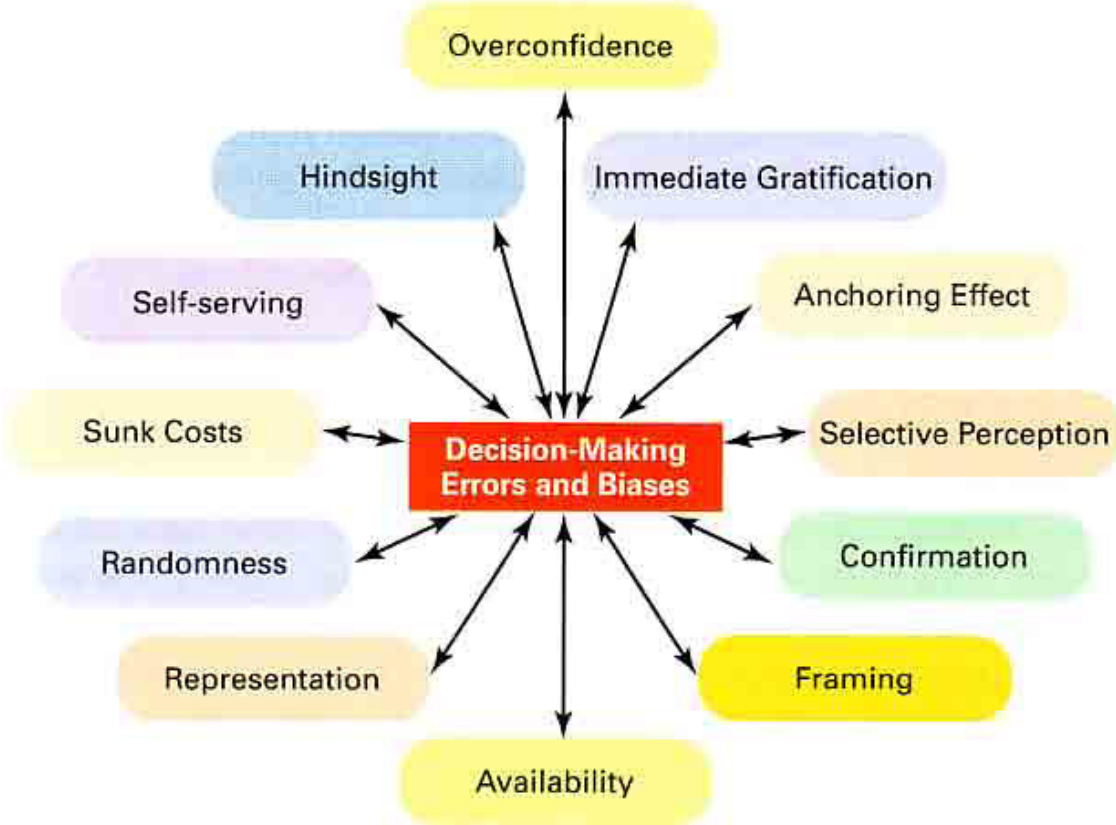
When managers make decisions, not only do they use their own particular style, but many use "rules of thumb," or **heuristics**, to simplify their decision making. Rules of thumb can be useful to decision makers because they help make sense of complex, uncertain, and ambiguous information.²² Even though managers may use rules of thumb, that doesn't

mean those rules are reliable. Why? Because they may lead to errors and biases in processing and evaluating information. Exhibit 5-12 identifies 12 common decision-making biases and errors. Let's take a quick look at each.²³

- *Overconfidence bias.* Decision makers tend to think they know more than they do or hold unrealistically positive views of themselves and their performance. For instance, a sales manager brags that his presentation was so good that there is no doubt the sale will be his. Later he learns that he lost the sale because the client found him obnoxious.
- *Immediate gratification bias.* Decision makers tend to want immediate rewards and to avoid immediate costs. For these individuals, decision choices that provide quick payoffs are more appealing than those in the future. For instance, you decide to go to a movie tonight rather than study for an exam that is coming up later in the week.
- *Anchoring effect.* Decision makers fixate on initial information as a starting point and then, once set, fail to adequately adjust for subsequent information. First impressions, ideas, prices, and estimates carry unwarranted weight relative to information received later. For instance, Helen saw the home she wanted at a good price, but she didn't have the money at the time. Six months later, house prices have risen significantly, but Helen doesn't understand why she can't buy a house for the old price now.
- *Selective perception bias.* Decision makers selectively organize and interpret events based on their biased perceptions. This influences the information they pay attention to, the problems they identify, and the alternatives they develop. For instance, before John meets with two job candidates, he learns that one went to his alma mater. He does not seriously consider the other job candidate because he believes that graduating from the same university as he did makes the candidate superior.

- *Confirmation bias.* Decision makers seek out information that reaffirms their past choices and discount information that contradicts past judgments. These people tend to accept at face value information that confirms their preconceived views and are critical and skeptical of information that challenges these views. For instance, Pierre continues to give business to the same supplier, even though the supplier has been late on several deliveries. Pierre thinks the supplier is a nice person, and the supplier keeps promising to deliver on time.
- *Framing bias.* Decision makers select and highlight certain aspects of a situation while excluding others. This distorts what they see and creates incorrect reference points. For instance, Mai knows that a decision she is about to present to her manager is extremely risky. However, she knows that if everything turns out well, the company will stand to make a lot of money from the decision. When she presents the decision to her boss, she says very little about the risk, and instead emphasizes how much money the company could make from this decision.
- *Availability bias.* Decision makers tend to remember events that are the most recent and vivid in their memory. The result? This tendency distorts their ability to recall events in an objective manner and results in distorted judgments and probability estimates. For instance, Stan has to prepare performance appraisals for his team this week. One member of his team did an outstanding presentation last week, covering for someone who had started off the presentation with a number of serious errors. Stan bases his annual evaluations on last week's presentations rather than considering each employee's performance over the entire year.
- *Representation bias.* Decision makers assess the likelihood of an event based on how closely it resembles other events or sets of events. Managers exhibiting this bias draw analogies and see identical situations where they don't exist. When investors invested in ill-conceived dot-com companies after concluding that Amazon.com was going to be the next great business model, they mistakenly thought that marketing on the Internet would be good for any new company, not just Amazon.com.

Common Decision-Making Biases and Errors



Working Together: Team-Based Exercise

The situation described in this problem is based on actual cases in which men and women lived or died depending upon the survival decision they made. Your “life” or “death” will depend on how well your group can share its present knowledge of a relatively unfamiliar problem, so that the group can make decisions that will lead to your survival.²⁹

It is approximately 2:30 p.m. on October 5, and you have just crash-landed in a float plane on the east shore of Laura Lake in the Subarctic region of the Northern Quebec–Newfoundland and Labrador border. The pilot was killed in the crash, but the rest of you are uninjured. Each of you is wet up to the waist and has perspired heavily. Shortly after the crash, the plane drifted into deep water and sank with the pilot’s body pinned inside. The pilot was unable to contact anyone before the crash. However, ground sightings indicate that you are 48 kilometres south of your intended course and approximately 22 air miles east of Schefferville, your original destination, and the nearest known habitation. Schefferville (pop. 240) is an iron ore–mining town approximately 300 air miles north of the St. Lawrence, 720 kilometres east of the James Bay/Hudson Bay area, 1290 kilometres south of the Arctic Circle, and 480 kilometres west of the Atlantic Coast. It is reachable only by air or rail, all roads ending a few miles from town. Your party was expected to return from northwestern Labrador to Schefferville no later than October 19 and filed a flight plan with Transport Canada via Schefferville radio to that effect.

The immediate area is covered with small evergreen trees (4 to 10 centimetres in diameter). Scattered in the area are a number of hills having rocky and barren tops. Tundra (arctic swamps) make up the valleys between the hills and consist only of small scrubs. Approximately 25 percent of the area in the region is covered by long, narrow lakes that run northwest to southeast. Innumerable streams and rivers flow into and connect the lakes. Temperatures during October vary between -4°C and 2°C , although it sometimes can go as high as 10°C and as low as -18°C . Heavy clouds cover the sky three quarters of the time, with only one day in ten being fairly clear. Thirteen to eighteen centimetres of snow are on the ground. However, the actual depth varies enormously because the wind sweeps the exposed areas clear and builds drifts 0.9 to 1.5 metres deep in other areas. The wind speed averages 20 to 25 kilometres/hour and is mostly out of the west-northwest.

You are all dressed in insulated underwear, socks, heavy wool shirts, pants, knit gloves, sheepskin jackets, knitted wool toques, and heavy leather hunting boots. Collectively, your personal possessions include \$150 in bills, 4 loonies, 4 quarters, 2 dimes, 1 nickel, and 3 pennies; 1 pocket knife (2 blades and an awl which resembles an ice pick); one stub lead pencil; and an air map.

Before the plane drifted away and sank, you were able to salvage the 15 items listed on the attached chart. Your task is to rank these items according to their importance to your survival, from “1” for the most important up to “15” for the least important.

Items	Step 1: Your ranking	Step 2: Team ranking
A magnetic compass		
A 4-litre can of maple syrup		
A sleeping bag per person (arctic type; down-filled with liner)		
A bottle of water purification tablets		
A 6 m x 6 m piece of heavy duty canvas		
13 wood matches in a metal screwtop, water- proof container		
75 m of 0.5-cm braided nylon rope, 20 kg test		
An operating 4-battery flashlight		
3 pairs of snowshoes		
A fifth of Bacardi rum (151 proof)		
Safety-razor shaving kit with mirror		
A wind-up alarm clock		
A hand axe		
One aircraft inner tube for a 35-cm wheel (punctured)		
A book entitled <i>Northern Star Navigation</i>		

C. F. Martin Guitar Company

The C. F. Martin Guitar Company has been producing acoustic instruments since 1833. A Martin guitar is among the best that money can buy. Current CEO Christian Frederick Martin IV—better known as Chris—continues to be committed to the guitar maker's craft. During 2002, the company sold about 77 000 instruments and hit a record \$77 million in revenue. Despite this success, Chris is facing some serious issues.

Martin Guitar is an interesting blend of old and new. Although the equipment and tools may have changed over the years, employees remain true to the principle of high standards of musical excellence. Building a guitar to meet these standards requires considerable attention and patience. In a 1904 catalogue, a family member explained, "How to build a guitar to give this tone is not a secret. It takes care and patience." Now well over a century later, this statement is still an accurate reflection of the company's philosophy.

From the very beginning, quality has played an important role in everything that Martin Guitar does. Part of that quality approach includes a long-standing ecological policy. The company depends on natural-wood products to make its guitars, but a lot of the wood supply is vanishing. Chris has long embraced the responsible use of traditional wood materials, going so far as to encourage suppliers to find alternative species. Based on thorough customer research, Martin Guitar introduced guitars that used structurally sound woods with natural cosmetic defects that were once considered unacceptable. In addition, Martin Guitar follows the directives of CITES, the Convention on

International Trade in Endangered Species of Wild Fauna and Flora (www.cites.org), even though it has the potential to affect Martin Guitar's ability to produce the type of quality products it has in the past. This treaty barred the export of the much-desired Brazilian rosewood, which is considered endangered. A guitar built from the remaining supply of this popular wood has a hefty price tag—more than \$9500. Similar prices may be in line for the leading alternative, Honduras mahogany. Chris says, "All of us who use wood for the tone [it makes] are scrambling. Options are limited."

Although the company is rooted in its past, Chris is wondering whether he should go in new directions. For instance, he could try selling guitars in the under-\$800 segment, a segment that accounts for 65 percent of the acoustic guitar industry's sales. A less expensive guitar would not look, smell, or feel like the company's pricier models. But Chris thinks that it would sound better than guitars in that price range made by other companies. Chris explains, "My fear is that if we don't look at alternatives, we'll be the company making guitars for doctors and lawyers. If Martin just worships its past without trying anything new, there won't be a Martin left to worship."

What should Chris do? Why?

Sources: Information from C. F. Martin's website, <http://www.cfmartin.com> (accessed April 24, 2003); D. Lieberman, "Guitar Sales Jam Despite Music Woes," *USA Today*, December 16, 2002, p. 2B; and S. Fitch, "Stringing Them Along," *Forbes*, July 26, 1999, pp. 90-91.