

# The Fundamental Decision Determining the Business of the Organization

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A major responsibility of any leader, according to Peter Drucker, is to determine the *real* business of an organization. I learned this lesson even before I met Drucker and became his student. I was a young manager, but although I had held management and executive titles in several business situations, I knew very little about business management. As a West Point graduate who had served in the Air Force, I knew something about leadership, but I hadn't sufficiently applied those skills to business management.

Shortly before meeting Drucker, I became director of research and development for a small company producing life-support equipment for military aviators as well as commercial airlines. The company was facing increasing difficulties resulting from the government's purchasing policies and timing. My company would receive a contract, and when the work was complete and the product delivered, it would have to wait another year for the next contract. This made planning difficult and resulted in a continuous

cycle of peaks and valleys in production, leaving us with too many or too few workers.

About 60 percent of our products went to the government, the remainder to the airlines. We had no product for the individual consumer. About every five years the president would raise this issue and arrive at essentially the same solution: develop a consumer product that would use the same machinery, workers, and materials to smooth out the peaks and valleys. Success would mean an end to this problem. Unfortunately, the result was always the same: initial enthusiasm and high hopes followed by a considerable investment, followed by failure and a big loss. Each failure apparently resulted from a different cause, so no one ever considered there might a larger issue.

One year, at our annual sales meeting, we gave each attendee a copy of Drucker's book, *Management: Tasks, Responsibilities, Practices*. In it, Drucker exhorted managers to determine what business they were in. This subject was number one on the agenda, and it soon became obvious why our efforts to enter the consumer market always failed. The products had nothing to do with our core business of providing life support protection for aviators. For example, we entered the market for protective motorcycle helmets, about which we knew nothing except how to produce the helmet. It turned out that what the military valued and what the consumer valued were entirely different. Furthermore, we had no idea how to reach the motorcycle helmet consumer. In the end, the company invested a million dollars, produced a heavy, very protective but very uncomfortable and high-priced motorcycle helmet that no one wanted, and almost went bankrupt trying to introduce it.

## Defining Your Business Is No Small Thing

Drucker taught that determining what business you are in is essential to creating an organization's future, and therefore is any leader's primary responsibility. Once that's determined, a lot falls into place.

An entire set of decisions follow naturally about how to run any organization.

Accurately defining your business automatically saves time, money, and resources that would otherwise be wasted on something that detracts from, rather than adds value to, your business. It also helps you focus on those opportunities and possibilities that are important to building your business. Just as no leader has enough resources to pursue every opportunity or avoid every threat, until you decide what business you are in, your organization will drift, no matter how effective a leader you otherwise are. This is a constant theme in management and leadership: resources of any kind are always limited. Therefore, leaders must make choices and concentrate their always limited resources where they will do the most good. This is true whether yours is a for-profit business, a nonprofit organization, a government agency, or any other organization. Your staff may be striving with all their abilities to support a direction that can hurt your business simply because they don't have a clear understanding of what the real business is or where it should be going.

Today, we call this definition a "mission statement." Drucker's favorite mission statement, though not recent or short, came from a very old business, Sears Roebuck. Simply stated, it was to be the informed and responsible retailer, initially for the American farmer, and later for the American family.<sup>1</sup> It changed Sears from a struggling mail order house, which was sometimes close to bankruptcy, to the world's leading retailer, all within ten years.

## **How to Obtain Commitment to the Mission Throughout the Organization**

Of course, there is only one leader, and ultimately this leader is responsible for the final mission statement and the business. That said, Peter learned much from the Japanese. He had observed an interesting difference in American and Japanese management practices.

American leaders made decisions very quickly but gained little real support for their decisions from leaders at all levels, which caused many of their initiatives to fail.

Japanese leaders made decisions more slowly. This frequently frustrated American leaders negotiating with them. However, once the decision was made, the entire organization was committed to it, and supported it much more than their American counterparts.

Why was this? Drucker found that the Japanese practiced a system known as *ringi*, where all major decisions had to be reviewed and commented on by managers throughout the company. This could require several cycles and months of feedback and revision. However, the consensus built by *ringi* resulted in major commitments by leaders at all levels, who all felt ownership in the decision.

I doubt that adopting *ringi* in all countries would be very effective. During the Japanese management fad of the early 1980s, many U.S. firms tried it. It didn't work. American emphasis on rapid decision making goes back to the frontier days when leaders had to make decisions quickly, and it became ingrained in our culture and the way our leaders operate.

Ideas usually cannot be imported without modification. The cultures and other aspects of leadership and management are different; therefore, that they fail without some modification shouldn't be surprising. Even adopting simple devices may cause problems. For example, traffic signals were invented in England, although the version used today was developed in the United States. Despite their successful use elsewhere, when traffic signals were introduced in Ireland, the Irish were so outraged they actually rioted. Why? Because the red light was on top and the green light on the bottom, and to the Irish, red is the color of Britain; green, Ireland. That red was placed over green was infuriated many Irish people. The solution was to mount the traffic lights horizontally.

Although copying *ringi* in America didn't work either, Drucker recognized the merit of the idea—in particular, the value of

consensus for all organizations—and adapted the concept to involve subordinate leaders, but in different ways than the Japanese.

In the past, meetings attended by all managers, or at least those most relevant to the question, were used to garner consensus. Usually someone in or outside the company facilitated the process.

These days, there are many ways to incorporate shared participation in the decision-making process, and these frequently involve new technologies. Glassdoor.com, an online site, allows employees to anonymously review their employers and share salary information. In its annual list of “the naughtiest and nicest chief executives” of 2008 (based on the anonymous reviews), Glassdoor picked Arthur D. Levinson, CEO of Genentech, as the “nicest.” He had an amazing 93 percent approval rating. The *New York Times* quoted a strategic planner at Genentech who wrote that Levinson had implemented a decision-making structure that forced authority downward to the lowest possible level in the company, which provided many opportunities to participate and exercise judgment.<sup>2</sup>

Contrary to what some think, general participation in the decision-making process does not make the leader seem weak or ineffective. In fact, an early advocate of this type of approach was the most effective chief of staff the Israeli Army ever had, General Moshe Dayan, the man responsible for victory in two of his country’s major wars: the Sinai campaign of 1956 as chief of staff, and the Six-Day War of 1967 as minister of defense. Observers accustomed to directive, high-speed decision-making by military leaders were amazed to see Dayan make some major decisions in his staff meetings by discussion followed by a show of hands!

## Why Everyone Should Be Heard

One major reason for listening to everyone as you define your mission statement is to gain commitment. Another, which goes right along with commitment, is that other leaders also have good ideas,

and may know something that you do not. By hearing all, you not only gain commitment, you may avoid missing both opportunities and threats to your mission statement. Some executives are reluctant to conduct public meetings about such a major decision, either fearing criticism or that their proposed definition will be defeated. If either happened, your proposal probably should be defeated, or at least modified. As Drucker noted, when making decisions about your business, dissent is a very good thing.

Finally, as Drucker pointed out, the answer to “What is our business?” is never obvious. You need help from others on your team.

Deciding on the central issues of your business or organization with a systematic method in which all key managers participate is essential. With others in your organization focused on the same question, you as leader are far more likely to come up with the answer that makes the best sense and enables you to build your business for the future.

Of course, you need not follow General Dayan’s example and settle this issue by a show of hands. The concept can be modified and applied as necessary. Your job is not to sell your preconceived notion but to arrive at an optimal definition of your business through consensus. Do this, and you will not only sharpen the wording of your original definition, you will see everyone in the organization quickly get behind and support the business definition decided upon.

## **How to Answer the Question, What Is Our Business?**

To formulate a definition, you need more than opinions. You must see the business from the customer’s point of view. As Drucker wrote, “The customer defines the business.”<sup>3</sup> That means certain questions must be asked and answered. Among them:

- Who exactly is the customer?

- Where is the customer located?
- What does the customer buy and why?
- How does the customer define value?<sup>4</sup>

## Who Exactly Is Your Customer?

Entrepreneur Joe Cossman started selling garden sprinklers—a flexible plastic hose with holes in it—mainly through supermarkets and similar outlets. One day he read that the poultry business used it to inexpensively cool poultry pens during the hot summer months. He immediately redefined his business and opened an entirely new market for his product.

Many businesses don't track their sales or, if they do, they make little use of the information to analyze and define their business, or redefine it if necessary, and to ensure that both the product itself and how it is sold support the definition of their customer.

## Where Is Your Customer Located?

The answer to this question lies primarily in keeping track of sales and the trends associated with them and understanding what they mean. Drucker pointed out that in the 1920s, Sears Roebuck successfully redefined its mission when it identified its customer as the American farmer, and then constructed its catalog—its primary selling tool—according to this definition. Years later (in 1993) Sears quit using the catalog when it saw that the nature of retailing had significantly changed as customers relocated to cities.

It is interesting to note that Aaron Ward at rival Montgomery Ward first introduced the mail order catalog in 1872. It was a single sheet of paper plus a price list. At its height, Montgomery Ward was one of the largest retailers in the country, originally all through the mail. It was said that every farmer owned two books: one was the Holy Bible and the other was the Montgomery Ward catalog. However, times change. Montgomery Ward did not

redefine its business until it was too late, and the original business ceased operations completely in 2001–2002—an important cautionary tale of what can happen when a business doesn’t know who and where its customer is.<sup>5</sup>

### What Does Your Customer Buy and Why?

Some years ago, Falstaff beer, a popular beer in the East, attempted to expand into the lucrative California market. Early attempts failed although blind taste tests confirmed that the brand was exactly what Californians wanted. The error was not in the product but in the advertising, which did not properly promote the *qualities* Californians desired to see associated with their beer.

In the mid-1980s Coca-Cola made a similar and grander mistake on a national level when it attempted to new introduce “New Coke,” as a revolutionary soft drink, in response to “The Pepsi Challenge,” which was slowly eroding Coke’s market. Coke had carefully conducted blind taste tests and formulated a product that was consistently preferred over either its own original product or that of its rival, Pepsi-Cola.

But taste was not why customers bought Coke. Image was. Coke was as much an American icon as mom, apple pie, and John Wayne. Coca-Cola’s previous “Real Thing” campaign resonated with this market. America rebelled in mass against “New Coke” which, to them, was not “the Real Thing.” Eventually Coke surrendered, dubbed old Coke “Classic Coke,” and “New Coke” was quietly withdrawn from the market.

### How Does Your Customer Define Value?

Not all customers define value in the same way. What you think may be valued may not be as important to your customer at all. At the same time, you may ignore what the customer really values.

Steve Jobs did a very good job of defining what his customers valued in computing—so good that he and his partners founded an



industry. But early on he made a glaring mistake in a computer he called “LISA” by not paying attention to what his potential customers valued. Some said the Lisa was named after his daughter of the same name, although Apple said it was an acronym for Local Integrated Software Architecture. The Lisa had many advanced features, including its graphics. However, at a time when the customer valued price, the Lisa sold for almost \$10,000 a shot. Customers flocked to buy—but they bought the competing IBM model, which had less advanced features but was priced much lower. Jobs said customers would buy it anyway despite its high price. They didn’t, and eventually even a less advanced but cheaper model was withdrawn from the market and three thousand machines had to be destroyed. It’s how your customer defines value that is important.

## **When Should You Define Your Business?**

Most leaders never ask this question, or if they do, it is usually only after they get into trouble, and then it is too late. A smart leader will ask this question when the business is formed and periodically thereafter. Waiting until the situation is critical is somewhat like approaching a doctor only when it is too late for a cure. To spot trends and address them before it becomes too late to take advantage of opportunities or avoid threats, it is wise to ask “What business are we in?” once a year formally, and even more frequently informally and on your own.

## **Drucker’s Advice on Defining the Business of the Organization**

- It is a leader’s primary responsibility.
- Organizations that failed to do this until too late litter the terrain.

- Make this decision together with other relevant organizational leaders.
- To analyze the business and get to the right answer, first answer the following questions:
  - Who exactly is the customer?
  - Where is the customer located?
  - What does the customer buy and why?
  - How does the customer define value?