

## Course Learning Outcomes for Unit I

Upon completion of this unit, students should be able to:

1. Summarize the foundational theories of managerial decision-making.
  - 1.1 Explain alternatives for a decision.
  - 1.2 Define System 1 and System 2 thinking.
  - 1.3 Explain the role of boundaries in decision-making.
  
2. Examine the rational decision-making process.
  - 2.1 Discuss the six steps to rational decision-making.
  - 2.2 Explain overconfidence in decision-making.

Course/Unit Learning Outcomes	Learning Activity
1.1	Unit Lesson Chapter 1 Unit I Assessment
1.2	Unit Lesson Chapter 1 Unit I Assessment
1.3	Unit Lesson Chapter 1 Unit I Assessment
2.1	Unit Lesson Chapter 1 Unit I Assessment
2.2	Unit Lesson Chapter 2 Reading: "Dumb Decisions" Unit I Assessment

## Reading Assignment

**Chapter 1:** Introduction to Managerial Decision Making

**Chapter 2:** Overconfidence

*In order to access the following resource, click the link below.*

Mauboussin, M. J. (2010). Dumb decisions. *The Futurist*, 44(2), 24–30. Retrieved from <http://link.galegroup.com/libraryresources.columbiasouthern.edu/apps/doc/A220203543/AONE?u=oran95108&sid=AONE&xid=b19dc26d>

## Unit Lesson

### Introduction to Managerial Decision-Making

This unit introduces decision-making. It provides a definition of the process and explains the role and importance of decision-making in organizations. This unit covers concepts related to System 1 and System 2

thinking, and outlines how boundaries and judgment play a part in decision-making. Chapter 2 within this unit deals specifically with how overconfidence plays a role in decision-making.

People do not intend to make poor decisions. Sometimes, circumstances beyond their control or unforeseen events derail choices made based on the best available information at the time. There are many factors surrounding decisions, however, that leaders and managers do control. Paying attention to how decisions are made has a lot to do with whether the decision makers select the best alternative with the greatest likelihood of success. Decision-making is at the heart of what managers and leaders are supposed to do within their organizations.

Before we go much further, it is important to understand the definitions of System 1 and System 2 thinking. *System 1* thinking relates to a person's intuitive thinking; it is quick, automatic, and emotional. Most of the decisions we make on a day-to-day basis use System 1 thinking. *System 2* thinking is thinking based on logic; it is slower and takes more effort. The logical steps in rational decision-making provide a prototype of System 2 thinking.

Click [here](#) to test your knowledge and put the six steps of the rational decision-making process in the correct order. Be sure that you have reviewed Chapter 1 before taking this quiz.

Our System 1 thinking is adequate in most cases. However, when making a big, important decision, it is preferable to use the more logical System 2 thinking (Bazerman & Moore, 2013).

### **What Is Decision-Making?**

Decision-making is the process of choosing between alternatives to achieve a desired outcome. It is cognitive, meaning it involves thinking, reasoning, and perception. It is also psychological in that it can be influenced by emotion, motivation, preferences, and bias.

Aspects of the situation also influence decisions; for example, some decisions are made under extreme time pressure or involve high degrees of uncertainty because of the lack of available information. Decision-making implies that some action will be taken as a result of the choice made. People sometimes wait for decisions to be made by others before they act.

Decisions must be implemented to have their desired effect. Planning and decision-making are linked because implementation requires identifying what needs to be accomplished, when it will be done, and who will do it. Decision-making involves understanding the substance of the alternatives as well as the factors they encompass such as resources, people, costs, and benefits. For example, imagine that you are a small business owner who has decided to relocate your retail store to a new location. A number of decisions must be made to reach this objective. Where should the new location be? How will you physically move your merchandise from one place to the other? How will you let your customers know where to find you? Each decision involves a different aspect of the relocation and must be considered on its own as a discrete choice.

The process of decision-making is separate from its substantive focus; therefore, how you make a decision can be independent of what the decision entails. A decision may be made by a single individual or by a group. It can involve extensive data collection and analysis, or it can be made more instinctively without much deliberate effort. Organizations typically have formal decision processes that specify who is responsible for making the decision and who is held accountable for its results. As individuals, we often make decisions without being aware that we are following a process, but each of us has developed a way of gathering information and considering alternatives, even if it only involves something as simple as making a list of pros and cons.

In this unit, we introduce rational decision-making but will cover it in depth in Unit VI. The term *rationality* refers to the decision-making process that should lead to the best result, based on an assessment of the decision maker's values and risks that he or she may take. The rational model of decision-making is based on the premise of how a decision should be made instead of how it is actually made (Bazerman & Moore, 2013).

## Categories of Decisions

Everything that happens in an organization is the result of a decision made by someone. Each decision, big and small, contributes in some way to the bottom line. The amount of responsibility and autonomy to make decisions typically varies by level of authority. Some managers make many decisions each day that have a wide impact, while many employees make few decisions that have an effect beyond their own tasks. Decisions made in organizations can be divided into three categories: strategic, tactical, and operational.



The three categories (or levels) of decisions  
(Alvarenga, 2009)

*Strategic decisions* are those related to the organization's reason for being. They determine the direction of the enterprise and how it will achieve its goals. This type of decision represents long-term (typically 1 year or longer) commitments of resources and is not readily changed. Strategic decisions are made by senior executives and boards of directors. Examples include choosing which markets to compete, what products or services to offer the consumer, and what the capital structure will be.

*Tactical decisions* are those that have an impact in the medium-term (typically less than 1 year) and are associated with how strategic decisions will be implemented. These are decisions that mid-level managers make. Examples include choosing the technology that will be used to manufacture a product and selecting channels of distribution. There

is more flexibility around tactical decisions than strategic ones; adjustments can be made more easily when results are poor because tactical decisions represent a less permanent type of investment that does not necessarily preclude making another choice.

*Operational decisions* are day-to-day choices made by line managers and employees that directly support the production and delivery of goods and services. Every business function has processes that require decisions to be made. Human resource departments make hiring decisions, a pharmaceutical research and development lab chooses what experiments to perform, and a fast-food restaurant manager decides whom to schedule for which shift. Operational decisions such as these determine how and when tasks are performed as well as who performs them.

## Evaluating Decisions

We can think of decision-making in terms of *efficiency* and *effectiveness*. We judge the quality of a decision by these characteristics.

*Efficiency* considers how many resources are used in making the decision (e.g., how many people are involved) and how long it takes to reach the decision. Efficiency takes into account inputs and outputs; more consequential or impactful decisions may require more time and resources as it may be wasteful to put the same amount of effort into making a much smaller decision.

The *effectiveness* of a decision describes how likely it is to result in the desired outcome. It is determined by several factors. Key components include the quality and reliability of the information used to identify alternatives and the weight of their advantages and disadvantages. Another component involves assessing the explicitness and the preciseness of the criteria by which the choice will be made. The rigor and logic with which the alternatives are identified and assessed, as well as the ultimate choice that is made, also contribute to decision effectiveness.

The ultimate success of a decision often depends on how well it is implemented. Efficiency and effectiveness do not always go together. An efficient decision-making process may nonetheless lead to an inappropriate or wrong decision. It is possible to reach a decision through an effective and efficient process but to implement it poorly so that it does not achieve its objectives. On the other hand, a decision reached through a lower quality process can be successful through careful attention and diligent effort to translate it into action.



When making a decision, it is always important to consider the effectiveness and efficiency of the decision. (Cunliffe, 2012)

### Judgmental Heuristics and Overconfidence

In this unit, we will also touch on *judgmental heuristics* and *overconfidence*. We now know that people use many simple strategies or practical methods when making decisions; these are called *heuristics*. Heuristics are the rules that help to direct our judgment, and they help us to cope with the implications of our decisions and the environment that surrounds those (Bazerman & Moore, 2013).

There is a whole chapter in the textbook devoted to understanding the effects of *overconfidence* in decision-making. To understand overconfidence, Bazerman and Moore (2013) state, “Overconfidence may be the mother of all biases. We mean this in two ways. First, overconfidence effects are some of the most potent, pervasive, and pernicious of any of the biases we document” (p. 14). They go on to say that overconfidence facilitates many of the other biases discussed in the textbook (Bazerman & Moore, 2013).

In his article “Dumb Decisions,” Mauboussin (2010), another decision-making scholar, summarizes overconfidence by stating that it is the biggest factor in poor decisions. He says that we use our natural decision-making process and that makes us vulnerable to mental mistakes. He gave an example of what psychologists call the *inside view*. This view says that we consider problems by focusing on a specific task, using information readily available, and then making predictions based on a narrow set of inputs. This view is common in planning and usually provides an overly optimistic plan.

As you can see, many things affect decision-making. The more you understand and learn about how decisions are made and what influences them, the easier it will be to make better decisions in the future. The bottom line for this course is to improve your judgment. After studying the textbook and completing all the units in this course, you should be well equipped to use your judgment to make better decisions.

Click [here](#) to complete a short activity and test your knowledge of the terms learned in this unit. Be sure you have reviewed Chapters 1 and 2 before taking this quiz.

### References

Alvarenga, L. (2009). *Decision levels* [Photograph]. Retrieved from [www.dreamstime.com](http://www.dreamstime.com)

Bazerman, M. H., & Moore, D. A. (2013). *Judgment in managerial decision making* (8th ed.). Hoboken, NJ: Wiley.

Cunliffe, L. (2012). *Time is money concept* [Image]. Retrieved from [www.dreamstime.com](http://www.dreamstime.com)

Mauboussin, M. J. (2010). Dumb decisions. *The Futurist*, 44(2), 24–30. Retrieved from <http://link.galegroup.com.libraryresources.columbiasouthern.edu/apps/doc/A220203543/AONE?u=oran95108&sid=AONE&xid=b19dc26d>