**CHAPTER TWO**

### **THE PLANNING FUNCTION**

# I. MEANING, NATURE AND IMPORTANCE OF PLANNING

## The Meaning of Planning

* **Planning** – is the dynamic process of making decisions today about future actions; and it is a selection or choice among alternatives as to: What missions or objectives be achieved, What actions should be taken, What organizational positions be assigned, How the end can be achieved, When to achieve it, Who is to do it, Where to do it. It bridges the gap between where we are now and where we want to be.
* **Planning -** is preparing today for tomorrow; it is the activity that allows managers to determine what they want and how to get it: They set goals and decide how to reach them. Planning focuses on the future: what is to be accomplished and how.

Answers six basic questions in regard to any intended activity:

* + - What (the goal or goals).
		- When (the time frame in which it will be accomplished)
		- Where (the place or places where the plans or planning will reach its conclusion).
		- Who (which people will perform the tasks).
		- How (the specific steps or methods to reach the goals).
		- What resources (resources necessary to reach the goals).
* Planning is a process of deciding what to do and how to do it before action is required.

Planning involves selecting missions and objectives and the actions to achieve to them; it requires decision-making, that is, choosing from among alternative future courses of actions. Managers who develop plans but do not commit themselves to action are simply wasting time. The outcome of the planning function is a plan, a written document that specifies the courses of action a firm will take.

**Nature of Planning**

Discussing the following points can highlight the nature of planning.

1. **The contribution of planning to purpose and objectives**

Every organization is established (exists) for the accomplishment of group purpose or objective. So, the purpose of any plan and its derivatives or supporting plans is to facilitate the accomplishment of organizational objectives.

1. **The primacy of planning**

All the five managerial functions - planning, organizing, staffing, directing and controlling- are designed to support the accomplishment of organizational objectives. However, planning precedes the execution of all other managerial functions, because all other managerial functions must be planned if they are to be effective. This does not mean that planning is the most important of all other managerial functions, because to be important or useful all other functions have to accompany it.

Although in practice all the functions mesh as a system of action, planning is unique in that it involves establishing the objectives necessary for all group effort. The entire gist of initiating, exercising, and activating the managerial functions of organizing, staffing, directing and controlling is to bring the objectives formulated during planning into fruition. In fact, the concept of especially control would be unthinkable without planning because any attempt to control without plans is meaningless, since there is no way for people to tell whether they are going where they want to go (the result of the task of control) unless they first know where they want to go (part of task of planning). Plans thus furnish the standards of control. Since planning and controlling are so much inseparable, they are treated as the Siamese twins of management.

**3. The pervasiveness /Universality of planning**

Planning is a function of all managers, although the character and breadth of planning varies with each manager’s authority and with the nature of policies and plans outlined by superiors. That is, all managers-from presidents to first-level supervisors plan. Even for personal life we plan. “It is difficult to call a person a manager if he or she doesn't plan “Koontz

**4. Planning and information**

Basically no plan exists without information. To plan managers have to gather relevant information from around the environment. Information is one of the valuable resources for planning to exist.

**5. Planning is a continuous process**

Planning deals with the future and the future is full of uncertainties. Hence, planning is subject to revision. It needs frequent revision in response to changes in the internal and external environments of the organization. Therefore, so for as the organization is in operation, planning is in continuous process. The more continuous the planning is, the higher its efficiency is.

**6. Planning is a means to an end**

Planning is not an end by itself. It is a means to an end (meeting objectives). Planning is an instrument that pushes people towards the achievement of objectives.

**7. Plans are arranged in a hierarchy**

Plans are first set for the entire organization. The corporate plan then provides the framework for the formulation of divisional, departmental, and sectional goals. Each of these organizational components sets its plans, programs, projects, budgets, resource requirements, etc.

As shown in the figure below, unit plans are summed up to form sectional plans and these in turn form departmental plans. Finally, the different divisional plans when summarized at corporate level, form corporate plan.

*Fig. Hierarchy of plans*

 Corporate plans

 Departmental/divisional plans

 Sectional plans

Unit plans

**The Importance of Planning**

**1. It provides direction and sense of purpose**

It is through planning that we can establish our objectives. Plans focus attention on sepicifc targets and direct employees effort toward important outcomes. Once organizations known what they can do and can't do over the future, they began to set objectives based on their capacity and the order of activities needed to accomplish their objectives. It provides direction and a common sense of purpose. This shared purpose enables both employees and managers to coordinate, unite, and guide their actions.

**2. It reduces uncertainties and anticipates the future/ preparing for change**

Planning is based on systematic and careful forecasts of future states of the economy, markets, technology, etc to reduce uncertainties to the extent they occur according to expectation. Thus, it is while planning that the manager should consider the potential areas for changes in the future; rather than merely reacting to it. Managers should cope with changes in their own organizations and functions in their environment through planning. Anticipating and preparing for possible future changes enables managers to control their environment. In so doing, planning **answers “what-if” questions.** In planning, managers develop several "what if" questions in order to reduce the risk of unpredictable future, so far as we plan for the future. By asking what if questions managers develop alternatives.

**3. It provides basis for controlling**

Standards /controlling mechanisms/ are developed during planning. It specifies what is to be accomplished and provides a standard for measuring progress.

**4. It forces managers to see the organization as a system**

While planning managers have to consider parts because the plan of one part (department) affects the operation of the whole organization so far as parts of an organization are interdependent

**5. It promotes efficiency**

Planning provides the opportunity for a greater utilization of the available organizational resources - because in planning we determine how many resources are necessary to reach the goals, and how to use these resources.

**6. It provides the base for cooperative and coordinated efforts**

Management exists because the work of individuals and groups in organizations must be coordinated, and planning is one important technique for achieving coordinated effort. Planning provides the basis for organized and coordinated effort by defining the objectives of the organization and the means for their achievement.

**7. Developing managers**

The act of planning involves high level of intellectual activity. Those who plan must be able to deal with abstract and uncertain ideas and information. Planners must think systematically about the present and the future. Through planning, the future state of the organization can be improved if its managers take an active role in moving the organization toward that future. Planning then implies that managers should be proactive and make things happen rather than reactive and let things happen. Through act of planning, managers not only develop their ability to think futuristically but, to the extent that their plans are effective, their motivation to plan is reinforced. Also, the act of planning sharpens manager's ability to think as they consider abstract ideas and possibilities for the future. Thus, both the result and the act of planning benefit both the organization and its managers.

**8. It provides guideline for decision making**

Decisions in an organization will be made in alignment with the plans and in accordance with desired outcomes. Managers make decisions on problems of recurring nature based on strategies and policies of the organization. Through specifying the actions necessary to accomplish the goals of the organization, planning serves as a framework for decision-making. It forces managers to make analytical thinking and evaluate alternatives through improved decisions.

**Limitations of Planning**

1. **Planning is risky**

This is because of uncertainties in the future and absence of accurate and adequate data.

1. **It is a difficult and complicated task**

Planning involves complex and interdependent decisions. Thus requires patience and commitment from those who are involved in the planning process. In addition to this, rapid changes in technology and customers’ tastes and preferences will also make planning difficult and exceptionally complex.

1. **It is expensive and time consuming**

Planning requires financial, physical, human, and time resources. The collection of the necessary data from various sources, the analysis, organizing and interpreting data consume time and requires a huge amount of financial outlay.

1. **It is affected by external factors**

External factors can put strain on the success of planning. These factors could be external impositions, government intervention, natural calamities, import-export policies, taxation and labor laws that can limit the success of planning.

# II. ORGANIZATIONAL OBJECTIVES

* *Objectives* are the important ends of planning toward which organizing, staffing, leading and controlling are aimed.
* *Objectives* are the important ends toward which organizational and individual efforts or activities are directed.
* Objectives are essential starting points in planning because they provide direction for all other managerial activities.
* While enterprise objectives are the basic plan of the firm, department may also have its own objectives. Its objectives naturally contribute to the attainment of enterprise objectives, but the two sets of objectives may be entirely different.

E.g. Objective of Business – To make a certain profit by producing a given line of home entertainment equipment

Objective of manufacturing department - To produce the required number of TV sets of given design and quality at a given cost.

These two objectives are consistent, but they differ in that the manufacturing department alone cannot ensure accomplishing the company’s objectives.

Goals and objectives can be used interchangeably.

* ***Mission/Purpose*** - denotes the reason for the existence of an organization.

 - denotes the organizations fundamental reason for existence.

Purpose and mission can be used interchangeably.

* ***Target*** – identifies specific qualitative or quantitative ends (points).

In short Mission/ purposes, objective, goals/ Targets differ in scope.

 Purpose/missions → objective → Targets/goals

**Nature of Objectives**

1. **Goals are predetermined or stated in advance.**
2. **Goals describe future desired results toward which present efforts are directed.**
3. **Goals should be specific and measurable.** If possible, goals should be expressed in quantitative terms.

**Goals should have defined time period.** They should specify the time period over which goals will be achieved and measured. However, the long-range objectives should provide the direction for short-range objectives. **‹‹ለለውጥ ተግተን እንሰራለን››**

1. **Objectives should be continually adjusted in light of environmental changes**. However, too frequent changes and adjustments may cause confusion and disruption of plans, strategies, policies, budgets, etc.
2. **Goals should be challenging but realistic.** If a goal is too difficult employees may give up. If too easy, and routine type they may not feel motivated. Therefore, goals should be set within the existing resource base and not beyond the department’s time, equipment, labor, and financial resources. This gives workers job satisfaction and a great desire to work hard. A difficult job is something beyond the resource capacity of the organization and the individual employee. It ends up with failure to achieve the stated goals.
3. **Objectives have hierarchy**

 In planning, broader and more comprehensive objective with long time frame will be formulated at the very top. These top-level objectives must successfully be broken down to more specific and shortsighted sub-objectives because moving the organization to goal attainment calls for achieving these sub-objectives which are the means by which objectives are attained. Each level of objective stand as ends relative to the levels below it and as a means relative to the level above it.

In short, like all management activities objectives have hierarchy. It ranges from the broadest organizational objectives to specific /individual objectives. Organizations typically have three levels of goals: strategic, tactical, and operational.

*Strategic goals* - are broadly defined targets or future end results set by top-level management. Such goals typically address issues relating to the organization as a whole rather than specific divisions or departments and may sometimes be stated in fairly general terms. Strategic goals are sometimes called official goals because they are formally stated by top management.

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*Tactical goals* - are targets or future end results usually set by middle management for specific departments or units. Goals at this level spell out what must be done by various departments to achieve the results outlined in the strategic goals. Tactical goals tend to be stated in more measurable terms than is sometimes true of strategic goals.

*Operational goals* - are targets or future end results set by lower management that address specific, measurable outcomes required from lower levels.

The three levels of goals can be thought of as forming a hierarchy of goals. With a hierarchy, goals at each level need to be synchronized so that efforts at the various levels are channeled ultimately toward achieving the major goals of the organization. In this way, the various levels of goals form a means-end chain, in which the goals at the operational level (means) must be achieved in order to reach the goals at the tactical level (end). Likewise, the goals at the tactical level (means) must be reached in order to achieve the goals at the strategic level (end).

1. **Multiplicity of objectives**

Even though there is only one broad and overall organizational objective, there are other multiple (many) objectives that are under the umbrella of the overall plan which are directed to attain the overall plan. It would have been relatively easy to achieve an objective and its sub-objective had an organization had only a single basic objective. But in reality organizations do have a multitude of objectives and any attempt to disregard this fact can invite failure to organizations.

 E.g. Organizational (Broad) objective: profit maximization

Satisfaction of customers

 Other objectives Research & development

Employee development

1. **Integrating character**

In order to achieve the broad organizational objective there should be harmony or integration among objectives.

Multiple → Integration → Network of

Objectives objectives

1. **Network of objectives**

Objectives of an organization form network, that is, objectives are interrelated and interdependent. The union of the individual objectives to form an overall objective makes network of objectives. If there were no network of objectives, it would be very difficult to achieve organizational objectives because people with their individual objective will pursue their activity as right and coordination can never be possible.

1. **Primacy of objectives**

Objectives are primary to organization because they are the very reason for the existence of an organization.

Benefits of Objectives

1. Objectives provide basis for the performance of all managerial functions. They serve as a benchmark for the formulation of plan, policies, strategies, rules, budgets, procedures, etc. Organizing exists when there are objectives and courses of action required for implementing plans, organizing signifies the need for staffing by creating jobs and positions and coordinating all organizational efforts to desired results.
2. Objectives provide guidelines for action. They help clarify expectations. When goals are set, organization members are more likely to have a clear idea of the major outcomes that they are expected to achieve. Without goals, organization members can all be working very hard but may collectively accomplish very little as if they were rowers independently rowing the same boat in different directions and together making very little progress. Goals direct and channel employees’ efforts by describing future desired results. They provide focus and direction for employees by prescribing what ‘should be’ done. And, they also help to allocate resources and tell employee how and where to direct their strongest efforts. Goals are basic for cooperative and organized effort.
3. Objectives can limit employee activities. They serve to prescribe what ‘should be done’ and ‘what should not be done’ by the employees.
4. Objectives provide a unique identity for organizations. Organizations have unique characteristics. They have their own values and identities that help one to differentiate them from others in the industry.
5. An organization’s goal can serve as a source of employee motivation. It helps to uplift their morale. By presenting a challenge, goals tell what characterizes success and how to achieve it. Accomplishment of organizational goals provides employees a sense of achievement and satisfaction. The added motivation develops from meeting goals, feeling a sense of accomplishment, and receiving recognition and other rewards for reaching targeted outcomes. On the other hand, managing employees based on the accomplishment of objectives rather than on the tasks and activities of every worker (management by objectives-MBO) can serve as an incentive to employees.
6. Objectives provide performance standards and bases for control. Control is the function of measuring, comparing and evaluating performance against predetermined standards. Thus, control will be meaningless in the absence of standards provided by objectives.

# *How Goals Facilitate Performance*

In order to make use of goals, managers need to understand just how goals can facilitate performance. Goals facilitate performance if they have the following components: goal content, goal commitment, work behavior, and feedback.

Goal Content: Goals that are effective in channeling effort toward achievement at the strategic, tactical, and operational levels have a content that reflects five major characteristics. Goals should be challenging, attainable, specific and measurable, time limited, and relevant.

Goal commitment:A criticalelement in using goals effectively is getting individualsand/or work groups to be committedto the goals they must carry out. Goal commitment is one's attachment to, or determination to reach, a goal. Without commitment, setting specific, challenging goals will have little impact on performance. Research indicates that five major factors positively influence goal commitment: supervisory authority, peer and group pressure, public display of commitment, expectations of success, and incentives and rewards.

Work Behavior: Given goals and commitment, how does the goal-setting process ultimately influence behavior? Research so far suggests that goal content and goal commitment affect an individual's actual work behavior by influencing four work behavior factors: direction, effort, persistence and planning.

**Direction:** Goals provide direction by channeling attention and action toward activities related to those goals, rather than to other activities. Thus goals to which we are committed can help us make better choices about the activities that we will undertake.

**Effort:** In addition to channeling activities, goals to which we are committed boost effort by mobilizing energy. As indicated by the research on goal setting, individuals are likely to put forth more effort when goals are difficult than when they are easy.

**Persistence:** Persistence involves maintaining direction and effort on behalf of a goal until it is reached, a requirement that may involve an extended period of time. Commitment to goals makes it more likely that we will persist in attempting to reach them.

**Planning:** In addition to the relatively direct efforts on direction, effort and persistence, goals also have an important indirect effect on work behavior by influencing planning. Goal setting affects planning because individuals who have committed themselves to achieving difficult goals are likely to develop plans or methods that can be used to attain those goals. With easy goals, however, little planning may be necessary.

Feedback: feedback to employees as to their performance will let them know if they have worker as to the expectation. By comparing their performance with the set goals, managers should give feedback on employees’ performance that will help them evaluate themselves and direct their effort towards achievement.

# *III. The Planning Process*

Like other managerial activities planning has its own processes or series of steps. These steps are interrelated and there is no rigid boundary between or among these steps, and one is the base for the other.

**1. Establishing objectives**

As objectives provide the direction for all other managerial functions, especially planning, objective setting is an important first step in the planning process. Objectives specify the expected results and indicate the ends of what is to be done, where the primary emphasis is t be placed, and what is to be accomplished by the network of strategies, policies, procedures, rules, budgets, and programs. They provide the direction necessary for achievement and without them there is little to keep a manager from simply wandering in all directions. Objectives are then, the ‘guiding light’ for the entire management process.

Objective setting is a three steps process, which involves assessing the present situation, anticipating future conditions, and then setting the objectives. It is only after the managers have at least the rudimentary knowledge about their capabilities and available opportunities that objective setting does make sense.

Organizations do not have one set of objectives, which each manager attempts to achieve. Rather, setting objectives involves establishing objectives for the entire organization, each subordinate work unit, and the long range as well as the short range. The hierarchy of objectives starts at the top of the organization with overall organizational objectives and proceeds downwards with narrower and more specific objectives for each level managers, derived from the objectives at the level

Objectives developed by organizational levels and peer managers should be compatible with one another. Top-level management should set the stage for goal setting by lower level management, thereby ensuring maximum use of resources. Enterprise objectives give direction to the major plans, which define the objective of every major department. Major department objectives, in turn, control the objectives of subordinate departments and so down the line.

**2. Developing premises**

Planning premises are assumptions about the environment within which the plan is to be carried out. Once objectives are established managers have to investigate the company's environment to know factors that facilitate or block the attainment of these objectives. This involves examining the external and internal factors which affect the performance of the organization: the external environment (for Treats and Opportunities) through PEST analysis and internal environment (for Strengths and Weaknesses) through Self-Audit.

* Strengths are internal competencies possessed by the organization in comparison with the competitors. These include structure and policies of the organization, location, financial soundness, knowledge of personnel, qualities of facilities, and so on.
* Weaknesses are attributes of the organization, which tend to decrease its competence in comparison to its competitors.
* Threat is reasonably probable events, which if it were to occur, would produce significant damage to the organization.
* Opportunity is a combination of circumstances, time, and place, which if accompanied by a certain course of action on the part of the organization, is likely to produce significant benefits.

The key element of planning at this stage is forecasting. It is based on the forecasts made in different areas that premises are made.

Because the future is so complex, it would not be profitable or realistic to make assumptions about every detail of the future environment of a plan. Therefore, premises are, as a practical matter, limited to assumptions that are critical, or strategic, to a plan, that is, those that most influence its operation.

**3. Determining alternative courses of actions**

Alternatives are courses of actions that are available to a manager to reach a goal. In developing alternatives, a manager should try to create as many roads to the objective as possible. Usually the most common problem is not finding alternatives but reducing number of alternatives so that the most promising may be analyzed.

**4. Evaluating alternative courses of action**

Having sought out alternative courses, managers evaluate the benefits, costs and effects of alternative courses in light of their weight to goals and premises. Because there are so many alternative courses in most situations and there are numerous variables and limitations to be considered, evaluation can be exceedingly difficult. This is a step in planning process that operations research and mathematical as well as computing techniques have their primary application to the field of management.

**5. Selecting a course of action**

This is the point at which the plan to be adopted is chosen or selected. It is the real point of decision-making. The analysis of each alternative’s disadvantages, benefits, costs and effects should result in determining one course of action that appears better than the others. If no one alternative emerges as clearly the best, consideration should be given to combining parts or the entire content of two or more alternatives. Whatever the course chosen, it should be one that gives you the most advantages and the fewest serious disadvantages.

**6. Formulating derivative plans**

At step 5 planning is ended. Formulating derivative plans means formulating other plans based on one major plan.

**7. Numberizing plans by budgeting**

Numberizing plans is converting them into budgets. Plans will have meaning when they are changed into numbers. Budgeting is the means of adding various plans together and set important standards against which planning process can be measured.

**8. Implementing the plan**

After the optimum alternative has been selected, the manager needs to develop an action plan to implement it. This is a step where by the entire organization will be in motion or real operation. All the planning in the world will not help an organization realize objectives if plans cannot be implemented. Implementation involves determining who will be involved, what resources will be assigned, how the plan will be evaluated, and the reporting procedure.

**9. Controlling and evaluating the results**

Once the plan is implemented, the manager must monitor the progress that is being made, evaluate the reported results, and make any modifications necessary. The environment that a plan is constructed in is constantly changing, so the plans may have to be modified. Or modification may be needed because a plan was not quite “perfect” when it was implemented. Hence, managers need to make certain that the plan is going according to expectations and making necessary adjustments.

# IV. Types of Plans

Plans can be classified on different bases or dimensions. These are:

* Scope/breadth dimension,
* Time dimension, and
* Use/repetitiveness

**I. Scope/Breadth Dimension**

Scope refers to the comprehensiveness/width of the plan, or it refers to the level of management where plans are formulated. This dimension creates hierarchy of plans. Based on scope/breadth we can classify plans into: Strategic, Tactical and Operational.

**Strategic Plan:** is organization wide plan that is formulated or developed by top-level management in consultation with the board of directors and middle level management.

* It applies to the entire organization.
* Looks ahead over the next two, three, five or more years.
* Develops the direction for the entire organization.
* Is primarily concerned with solving long-term problems associated with external environmental influences.
* *Establishes overall objectives and positions for an organization in terms of its environment.*

The following are distinguishing characteristics of strategic plan.

* 1. *It requires looking outside the organization for threats and opportunities.*
	2. *It requires looking inside the organization for strengths and weaknesses*
	3. *It takes a longer view, i.e. it covers a relatively long time horizon > 5 years.*
	4. *It tends to be top management responsibility, but it reflects a mentality useful at all levels.*
	5. *It is expressed in relatively general non-specific terms.*

Strategic plans address such questions as:

* What business are we in?
* What business should we be in?
* Where will we be in ten years if we continue doing what we are now doing?

*The difference between firms would like to be (where we want to be) and where it will be if it does nothing is called the* ***Planning gap.***Strategic planning is primarily concerned with closing that gap.

* The success or failure of an organization depends up on the success or failure of strategic plans. It makes premises/location for tactical plans.

**Tactical Plan:** refers *to the implementation of activities and the allocation of resources necessary for the achievement of the organization’s objectives.*

- is an intermediate plan that helps to reduce long range planning into intermediate one by increasing the amount of specificity and making the actions goal oriented. Tactical plans are specific and more goal oriented than strategic plans. Middle level management in consultation with lower level management develops them.

* Tactical plans are the means charted to support the implementation of the strategic plans and achievement of tactical goals. They are concerned with shorter time frames and cover a narrower scope (narrower range of activities).
* Structures a firm’s resources to achieve maximum performance.
* Concerned with what the lower level units within each division must do, how they must do it, and who will have the responsibilities for doing it.
* Tactical plans make premises for operational plans.
* is narrower in scope than strategic plan and wider than operation plan; but more detailed than strategic plan and less detailed than operational plan

E.g. what is the best pricing policy?

 Which city or town is suitable for marketing our products?

**Operational Plan: i**s concerned with the day-to-day activities of the organization and is made at the lower level management in consultation with middle level management. Operational plans *spell out specifically what must be accomplished to achieve specific/operational goals. It is concerned with the efficient, day-to-day use of resources allocated to a department manager’s area of responsibility.*

- Operational plans have relatively short time frame (< 1 yr). It is the most detailed (more specific) and narrowest plan compared to the above two; because it is to be implemented day-to-day.

 E.g. –What production technique is best?

* What materials are needed for operation?
* *Unless operational goals are achieved in organizations, tactical and strategic plans will not be successful and goals at those levels will not be achieved.*

**II. Time Dimension**

Time dimension refers *to the periods for which the planning is intended.* Based on the length of time a plan covers, we do have three types of plans: Long-range (five years or more), medium-range (between one and five years) and short-range plans (one year or less).

* *Time dimension and scope dimension are the same except the former is about the length of time that the plan covers and the later about the level of management where the plan is formulated.*

 All strategic plans are long-range plans.

All tactical plans are medium-range plans.

All operational plans are short-range plans.

**III. Use Dimension**

Use dimension refers *to the extent to which plans will be used on a recurring basis*, i.e. based on how repeatedly/frequently a given plan is used. Based on this dimension we do have two types of plans: standing plans and single use plans.

**Standing Plans:** are plans that provide an ongoing guidance for performing recurring activities.

* They are plans, which are formulated to be used again and again for the day-to-day operation of the organization. That is, repetitive situations or actions require the development of such plans. They become necessary when the same kinds of actions are to be taken repeatedly. Standing plans become valuable under relatively stable situations.

Once established, standing plans allow managers to conserve time used for planning and decision-making because similar situations are handled in a predetermined, consistent manner.

E.g. A bank can more easily approve or reject loan requests if criteria are established in advance to evaluate credit ratings, collateral assets, and related applicant information.

The major types of standing plans are policies, rules, and procedures.

**a. Policies:** is a general guide that specifies the broad parameters within which organization members are expected to operate in pursuit of organizational goals.

* Policies are general statements or understandings which guide or channel thinking and actions in decision-making to achieve organizational objectives.

Not all policies are “statements”, they are often merely implied from the actions of managers.

 **Policies have the following characteristics:**

1. Policies define an area within which a decision is to be made and ensure that the decision will be consistent with and contribute to an objective.
2. Policies help to decide issues before they become problems; make it unnecessary to analyze the same situation every time it comes up and unify other plans.
3. Policies tell us what to do in a general sort of way.
4. Policies provide discretion within limits since they are guides to decision-making. Policy is a means of encouraging discretion and initiative, but within limits. The amount of freedom will naturally depend up on the policy and in turn will reflect position and authority in the organization.
5. Policies must be flexible.
* Policies are usually established formally and deliberately by top managers of the organization. They can also emerge informally and at lower levels in the organization from a seemingly consistent set of decisions on the same subject made over a period.

Policies are established at the top because:

1. They feel it will improve the effectiveness of an organization.
2. They want some aspect of the organization to reflect their personal values (E.g. Dress codes)
3. They need to clear up some conflict or confusion that has occurred at a lower level in the organization.

Examples of policy:

* 1. Except for token gifts of purely nominal or advertising value, no employee shall accept any gift from any supplier at any time.
	2. Hiring university trained engineers
	3. To promote from within
	4. We accept returned merchandise

**b. Rules:** spell out specific required action or non-actions, i.e., actions that must be or must not be taken, allowing no discretion, in a given situation.

E.g. No smoking, cheating is prohibited.

* A rule is an ongoing, specific plan for controlling human behavior and conduct at work.
* The purpose of policies is to guide decision-making by marking off areas in which managers can use their discretion. Although rules also serve as guides, they allow no discretion in their application.
* Rules are the most explicit of standing plans and are not guides for thinking or decision-making. Rather, they are substitutes for them. The only choice a rule leaves is whether or not to apply it to a particular set of circumstances.

**c. Procedures:** are statements that detail the exact manner in which certain activities must be accomplished. They put the precise order of activities to be carried out to do a task and thus, procedures are chronological sequences of required actions. They provide detailed step-by-step instructions as to what should be done. Procedures prescribe exactly what actions are to be taken in a specific situation and specify the chronological sequence of activities. For example, material procurement, university admission, bidding, etc.

When we compare the above three, policies, procedures and rules, we can understand that all are alike in the sense that they are directives to guide people’s behavior to the desired ends and they are plans which are to be followed in the future. Conversely, procedures and rules are different from policies in that the formers are guides to actions while the latter are guides to thinking. So, procedures and rules render no freedom and hence should be used when we want to discourage initiative or repress thinking. But, policies must permit freedom within limits and hence are used when people’s involvement, participation or initiative is desired.

Though both rules and procedures repress thinking, they are different. Unlike procedures, rules (1) guide actions without specifying a time sequence (2) spell out that a certain action must or must not be taken. Procedures, however, specify a time sequence. In fact a procedure may be looked upon as a sequence of rules. A rule, however, may or may not be part of a procedure.

**Single use plans:** are plans aimed at achieving a specific goal that, once reached, will most likely not recur in the future and dissolved when these have been accomplished.

* + - Are designed to accomplish a specific objective usually in a relatively shorter period of time and it is non repetitive.
		- They are detailed courses of action that probably will not be repeated in the same form in the future.

 The major types of single use plans are programs, projects, and budgets.

 E.g. A firm planning to build a new warehouse-location, construction costs, labor availability, zoning restrictions.

**a. Programs:** is a comprehensive plan that coordinates a complex set of activities related to a major non-recurring goal.

* Are a complex of goals, policies, procedures, rules, task assignments, steps to be taken, resources to be employed and other elements necessary to carryout a given course of action
* Single use plans may use standing plans and other single use plans to be effective.

 Single use plan = Standing plans + Single use plans

* A program may be as large in scope as placing a person on the moon or as comparatively small as improving the reading level of fourth grade students in a school district. Whatever its scope, it will specify many activities and allocations of resources within an overall scheme that may include such other single use plans as projects and budgets.

**\*** A program may be repeated with modification but not as it is.

**b. Projects:** is a plan that coordinates a set of limited scope activities that do not need to be divided into several major projects in order to reach a major non-recurring goal.

* + - Projects are the smaller and separate portions of programs. Each project has limited scope and distinct directives concerning assignments and time. Each project will become the responsibility of designated personnel who will be given specific resources and deadlines.

E.g. Building a warehouse can be taken as a program. In the warehouse example, typical projects might include the preparation of layout drawings, a report on labor availability, and recommendations for transferring stock from existing facilities to the new installation.

**c. Budgets:** are statements of expected results expressed in numerical terms.

* Are statements of financial resources set aside for specific activities in a given period of time.

- Budget is a single use plan that commits resources to an activity over a given period. It may be expressed in Birr, labor hours, units of product, machine hrs, or any other numerically measurable term.

* It may be referred to as a “numberize” program.

Budgets are also control devices. However, making a budget is clearly planning.

Characteristics of a Good Plan

Every sound business plan must have these characteristics:

* **Objectivity**

Planning should, first of all, be based on objective thinking. It should be factual, logicaland realistic. It should be directed to achieving organizational goals rather than personal objectives.

* **Futurity**

Since a plan is a forecast of some future action, it must have the quality of futurity; otherwise, it has little value as a basis for future action. If a plan is to be effective, it must foresee with reasonable accuracy the nature of future events affecting the industry and the firm. The inability to foresee future events, a human limitation that we cannot overcome, is the weak link in planning process.

* **Flexibility**

Because no one can foresee the future, plans must have flexibility. They must adjust smoothly and quickly to changing conditions without seriously losing their effectiveness. The more difficult it is to predict the future, the more flexible the plans must be.

* **Stability**

Stability is related to flexibility. A stable plan will not have to be abandoned because of long-term changes in the company’s situation. It may be affected by long-range developments, but it should not be changed materially from day to day.

* **Comprehensive**

A plan must be comprehensive enough to provide adequate guidance, but not so detailed as to be unduly restrictive. It should cover everything required of people, but not in such detail that it inhibits initiative.

* **Simplicity and clarity**

Although a good plan must be comprehensive, it should also be simple. A simple plan seeks to attain its objective with the fewest components, forces, effects and relationships. A plan should not be ambiguous. Lack of clarity makes understanding and implementation difficult.

* **Contingency planning** is the development of alternative plans for use in the event that environmental conditions evolve differently than anticipated, rendering original plans unwise or unfeasible.
* **Planning staff-** is a small group of individuals who assist top-level managers in developing the various components of the planning process.

**Skills Required In Planning**

Skills required in planning are

*(i) Forecasting*

*(ii) Decision Making*

1. **Forecasting:** is the attempt to predict outcomes and future trends that can serve as basis for planning, by inferences from known facts. By relating the past and the present information or data, management should be able to anticipate the future environment.

In developing premises, the kind of markets, volume of sales, prices, products, technical developments, costs, tax rates, policies, policies related to dividends, the social and political environment, long-term trends, etc of the future should be predicted with the help of forecasting.

Effective planning is made with the help of forecasting because planning itself is a future oriented course of action. Accordingly, we have to assess the dynamism of both the internal and external environment. When managers assess the alternatives, they try to forecast how events both within and outside the organization will affect each alternative and what the outcome of each will be.

**Forecasting Methods**

We can use both qualitative & quantitative forecasting methods to predict future situations.

**Qualitative Forecasting: -** it is a judgment-based forecasting technique used when hard data are scarce or difficult to use. It is appropriate when hard data are scarce or difficult to use. It thus involves the use of subjective judgments and rating schemes to transform qualitative information into quantitative estimates. Example includes the jury of executive opinion, market research and the survey of expert opinion.

**Quantitative Forecasting**: - It is a technique used when enough hard data exist to specify relationships between variables. It is used when there is sufficient "hard" or statistical data to specify relationships between key variables. Extrapolation forecasting, such as time-series analysis, uses past or current trends to project future events. Sales records of the past several years, for example, could be used to extend the sales pattern into the coming year. It disregards political considerations, action of competitors, technological changes. It merely depends on the past and current trends.

Quantitative forecasting can be used if information exists about the past, if information exists about the present, if information exists about the present, if this information can be specified numerically and if it can be assumed that the pattern of the past will continue. To the contrary, inputs to qualitative forecasts are mainly the results of intuitive thinking, judgment, and accumulated knowledge. However, it is believed that quantitative techniques are generally more accurate than qualitative ones. To conclude, our forecasting should be accurate, up to date, applicable and less costly as much as possible.

**ii Managerial decision making**

**Meaning:**

* Decision-making is a rational choice or selection of one alternative from among a set of alternatives; i.e. it is the act of choosing one alternative from among a set of alternatives.
* Decision-making is the management function that consists of choosing one course of action from all the available alternatives.

Decision-making is part of every aspect of the manager’s duties, which include planning, organizing, staffing, leading and controlling, i.e. decision-making is universal. In all managerial functions decision-making is involved. All managerial functions have to be decided. For example, managers can formulate planning objectives only after making decisions about the organization’s basic mission. Even though in all managerial functions decision-making is involved, the critical decision-making is during planning because planning identifies the objectives of the organization; i.e. decision must be made to identify the objectives/missions of an organization. In the planning process, managers decide such matters as what goals or opportunities their organization will pursue, what resources will be used, who will perform each required task etc. The entire planning process involves managers in a continual series of decision-making situations.

**Decision-making has three elements (parts)**

1. When managers make decisions; they are choosing or selecting from among alternatives.
2. When managers make decisions, they have available alternatives. When there are no alternatives, there is no decision-making, rather it become mandatory.
3. When managers make decisions, they have purpose in mind. The purpose in mind is organizational objectives.

**THE DECISION-MAKING PROCESS**

Decisions are organizational responses to problems. Every decision is the outcome of a dynamic process that is influenced by multitude of forces. So decision-making has its own processes / series of steps. The process is a sequential process rather then a series of steps.

**1. Identifying problems**

A necessary condition for a decision to exist is a problem - the discrepancy between an actual and desired state; a gap between where one is and where one wants to be. If problems do not exist, there will be no need for decisions; i.e. problems are prerequisites for decisions. How critical a problem for the organization is measured by the gap between levels of performance specified in the organization’s goals and objectives and the level of performance attained; i.e. it is measured by the gap between level of performance specified (standards set) and level of performance attained. The problem is very critical when the gap between the standard set and actual performance attained is very high. To locate problems, managers rely on several different indicators:

* Deviations from past performance. A sudden change in some established pattern of performance often indicates that a problem has developed. When employee turnover increases, sales decline, selling expenses increase, or more defective units are produced, a problem usually exists.
* Deviation from plan. When results do not meet planned objectives, a problem is likely. For example, a new product fails to meet its market share objective, profit levels are lower than planned, the production department is exceeding its budgets. These occurrences signal that some plan is off course.
* Out side criticism. The actions of outsiders may indicate problems. Customers may be dissatisfied with a new product or with their delivery schedules; a labor union may present a grievance; investment firms may not recommend the organization as a good investment opportunity; alumni may withdraw their support from an athletic program.

**Decision makers face three types of problems:**

* A crisis problem is a serious difficulty requiring immediate action. An example of a crisis is a severe cash flow deficiency that has a high potential of evolving into serious losses, and a customer protest against the quality of a product.
* A non-crisis problem is an issue that requires resolutions but does not simultaneously have the importance and immediacy characteristics of a crisis. Many of the decisions that managers make center on non-crisis problems. Example of such problems is a factory that needs to be brought into conformity with new state antipollution standards during the next three years and an employee who frequently is late for work.
* An opportunity problem is a situation that offers strong potential for significant organizational gain if appropriate actions are taken. Opportunities typically involve new ideas and novel directions that could be used, rather than difficulties that must be resolved. Non-innovative managers tend to focus on problems rather than opportunities.

Confusions are common in problem definition because the events or issues that attract the manager’s attention may be symptoms of another more fundamental and pervasive difficulty than the problem itself. That is, there may exist confusion on the identification of a problem and its symptoms. The accurate definition of a problem affects all the steps that follow. Managers once they have identified problems, they have to try to diagnose the cause of the problem. Causes unlike symptoms are seldom apparent.

This step has three general stages: scanning, categorization, and diagnosis.

**Scanning stage :-** involves monitoring the work situation for changing circumstances that may signal the emergence of a problem. At this point the manager may be only vaguely aware that an environmental change could lead to a problem or that an existing situation constitutes a problem.

**Categorization stage :-** entailsattempting to understand and verify signs that there is some type of discrepancy between the current state and the desired state. At this point the manager attempts to categorize the situation as a problem and a no problem, even though it may be difficult to specify the exact nature of the problem, if one exists.

**Diagnosis stage : -** involves gathering additional information and specifying both the nature and the causes of the problem. Without appropriate diagnosis, it is difficult to experience success in the rest of the decision-making process. At the diagnosis stage, the problem should be stated in terms of the discrepancy between current conditions and what is desired; the cause of the discrepancy should be specified.

**2. Developing Alternatives**

Before a decision is made feasible alternatives should be developed. This is a search process in which relevant internal and external environment of the organization are investigated to provide information that can be developed into possible alternatives. At this point it is necessary to list as many possible alternatives solutions to the problem as you can. No major decision should be made until several alternative solutions have been developed. Decision-making at this stage requires finding creative and imaginative alternatives using full mental faculty. The manager needs help in this situation through brainstorming or Delphi technique.

**3. Evaluating Alternatives**

Once managers have developed a set of alternatives, they must evaluate them to see how effective each would be. Each alternative must be judged in light of the goals and resources of the organization and how well the alternative will help solve the problem. In addition, each alternative must be judged in terms of its consequences for the organization. Will any problems arise when a particular course of action is followed? Such factors as worker’s willingness…

**4. Choosing an Alternative**

Based on the evaluation made managers select the best alternative. In trying to select an alternative or combination of alternatives, managers find a solution that appears to offer the fewest serious disadvantages and the most advantages. The purpose of selecting an alternative is to solve the problem so as to achieve a predetermined objective. Managers should take care not to solve one problem and create another with their choice.

A decision is not an end by itself but only a means to an end. This means the factors that lead to implementation and follow –up should follow solution selection.

**5. Implementing and Monitoring the Chosen Solution**

For the entire decision-making process to be successful, considerable thought must be given to implementing and monitoring the chosen solution. It is possible to make a "good' decision in terms of the first five steps and still have the process fail because of difficulties at this final step.

**Implementing the Solution:** A decision that is not implemented is little more than an abstraction. In other words, any decision must be effectively implemented to achieve the objectives for which it was made. Implementing a decision involves more than giving orders. Resources must be acquired and allocated. Decisions are not ends by themselves they are means to an end; so proper implementation is necessary to achieve that end.

**Monitoring the solution:** Monitoring is necessary to ensure that things are progressing as planned and that the problem that triggered the decision process has been resolved. Effective management involves periodic measurements of results. Actual results are compared with planned results (the objective); if deviations exist, changes must be made. Here again we see the importance of measurable objectives. If such objectives do not exist, then there is no way to judge performance. If actual results do not much planned results, then the changes must be made in the solution chosen, in its implementation, or in the original objective if it deemed unattainable. The various actions taken to implement a decision must be monitored. The more important the problem, the greater the effort that needs to be expended on appropriate follow up mechanisms. Are things working according to plan? What is happening in the internal and external environments as a result of the decision? Are subordinates performing according to expectations? ……. must be closely monitored.

**Decision-Making Conditions**

When managers make decisions, the amount of information available to them or the degree of knowledge they have about the likelihood of the occurrence of each alternative vary from managers to managers or/and from situation to situation. To put it in other way, decisions are made under three basic conditions. These are condition of certainty, condition of risk, and condition of uncertainty.

1. **Decision-making under Certainty**

When managers know with certainty what their alternatives are and what conditions are associated with each alternative, a state of certainty exists. Decisions under certainty are those in which the external conditions are identified and very predictable; i.e. we are reasonably sure what will happen when we make a decision. The information is available and is considered to be reliable, and we know the cause and effect relationships. In decision-making under certainty there is a little ambiguity and relatively low chance of making poor/bad decisions. Decision-making under certainty seldom occurs, however, because external conditions seldom are perfectly predictable and because it is impossible to try to account for all possible influences on any given outcome it is very rare.

1. **Decision-making under Risk**

A more common decision-making situation is under risk. Under the state of risk, the availability of each alternative, the likelihood of its occurrence and its potential payoffs and costs are associated with probability estimates; i.e. decisions under risk are those in which probabilities can be assigned to the expected outcomes of each alternative. In a risk situation, managers may have factual information, but it may be incomplete. There is moderate ambiguity and moderate chance of making bad decision.

 E.g. tossing a coin, metrology

1. **Decision-making under Uncertainty**

Under this condition the decision maker does not know what all the alternatives are, what the probability of each will occur is or what consequences each is likely to have. This uncertainty comes from the dynamism of contemporary organizations and their environment. Big multi-national corporations assume these kinds of decisions. Decision-making under uncertainty is the most ambiguous and there is high chance of making poor decisions. In decision-making under uncertainty, probabilities cannot be assigned to surrounding conditions such as competition, government regulations, technological advances, the over all economy, etc. Uncertainty is associated with the consequences of alternatives, not the alternatives themselves. The decision-making is like being a pioneer. Reliance on experience, judgment, and other people's experiences can assist the manager is assessing the value of alternatives.

E.g. Innovation of new machine, journey of discoverers.

**Types of Decisions**

Decisions can be classified in to: programmed and non programmed.

* 1. **Programmed Decisions**

Programmed decisions are those made in routine, repetitive, well-structured situations through the use of predetermined decision rules. The decision rules may be based on habit, computational techniques, or established policies and procedures. Such rules usually stem from prior experience or technical knowledge about what works in the particular type of situation. Most of the decisions made by first line managers and many of those made by middle managers are the programmed type, but very few of the decisions made by top-level managers are the programmed type. Managers can usually handle programmed decisions through rules, procedures, and policies.

**E.g.** Establishing a re-order point, Decide if students meet graduation requirements, Determination of employee pay rates

* 1. **Non-programmed Decisions**

Non-programmed decisions are used to solve non-recurring, novel, and unstructured problems. No well-established procedure exists for handling them, because it has not occurred before managers do not have experience to draw up on, or problems are complex or completely new. Because of their nature non-programmed decisions usually involve significant amounts of uncertainty. They are treated through farsightedness. Most of the highly significant decisions that managers make fall into the non-programmed category. Non-programmed decisions are commonly found at the middle and top levels of management and are often related to an organization’s policy-making activities.

**E.g.** To add a product to the existing product line, to reorganize a company, to acquire another firm

 ***Types of Managerial Decisions***

|  |  |  |  |
| --- | --- | --- | --- |
| Type of decisions | Type of problem | Procedures  | Examples  |
| Programmed  | Repetitive, routine | Rules, standard operating procedures, policies  | Business: processing payroll vouchersCollege: processing admission applicantsHospital: preparing patient for surgery.Government: using state owned motor vehicle. |
| Non-programmed | Complex, novel | Creative problem solving | Business: introducing a new product.College: constructing new classroom facilitiesHospital: reacting to regional disease epidemicGovernment: solving spiraling inflation problem |

In reality most decisions fall between the two; i.e. a continuum of decision situations exists ranging from those that are highly structured to those that are unstructured. Situations between the two extremes are partially structured. As the name suggests, in a partially structured situation, only a part is well structured. Typically, although the manager has a great deal of data available, the final choice is not obvious. Many intangibles are involved in the final choice. Therefore, the manager must base the ultimate decision on the data and supplementary factors, using judgment and experience.

E.g. A hospital wishing to improve patient care may adjust its patient-staff ratio (programmable situation), reorganize its staff (a non programmable situation).

**Continuum of Decision situations**

WELL STRUCTURED PARTIALLY ILL-STRUCTURED

 (PROGRAMMED) STRUCTURED (NON PROGRAMMED)

1. Specification of 1. Only a part of 1. Decision procedure

 decision procedure decision process can not be completely

 agreed in advance can be completely structured in advance

 of resolution. specified and of resolution.

 structured.

2. Little managerial 2. Manager makes 2. Individuals resolve

 involvement at time final resolution each situation on the

 of each resolution from structured basis of experience

 portion of his/her and judgment.

 experience and from

 intuition.

3. Repeated resolutions 3. Different managers may 3. Different managers may

 with same data yield agree on certain data reach different conclusions.

 same results.

**Why Do Managers Make Poor Decisions?**

All managers recognize the importance of making sound decisions. Yet most managers readily admit having made poor decisions that hurt their company or their own effectiveness. Why do managers make mistakes? Why don’t decision always result in achieving some desired goal? Making the wrong decision can result from any one of these decision-making errors:

* **Lack of adequate time**

Waiting until the last minute to make a decision often prevents considering all alternatives. It also hampers thorough analyses of the alternatives.

* **Failure to define goals**

Objectives cannot be attained unless they are clearly defined. They should be explicitly stated so that the manager can see the relationship between a decision and a desired result.

* **Using unreliable sources of information**

A decision is only as good as the information on which it is based. Poor sources of information always result in poor decisions.

* **Fear of consequences**

Managers often are reluctant to make bold, comprehensive decisions because they fear disastrous results. A “play it safe” attitude sometimes limits a manager’s effectiveness.

* **Focusing on symptoms rather than causes**

Addressing the symptoms of a problem will not solve it. Taking aspirin for a toothache may provide temporary relief, but if an abscess causes the pain, the problem will persist. Business managers too often foul on the results of problems instead of the causes.

* **Reliance on Hunch and Intuition**

Intuition, judgment and ‘feel’ are important assets to the decision maker. But a manager who permits intuition to outweigh scientific evidence is likely to make a poor decision.

Sometimes a manager’s decision is not exactly “poor”, but it still doesn’t produce optimal results. Less than optimal decisions can have three causes:

1. **Bounded rationality** imposes limits on a decision, such as that it should be economical or logistically practical. This limit serves as a screening device, eliminating some of the alternatives. The manager must choose from the options that have filtered through the restrictions. The overall optimal decision may no longer be a valid option when using this method. The decision maker simply selects the best alternative, given various specifications that must be met.
2. **Sub optimization** is a manager’s tendency to operate solely in the interests of his/her department rather than in the interests of the company as a whole. In making a decision, the department manager cannot be so self-centered as to ignore the effects of the action on other areas. The key is to improve the company’s performance, not just the performance of one department.
3. **Unforeseen changes in the business environment** also cause less than optimal decisions.