No matter how carefully managers plan, there is always the chance of failure. Moreover, managers often make matters worse by persisting with failing ventures and end up throwing good money after bad – a phenomenon known as escalation. But there are simple ways to avoid it.

Almost all decisions involving uncertainty have some unintended consequences. Sometimes, however, the results are the very opposite of what was hoped for.

When it becomes obvious that a venture is failing managers may be faced with a choice between cutting their losses or persisting, in the hope of eventually succeeding though at the risk of making matters worse. History is rich in examples of managers choosing to carry on to the bitter end. For example, US film studio United Artists continued making *Heaven’s Gate* even though it knew that the venture might put the studio out of business – as indeed it did. Barings continued posting millions of pounds in collateral to support Nick Leeson’s trading even though the financial markets in the Far East were ablaze with rumours suggesting that Barings was close to collapse.

Why do experienced and sophisticated managers behave in such an apparently irrational way? The issue is important because although market forces eventually curb non-viable ventures they are frequently slow to act. By the time such forces play themselves out the damage is usually well and truly done. Meanwhile organisations may incur needless losses that are ultimately passed on to society in higher prices, diminished pension funds and other losses.

**Bright promises**

Part of the problem is that we know a lot more about how to galvanise organisations into action than we do about how to stop them if they start to move in the wrong direction. That said, research by social scientists offers some clues.

For example, the most dangerous time in a new venture is usually at an early stage. These are dangerous because enthusiasm and confidence tend to be high. It is a time when almost anything appears possible and when ventures can appear more important than they really are. It is also a time when decisions are taken that subsequently return to haunt the takers. United Artists, for example, was ecstatic when it succeeded in contracting the hugely successful Michael Cimino to produce *Heaven’s Gate*.

Believing that they could not fail with Cimino in charge, United Artists agreed to all his conditions, including complete artistic freedom, absolute control over the making of the film and other onerous terms.
Technically, a decision fails if expectations are not met. In order to gain support a prospective venture has to promise much. The trouble is that managers frequently create problems for themselves by promising too much at the outset only to discover that they are unable to deliver. Eurotunnel, for example, assured prospective investors that constructing the Channel tunnel would be a fairly easy task and even if there were problems the venture would still yield fabulous profits.

In theory, managers can protect themselves against making rash promises by taking an analytical approach to decision making. In practice, planning can actually produce myopic vision.

Planning involves envisaging something that does not yet exist. It is basically dreaming with discipline. What can happen is that the plans are made to fit the dream. Estimates of costs are pared down, projected revenues are scaled up and time scales shortened until the venture makes economic sense.

For example, when planners say that Manchester’s new tramline extension will carry 45 million passengers a year, how do they know? What they really mean is that it had better carry that number of passengers if the venture is to be financially viable. What is really frightening, however, is that decisions can be authorised even though the figures are absurd. For example, the attendance estimates for the Canadian Expo 86 trade fair assumed that every man, woman and child in Canada would visit the fair at least once.

All is human

It is easy to say we would never allow such things to happen. But research suggests that as human beings we are more sensitive to the relative magnitude of change than the absolute magnitude. This means that managers can easily lose sight of the totality of tinkering and fine tuning that may lie behind best-laid plans. In addition, research suggests that the very existence of a plan (especially if it is supported with copious information) can make managers overconfident. Indeed, business plans can be made to sound so convincing that it is easy to forget that they are only guesswork.

Few things are achieved without will and determination. Yet we can become so obsessed in the pursuit of an ambition that it becomes an obsession. Although the cliché states that something is worth what someone is willing to pay for it, that does not always turn out to be true.

The auction of the UK’s third-generation (3G) mobile phone licenses may turn out to be a case in point. Analysts forecast that the winning contenders might end up paying as much as £3bn. In fact, the auction raised over £20bn, the real winner being the government. The Financial Times called it “the most expensive poker game in history” and “a gamble of heroic proportions” by companies desperate for additional spectrum but which “were bidding without knowing what the services will look like, or how many people will be prepared to pay a premium for them. In effect, they are buying an option that may never come into the money”.

Perceived need may not have been the only factor fuelling an auction. Our determination to succeed is not always driven by reason. To illustrate the point to MBA students I sometimes auction a textbook that will be useful to them on the course. There is no reserve price on the book so in theory an impecunious student could acquire it for as little as 1p compared with a cover price of £20. There is a catch, however, in that the second-highest bidder must also pay the bid price. Students typically start bidding and racking up the stakes for fun but inevitably two parties become trapped in an ascending spiral. The book almost always sells for at least double the cover price though bids of £70 (with £50 as the second-highest bid) have been achieved. When students are questioned afterwards about what drives them to make such extravagant bids, they frequently report that they would rather pay money than lose face.

Just how many dangerous price wars between newspapers, airlines and supermarkets have been perpetuated for the same reason? Did Motorola really say it would rather throw its prestigious Startac telephones in the dustbin than bring the price down to a level that ordinary consumers could afford?

Research suggests that our unwillingness to appear foolish in front of other people in scenarios like the book auction may mean that bidding becomes driven by the desire for revenge. When someone humiliates us they damage our self-esteem. Revenge is sweet because it restores it. Since self-esteem may be worth more than money, no price may be too high if it enables
us to achieve restoration. Business is by nature competitive and competition creates winners and losers. Just how many ill-advised mergers and acquisitions, for example, have actually been motivated by a desire for revenge?

**The rutted road of reality**

The reckoning comes when plans and reality meet. The sequence is like a medieval cart piled high with pottery setting out along a rutted road. The result may be a chain reaction as one bad decision forces another.

The London Stock Exchange learned this lesson when it agreed with the financial establishment’s demand that Project Taurus, an £80m computer system aimed at enabling paperless share trading, would be completed in 18 months – a ridiculously ambitious time scale for such a huge infrastructure project.

Having committed itself, the Stock Exchange then decided that the only way to meet the deadline was to buy a software package known as Vista to drive the system. Vista is a good package but it was never designed for the uniquely complex UK stock market. A rule of thumb in software engineering is that if alterations to a package are likely to exceed 50 per cent it is better to build from scratch. Once it had started on the task, however, there was no question of abandoning the Vista package despite the near insuperable difficulties of adapting it. The budget for re-engineering Vista was £4m. When the Stock Exchange cancelled the project three years later the cost had risen to over three times that and the task was still far from complete.

It is not the inevitable breakages that do the damage, however, so much as managers’ slowness to acknowledge failure – especially if they are liable to be held personally responsible for it. Instead they tend to go into denial, seizing on any information that seems to support their preconceived views, even if it means clutching at straws, while downplaying or even ignoring potentially ominous news. Since this process occurs unconsciously managers can end up living in a fool’s paradise while matters go from bad to worse. Managers may even develop a “bunker mentality”, cutting themselves off mentally and physically. In consequence they soon lose sight of reality altogether – just as Hitler retreated to his bunker only to end up issuing orders to an army and air force that no longer existed.

Money sunk and lost

Experiments by psychologists have shown that people may go to extraordinary lengths to avoid loss – even if it means behaving recklessly. To be more precise, research has shown that faced with a choice between accepting a definite loss and the possibility of incurring a much greater loss later on, we tend to become risk seeking. To be risk seeking is taking a bigger gamble than objective conditions warrant – like betting on a “long shot”. Interestingly, most betting on long shots takes place during the last race as race-goers try to recoup earlier losses. By definition, gambling against heavy odds seldom pays off.

Taurus could have been was cancelled 18 months earlier. The Stock Exchange and, indeed, the financial community had so much invested in the project however that they decided to press on despite deepening unease only to compound the waste of time and money. Likewise, officials’ unwillingness to slaughter a few thousand cattle as a precaution when BSE was first diagnosed in the UK a few years ago led to the destruction of millions of healthy cattle later on.

The experience of loss can affect us in other ways. Research by psychologists suggests that loss has more impact that gain. For example, the pain of losing a £20 note is much greater than the pleasure experienced in finding the same amount. In the context of business strategy, managers may react irrationally to losing market share or part of the business by engaging in an all-out effort to win it back. It is not the initial loss
that does the damage but the opportunity cost of expending resources in a futile quest.

It is not only monetary loss that we dislike. Flagship ventures can absorb huge resources and create huge opportunity costs for little strategic value. Yet organisations cling to them, fearing the loss of prestige. Barclays Bank should have disposed of its merchant-banking acquisition BZW when it became obvious that the merger had failed. Instead, Barclays clung to the dream of becoming a global investment bank for over a decade only to end up, according to analysts, virtually paying Credit Suisse First Boston to take BZW off its hands.

More recently, the London-based restaurant chain Chez Gerard has suffered severely thanks to a failed ambition for expansion into the provinces. If it had closed the loss-making restaurants and accepted the loss of prestige it might have avoided the possible humiliation of a take-over bid.

The march of folly
Generally speaking, it becomes more difficult to terminate a failing course of action as time passes. Outside investors may have a stake in the outcome. Sponsors expect to see results. Staff may be recruited and whole departments created to support the venture. What manager wants to rock the boat? Eventually the venture may acquire a taken-for-granted status. That is, it survives because no one dares to question it.

Some projects, however, are retained because they are too expensive to close. When Chicago’s new sewer system was finally completed it was such a poor effort that it was inevitably dubbed money down the drain by the media. Yet there was no possibility of starting again – it was just too expensive. A more recent white elephant is Sheffield’s “super tram” system. The trams have never carried anywhere near the number of passengers originally forecast but the sheer cost of ripping up the tracks meant that it would be unthinkable to abandon the project.

So-called “long-haul” projects that require huge investment and yield no revenues until the work is finished are particularly fraught because time equals risk.

Concorde was planned when aviation fuel was cheap. By the time the plane entered service, however, that situation no longer applied – one reason why the development costs have never been recouped. How will the market for mobile telephones have changed by the time 3G applications become available?

Nothing succeeds like success?
Ironically it is the managers with the most successful track records who are most prone to making the kind of misjudgements that lead to escalation. This is because as human beings we interpret success as confirming our competence even if it is due entirely to luck.

Repeated success can be dangerous because it makes us feel infallible and therefore encourages us to take bigger and bigger risks. Research into gambling behaviour has shown that players who experience early wins in games of chance tend to bet more than their less successful counterparts. Repeated success can undermine a manager’s decision-making ability because it leads to complacency.

For example, repeated success may tempt a manager to dispense with market research and rely upon hunches because he or she has always been right in the past. The trouble is that the reason they were successful was because they took the trouble to conduct careful market research. Inevitably there comes a reckoning.

Although the precise links between escalation and perceived self-efficacy are unclear, managers with successful track records are more likely to persist in the face of failure because their self-confidence tells them they will win through in the end. It can be very hard for those unaccustomed to failure to recognise

McDonald’s: protecting its reputation
the limits of their powers. Sometimes it takes a severe shock, such as a profits warning, to force them to recognise reality. By then, however, it may be too late.

**Managing escalation**

The first question managers should ask themselves before becoming involved in anything is:

**What might you be getting into?**

The Chinese proverb “he who rides a tiger can never dismount” suggests that it is easier to get into something than it is to get out. It is important to think through the implications of embarking on a course of action that may seem to involve little risk and can easily be broken off if it fails. The fast-food chain McDonald’s decision to sue environmental campaigners John Morris and Helen Steel for libel was a public relations disaster. Yet McDonald’s did not begin by issuing writs – it merely sought an apology.

As human beings we tend to be more aware of why we are doing something rather than what we may be doing. The trick is to consider the significance and possible long-term consequences of embarking upon a particular course of action. Although decision making is surrounded by doubt, there are also some certainties. A decision is like a bridge – it separates us from some future state. A question that should always be asked before crossing that bridge is: “If I do X what will definitely follow?” For example, anyone who enters my book auction risks becoming trapped in a bidding war yet few students think about what they might be getting into and what a few moments of fun might end up costing them. The wisest students in my book auction are those who never bid.

In theory, withdrawal is always an option. Yet it may be wiser to assume the opposite and then consider whether a decision still makes sense. Quite simply, once you invest resources in a venture you are committed and therefore bound to deliver – come what may. This applies particularly to long-haul projects. In the words of the aviation industry, managers should always remember that although takeoff is optional, landing is compulsory.

**Begin with doubts**

It was Francis Bacon who said that it is better to begin with doubts than certainty. All decisions involving uncertainty run the risk of failing to turn out as expected, no matter how rock solid they may appear. For example, McDonald’s had good reason to believe that an apology would be forthcoming because of its experience of similar cases. To McDonald’s surprise and consternation, however, Steel and Morris refused.

It can be difficult for managers to resist becoming caught up in a tidal wave of enthusiasm that may accompany a prospective new venture. The best way of countering myopic vision is to confront the risks and the possible downside of a venture in addition to conducting a conventional cost/benefit analysis. No one can make a decision without guessing what the future is likely to hold. Ultimately managers can only play their cards and take their chances. The point is that they must remember that they are doing precisely that.

**What are you trying to achieve?**

Almost all ventures are a means to an end but they can become an end in themselves. Managers can become so absorbed in a particular venture that they develop tunnel vision. Completing the project becomes all-important at the expense of considering whether the project makes sense any more and whether there might be better or easier ways of reaching a particular goal. The solution is to stand back from things periodically and consider what you are trying to achieve.

**Insist on facts, not optimism**

The next question is how you can be sure of achieving the goal. This is where mental rigour and determination really count, as it is essential to pin others down to facts and figures. Managers also need to pay proper attention to what their information is telling them and resist the urge to escape into wishful thinking.

**Winner’s curse**

As the saying goes, “you can have anything you want provided you are prepared to pay too much for it”. Managers should set limits on their involvement and pull out once those limits are reached. This applies particularly to auctions, as emotions can run high and once the gavel falls you are committed. Besides, all auctions are a trap. This is because logically the true worth of an item is the second-highest bid – hence the aphorism “winner’s curse”.

**Alternatives are power**

It is easier to let go of a cherished ambition if there is something to take its place. Alternatives are a source of power. Managers who possess alternatives

Spring 2003
are much less likely to become caught up in an escalatory spiral or pay too high a price for something because the possession of alternatives increases their freedom of action and enables them to view competition with detachment.

**Fiasco does not just happen, it is created**

Although management may involve the application of commonsense, commonsense can be wrong and managers need to develop an eye for a potentially destructive paradox. For example, our efforts to prevent something can create the very situation that we are trying to avoid. McDonald's sued in order to protect its reputation but did infinitely more damage than if it had simply ignored the protest. It never stopped to think whether the cure might be worse than the disease.

Another dangerous scenario is when people interfere with a project. Interference is often prompted by good intentions but ends up paving the road to hell because the venture effectively becomes “something else”. For example, what may have started as a simple project using tried-and-tested technology becomes more and more complicated and therefore more risky.

**Don’t be afraid to hear the worst**

It was Winston Churchill who said that in war truth is so precious that it must be guarded with a tissue of lies. The same can apply to failing ventures. It can be difficult for managers to discover the true state of affairs because politically adroit subordinates are only too aware of what can happen to messengers bringing bad news. The only way to counter such caution is to demonstrate, by deed, that you are equal to hearing the worst. Failing that, the best people to ask for information are junior staff working at the “coal face”. They may respond bluntly but that is because they are being honest.

**Can the project be modified?**

Technically a venture fails when expectations cannot be met. A venture only really fails, however, when it no longer commands the support of people in the organisation. It may be possible to restore support for a failing venture by redesigning it or by dividing it into smaller, less-risky ventures. In order to do this it may be necessary to change the project manager and other key personnel. Dedicated and committed staff can become a liability if their passion descends into monomania.

**Does the project still make sense?**

One way of resisting the temptation to engage in risk-seeking behaviour is by acting on reality and thereby changing it. More specifically, we tend to become risk seeking when we see the situation as a choice between losses – either a definite loss at time A or a possible bigger loss at time B. The way out of this mental trap is to forget all about losses and simply to ask whether continuance represents the best return on investment or whether alternative courses of action might be more rewarding.

**A good decision maker has no ego**

In theory, ego is easily subtracted from the equation because it is within the control of the individual. In practice, because all is human, subtracting ego can very difficult – but not impossible. One possibility is to consider what ego-defensiveness is going to cost.

Although escalation is a trap, nothing need be inevitable. Setting one’s ego aside can be the key to liberation. Significantly the word risk derives from the early-Italian *risicare*, meaning “to dare”. It requires daring to persist against ever-widening odds just as it requires daring to say “stop”. “To dare” implies that escalation is not a fate but a choice.

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**Resources**


