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Dear Executive:

I couldn't let a year go by without sending at least one letter to my long-suffering readers. I've found a lot more to do – or I should say that a lot more to do has found me – in my semi-retirement that I had anticipated. A lot of it has been for what "The Man of Many Hats," Bud Kulesza, calls "psychic income," but for someone in my position, that is often more satisfying than the monetary variety. Finding more ways to share five decades of experience with a wider audience before the "gone out to lunch" sign goes up is always welcome. Fortunately, watching Major League Baseball's post-season activity over the past six weeks has provided me with something to comment on, so here is your "rant" for 2017.

Management Lessons from the 2017 Baseball Post-Season

Over the years, I've found many business analogies in the game of baseball. This year's baseball post-season provided a few that relate to the subject on which I focused much of my attention during the past year; namely, human behavior and decision making.

It has been shown by both psychologists and neurologists that human decision making is driven primarily by emotion. In this sense, emotions are the psychological and physical signals and their evoked feelings that are consciously or subconsciously associated with past outcomes. These are the signals and feelings that bias human's decision making towards certain behaviors and away from others. Among the bases for these emotions are memories of previous experiences, perceptions of why certain results followed earlier events, personal goals and personal fears. Emotional decisions are not particularly sophisticated or precise, but their speed and utility often make up for what they lack in sophistication and precision. The ability to make emotion only-based has been critical to our survival as a species. After all, our ancestors would have been in big trouble had they taken the time to do an analysis of the best way to escape from a tiger when one suddenly confronted them while strolling across the savanna. So when time is of the essence, emotions are the most critical element in decision making.

Data and analytics are also used by humans in the decision making process, but most often they are used to justify decisions that have already been made emotionally. The informal, unscientific survey I've been conducting for the past twelve years (during which I've quizzed 60-70 individuals) indicates that about 25% of decisions are based on "the data" and 75% use "the data" to justify decisions that have already been made. This is especially the case when the decision maker has a great deal of experience. These well-seasoned decision makers' emotions lead them to certain conclusions and then, when it is necessary, they ask their accountants for an analysis that justifies than conclusion.

For example, a decision maker wants to win a particular contract, so the cost estimator manages to come up with an analysis that shows the contract will be profitable at a price that will win the job. Another decision maker wants to buy a certain new piece of capital equipment, so the financial analyst manages to come up with an ROI calculation that shows that equipment will generate an acceptable return. Still another decision maker doesn't want to get fired because of an unfavorable forecast, so the accountant manages to come up with a much rosier forecast that will keep the decision maker employed. It happens all the time; 75% of the time by my calculations.

Emotions are extremely valuable when there is no time for analytics or when the decision maker's emotions (which should always be a factor) tell him or her that the current situation is an exception to the decision the analytics suggests. Otherwise, "the data" should a decision's primary driver.

Which brings us to baseball's post-season. Before the World Series ended, three teams that made the post-season playoffs fired their very successful, well-experienced managers; Joe Girardi of the Yankees, Dusty Baker of the Nationals and John Farrell of the Red Sox. Reports indicate that the dismissals were due to these managers being too "old school" – they relied primarily on their emotions and paid too little attention to analytics. As of this writing, four new managers had been hired by major league baseball teams, Alex Cora by the Red Sox, Gabe Kapler by the Phillies, Dave Martinez by the Nationals and Mickey Callaway by the Mets. None of them have any major league managing experience, highlighting what appears to be a new trend in baseball; organizations are placing a greater emphasis on younger personnel with the ability to integrate analytics into the game than they are those with experience in the dugout. Analytics are gaining on emotion.

Consider the World Series Champion Huston Astros – a team dedicated to the use of analytics. They rely heavily on analytics in drafting players. They rely heavily on analytics is setting their 40-man roster; going so far as to release future slugger J. D. Martinez to make room on the roster for eventual World Series MVP George Springer back in 2014. They use analytics to evaluate pitcher/batter match ups, adjust defensive alignments based on the hitter/pitcher match ups, and make other decisions where there is sufficient time to study the data and evaluate the options.

Then comes game time – a time when decisions must be made quickly. Houston's manager, A. J. Hinch, is a psychology major from Stanford University who had only 212 games of managing experience when hired by the Astros. His primary post-playing career (350 major league games) experience was in the front offices of the Arizona Diamondbacks and San Diego Padres where his work relied heavily on analytics. During the World Series he had all the assembled analytics at his fingertips, but at certain points in the Series had to recognize situations where those analytics might not apply. In those cases, he took a chance and used his emotions to override the decision suggested by "the numbers."

In Game 3, pitcher Brad Peacock – a starter for most of the year – was brought into the game in the 6th inning to try to hold Houston's lead. After eight innings, Houston had a 5-3 lead and Peacock had pitched effectively for 2 1/3 innings. The analytics would say to bring in "the closer," or at least an experience relief pitcher to close out the game in the 9th. But Hinch went by the evidence of his eyes – his emotions – and left Peacock, who had been pitching well, in the game to close it out. He succeeded.

In Game 5, the 13-12, 10-inning marathon, Hinch made another emotional decision that paid off. With two outs in the bottom of the 10th, the potential tying run was on second base, but that runner was slow-footed catcher Brian McCann. Houston's back-up catcher, Evan Gattis, was already in the game as Houston's designated hitter, so if he pinch ran for McCann and Houston didn't score, he would either lose the designated hitter or have to insert third-string catcher Juan Centeno, who had played in only 22 games all season and had only 57 plate appearances, into an important game at a critical point. Despite the risk, Hinch pinch ran the speedy Derek Fisher for McCann and Fisher scored the game winning run on a single that would not have scored McCann.[1]

In Game 7, Hinch overrode analytics again with a decision similar to the one he made in Game 3. Charlie Morton, another Houston starting pitcher, was brought in to relieve in the 6th inning. He pitched effectively for three innings, giving up just one run, and analytics would again suggest it was time to close out the game with an experienced "closer." Again, Hinch followed his emotions. The evidence of his eyes told him Morton was pitching well and was the best choice to finish the game successfully. He promptly did so by retiring three batters in order.

The Houston Astro's management team developed and used accurate and relevant analytical information to put the team in a position to succeed. It relied heavily on analytics to assemble its roster, develop its players, select its management team and provide guidance for the minute-by-minute decisions made during a game. But decisions were not made exclusively by "the numbers." At every level experienced decision makers – individuals who have accumulated a vast store of emotions – monitored the conclusions suggested by the data and overrode those conclusions only when they were confident that their emotional knowledge told them "the analytics do not apply in this case."

Sadly, this is not the process I've seen most business decision makers follow. Instead, they let their over-confidence, or sometimes egotism, put too much value on their emotions and then turn to selective – and often distorted – analytics as a means of "proving" the correctness of their emotional decisions. During my four decades as a senior financial executive and consultant, I've seen scores of companies underachieve, struggle to survive and even fail due to the ascendancy of emotional decisions made without the benefit of accurate and relevant analytical data.

Perhaps today's business leaders could learn a lesson from the Houston Astros.

Center for Managerial Costing Quality

One of the psychic income activities I've been involved with for the past eighteen months has been working with an Institute of Management Accountants' task force created to "help management accountants and the broader business community recognize and understand the need, the benefits, and a path forward for improving cost information for internal decision support." My cohorts on the task force are Raef Lawson and Kip Krumwiede of the IMA, fellow practitioners Gary Cokins and Larry White and professors Monte Swain (BYU) and Doug Clinton (NIU). As part of our work, we've been constructing a "Center for Managerial Costing Quality" website (www.thecmcq.org) resources for the many diverse stakeholder groups affected by the quality of their organization's managerial costing practices. If you're interested in advancing the use of sound managerial costing in industry, I think you'll find the information already included on the website a source of useful information. A good place to start would be the nine-question quick assessment at www.thecmcq.org/quick-assessment. We've just gotten started, so check back occasionally for new information and resources.

IMA Detroit's 2018 Spring Management Accounting Conference

Save the date – Thursday, March 22, 2018 – for IMA Detroit's 2018 Spring Management Accounting Conference. The conference's theme will be "Managerial Costing in the Automotive Supply Industry" and it will address many of the industry's cost-related issues. As in past years, the cost of this year's conference will be less than $200 per participant. Like last year, the conference will again be held at Laurel Manor in Livonia, Michigan. Additional details and registration information will be available after the holidays. Stay tuned!

As always, I look forward to hearing from any of you who have questions or comments regarding this letter and you should feel free to forward a copy to anyone you believe might be interested (or at least mildly amused).

HAVE A JOYOUS HOLIDAY SEASON AND A HEALTHY, HAPPY AND PROSPEROUS 2018!

Very truly yours,

Doug

Douglas T. Hicks, CPA
President

[1] This is a move that the Detroit Tigers' recently-released manager, Brad Ausmus, often made in the late innings and for which he was greatly criticized in the press and on talk radio. When slow-footed designated hitter Victor Martinez would end up in scoring position late in a close game, Ausmus would pinch run for him. Unfortunately, the next hitter would seldom cooperate and fail to score the pinch runner. The Tigers would then have a weak hitter in the DH spot for the rest of the game and the critics would have a field day.