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## Learning Byte 251 The Halo Effect



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# The Halo Effect - and Other Managerial Delusions

***Companies cannot achieve superior and lasting business performance simply by following a specific set of tests.***

Executives often rely on business books, articles and business case studies that claim to reveal a blueprint for lasting competitive advantage in order to achieve superior performance. The research underpinning this research, however, is often flawed and obscures the basic truth that success in the business world is based on decisions made under uncertainty and in the presence of factors that the executives cannot control.

## Beware the halo effect

### What is the Halo Effect?

Many studies of company performance are undermined by a problem known as the halo effect. The **Halo Effect** is the tendency to make specific inferences on the basis of a general impression.

### How does the halo effect manifest itself in the business world?

Company performance, good or bad, creates an overall impression, a halo that shapes how we perceive its strategy, leaders, employees, culture, and other elements.

Wise managers know to be wary of the halo effect. They look for independent evidence rather than merely accepting the idea that a successful company has a visionary leader and a superb customer orientation or that a struggling company must have a poor strategy and weak execution.

The halo effect is especially damaging because it often compromises the quality of data used in research. The reliance on questionable data, in turn, gives rise to a number of further errors in logic.

Two delusions of absolute performance and of lasting success have particularly serious repercussions for business strategists:

#### 1. The delusion of absolute performance

- Business best sellers claim that companies can achieve success if it follows a specific set of steps.
- These studies often rely on sources of data that are routinely undermined by the halo effect.
- As a result, where a given set of factors may appear to have led predictably to success, the reverse is more likely.
- Following a given formula can't ensure high performance.
- Success and failure depend not only on a company's actions but also on those of its rivals.
- The **delusion of absolute performance** is very important because it suggests that a company can achieve high performance by following a simple formula, regardless of the actions of competitors.
- High performance comes from doing things better than rivals can.

#### 2. The delusion of lasting success

- Suggests that companies can achieve enduring success in a predictable way.
- These studies typically begin by selecting a group of companies that have outperformed the market for many years.
- Much of the data comes from sources that are commonly contaminated by the halo effect.
- Corporate longevity is neither very likely nor generally associated with high performance.
- High performance is difficult for companies to maintain - in a free-market economy, profits tend to decline as a result of imitation and competition.
- The **delusion of lasting success** is a serious matter because it casts building an enduringly high-performing company as an achievable objective.



## Clear thinking for business strategists

- No formula can guarantee a company's success in a competitive business environment.
- If success could be reduced to a formula, companies would not need strategic thinking.
- What makes strategic decision making so difficult, but valuable to companies, is that there are no guaranteed keys to success.
- The ability to make the sorts of difficult, complex judgments that are pivotal for a company's fortunes is a business executive's most important contribution.

### **Business executives must recognize the fundamental uncertainty of the business world:**

- Anticipating what customers will do.
- Anticipating technological change.
- The company's internal capabilities.

Clear-thinking executives know that in an uncertain world, actions and outcomes are imperfectly linked. Wise managers resist the natural tendency to make attributions based solely on outcomes.

This is a précis of an article adapted from the article "*The Halo Effect: ... and the Eight Other Business Delusions That Deceive Managers*", New York: Free Press, 2000. Copyright © 2007 McKinsey & Company. All rights reserved - written by Phil Rosenzweig, a professor of strategy and international management at the International Institute for Management Development (IMD), in Lausanne, Switzerland.

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