BUSINESS OBJECTIVES AND SURVIVAL NEEDS: NOTES ON A DISCIPLINE OF BUSINESS ENTERPRISE

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The literature of business management, confined to a few “how to do” books only fifty years ago, has grown beyond any one man’s capacity even to catalogue it. Professional education for business has become the largest and most rapidly growing field of professional education in this country and is growing rapidly in all other countries in the free world. It also has created in the advanced postgraduate education for experienced, mature, and successful executives—perhaps first undertaken in systematic form at the University of Chicago—the only really new educational concept in a hundred and fifty years.

Yet so far we have little in the way of a “discipline” of business enterprise, little in the way of an organized, systematic body of knowledge, with its own theory, its own concepts, and its own methodology of hypothesis, analysis, and verification.

THE NEED FOR A THEORY OF BUSINESS BEHAVIOR

The absence of an adequate theory of business enterprise is not just an “academic” concern; on the contrary, it underlies four major problems central to business as well as to a free-enterprise society.

1. One is the obvious inability of the layman to understand modern business enterprise and its behavior. What goes on, and why, “at the top” or “on the fourteenth floor” of the large corporation—the central economic and one of the central social institutions of modern industrial society—is as much of a mystery to the “outsider” as the magician’s sleight of hand is to the small boy in the audience. And the “outsiders” include not only those truly outside business enterprise. They include workers and shareholders; they include many professionally trained men in the business—the engineers or chemists, for instance—indeed, they include a good many management people themselves: supervisors, junior executives, functional managers. They may accept what “top management” does, but they accept on faith rather than by reason of knowledge and understanding. Yet such understanding is needed for the success of the individual business as well as for the survival of industrial society and of the free-enterprise system.

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One of the real threats is the all-but-universal resistance to profit in such a system, the all-but-universal (but totally fallacious) belief that socialism—or any other ism—can operate an industrial economy without the "rake-off" of profit, and the all-but-universal concern lest profit be too high. That the danger in a dynamic, industrial economy is that profit may be too low to permit the risks of innovation, growth, and expansion—that, indeed, there may be no such thing as "profit" but only provision for the costs of the future—very few people understand.

This ignorance has resisted all attempt at education; this resistance to profits has proved impervious to all propaganda or appeals, even to the attempts at "profit-sharing."

The only thing capable of creating understanding of the essential and necessary function of profit in an expanding, risk-taking, industrial economy is an understanding of business enterprise. And that for all without personal, immediate experience in the general management of a business can come only through a general "model" of business enterprise, that is, through the general theory of a systematic discipline.

2. The second problem is the lack of any bridge of understanding between the "macro-economics" of an economy and the "micro-economics" of the most important actor in this economy, the business enterprise. The only "micro-economic" concept to be found in economic theory today is that of "profit maximization." To make it fit the actual, observable behavior of business enterprise, however, economists have had to bend, stretch, and qualify it until it has lost all meaning and all usefulness. It has become as complicated as the "epicycles" with which pre-Copernican astronomers tried to save the geocentric view of the universe: "profit maximization" may mean short-run, immediate revenue or long-range basic profitability of wealth-producing resources; it may have to be qualified by a host of unpredictables such as managerial power drives, union pressures, technology, etc.; and it completely fails even then to account for business behavior in a growing economy. It does not enable the economist to predict business reaction to public policy any more; to the governmental policy-maker business reaction is as "irrational" as government policy, by and large, seems to the businessman.

But in modern industrial society we must be able to "translate" easily from public policy to business behavior and back again. The policy-maker must be able to assess the impact of public policy on business behavior; and the businessman—especially in the large enterprise—must be able to assess the impact of his decisions and actions on the "macro-economy." "Profit-maximization" does not enable us to do either, as this paper intends to show, primarily because it fails to understand the role and function of profit.

3. The third area in which the absence of a genuine theory of business enterprise creates very real problems is that of the internal integration of the organization. The management literature is full of discussions of the "problem of the specialist" who sees only his own functional area or of the "problem of the scientist in business" who resents the demand that he subordinate his knowledge to business ends. Yet we will be getting ever more specialized; we will, of necessity, employ more and more highly trained "professionals." Each of those must be dedicated to his specialty; yet each must share a common vision and common
goals and must voluntarily engage in a common effort. To bring this about is already the most time- and energy-consuming job of management, certainly in our big businesses, and no one I know claims to be able to do it successfully.

Twenty years ago it was still possible to see a business as a mechanical assemblage of “functions.” Today we know that, when we talk of a “business,” the “functions” simply do not exist. There is only business profit, business risk, business product, business investment, and business customer. The functions are irrelevant to any one of them. And yet it is equally obvious, if we look at the business, that the work has to be done by people who specialize, because nobody can know enough even to know all there is to be known about one of the major functions today—they are growing too fast. It is already asking a great deal of a good man to be a good functional man, and, in some areas, it is rapidly becoming almost too much to ask of a man. How, then, do we transmute functional knowledge and functional contribution into general direction and general results? The ability of big business—but even of many small ones—to survive depends on our ability to solve this problem.

4. The final problem—also a symptom both of the lack of discipline and of the need for it—is of course the businessman’s own attitude toward “theory.” When he says, “This is theoretical,” he by and large still means: “This is irrelevant.” Whether managing a business enterprise could or should be a “science” (and one’s answer to this question depends primarily on how one defines the word “science”), we need to be able to consider theory the foundation for good practice. We would have no modern doctors, unless medicine (without itself being a “science” in any strict sense of the word) considered the life-sciences and their theories the foundation of good practice. Without such a foundation in a discipline of business enterprise we cannot make valid general statements, cannot therefore predict the outcome of actions or decisions, and can judge them only by hindsight and by their results—when it is too late to do anything. All we can have at the time of decision would be “hunches,” “hopes,” and “opinions,” and, considering the dependence of modern society on business enterprise and the impact of managerial decisions, this is not good enough.

Without such a discipline we could also neither teach nor learn, let alone work systematically on the improvement of our knowledge and of our performance as managers of a business. Yet the need both for managers and for constant improvement of their knowledge and performance is so tremendous, quantitatively as well as qualitatively, that we simply cannot depend on the “natural selection” of a handful of “geniuses.”

The need for a systematic discipline of business enterprise is particularly pressing in the underdeveloped growth countries of the world. Their ability to develop themselves will depend, above all, on their ability rapidly to develop men capable of managing business enterprise, that is, on the availability of a discipline that can be taught and can be learned. If all that is available to them is development through experience, they will almost inevitably be pushed toward some form of collectivism. For, however wasteful all collectivism is of economic resources, however destructive it is of freedom, dignity, and happiness, it economizes the managerial resource through its concentration of entrepreneurial and managerial decisions in the hands of a few “planners” at the top.
WHAT ARE THE SURVIVAL NEEDS OF BUSINESS ENTERPRISE?

We are still a long way from a genuine "discipline" of business enterprise. But there is emerging today a foundation of knowledge and understanding. It is being created in some of our large companies and in some of our universities. In some places the starting point is economics, in some marketing, in some the administrative process, in others such new methodologies as operations research and synthesis or long-range planning. But what all these approaches, regardless of starting point or terminology, have in common is that they start out with the question: What are the survival needs of business enterprise? What, in other words, does it have to be, to do, to achieve—to exist at all? For each of these "needs" there has, then, to be an "objective."

It may be said that this approach goes back to the pioneering work on business objectives that was done at the Bell Telephone System under the presidency of Theodore Vail a full forty years ago. Certainly, that was the first time the management of a large business enterprise refused to accept the old, glib statement, "The objective of a business is to make a profit," and asked instead, "On what will our survival as a privately owned business depend?" The practical effectiveness of the seemingly so obvious and simple approach is proved by the survival, unique in developed countries, of privately owned telecommunications in the United States and Canada. A main reason for this was certainly the "survival objective" Vail set for the Bell System: "Public satisfaction with our service." Yet, though proved in practice, this remained, until recently, an isolated example. And it probably had to remain such until, within the last generation, the biologists developed the approach to understanding of "systems" by means of defining "essential survival functions."

"Survival objectives" are general; they must be the same in general for each and every business. Yet they are also specific; different performance and different results would be needed in each objective area for any particular business. And every individual business will also need its own specific balance between them at any given time.

The concept of survival objectives thus fulfils the first requirement of a genuine "theory"—that it be both formal and yet concretely applicable, that is, "practical." Survival objectives are also "objective" both as to their nature and as to the specific requirements in a given situation. They do not depend on "opinion" or "hunch." Yet—and that is essential—they do not "determine" entrepreneurial or managerial decisions; they are not (as is so much of traditional economics or of contemporary behavioral science) an attempt to substitute formulas for risk-taking decision or responsible judgment. They attempt rather to establish the foundation for decision and judgment, to make what is the specific task of entrepreneur and manager possible, effective, and rational, and to make it understandable and understood.

We have reached the stage where we know the "functions" of a business enterprise, with "function" being used the way the biologist talks about "procreation" as a "function" essential for the perpetuation of a living species.

There are five such "survival functions" of business enterprise. Together they define the areas in which each business, to survive, has to reach a standard of performance and produce results above a minimum level. They are also the areas
affected by every business decision and, in turn, affecting every business result. Together these five areas of “survival objectives” describe therefore (operationally) the “nature of business enterprise.”

1. The enterprise needs, first, a human organization designed for joint performance and capable of perpetuating itself. It is an assemblage not of brick and mortar but of people. These people must work as individuals; they cannot work any other way. Yet they must voluntarily work for a common result and must therefore be organized for joint performance. The first requirement of business is therefore that there be an effective human organization.

But business must also be capable of perpetuating itself as a human organization if only because all the things we decide every day—if, indeed, we are managers—take for their operation more time than the good Lord has allotted us. We are not making a single decision the end of which we are likely to see while still working. How many managerial decisions will be liquidated within twenty years, will have disappeared, unless they are totally foolish decisions? Most of the decisions we make take five years before they even begin to have an impact; this is the short range of a decision. And then they take ten or fifteen years before (at the very earliest) they are liquidated, have ceased to be effective, and, therefore, have ceased to have to be reasonably right.

This means that the enterprise as a human organization has to be able to perpetuate itself. It has to be able to survive the life-span of any one man.

2. The second survival objective arises from the fact that the enterprise exists in society and economy. In business schools and business thinking we often tend to assume that the business enterprise exists by itself in a vacuum. We look at it from the inside. But the business enterprise is a creature of society and economy. If there is one thing we do know, it is that society and/or economy can put any business out of existence overnight—nothing is simpler. The enterprise exists on sufferance and exists only as long as society and economy believe that it does a job and a necessary, a useful, and a productive one.

I am not talking here of “public relations”; they are only one means. I am not talking of something that concerns only the giants. And I am not talking of “socialism.” Even if the free-enterprise system survives, individual businesses and industries within it may be—and of course often have been—restricted, penalized, or even put out of business very fast by social or political action such as taxes or zoning laws, municipal ordinances or federal regulation, and so forth. Anticipation of social climate and economic policy, on the one hand, and organized behavior to create what business needs to survive in respect to both are therefore genuine survival needs of each business at all times. They have to be considered in every action and have to be “factored” into every business decision.

Equally, the business is a creature of the economy and at the mercy of changes in it—in population and income, ways of life and spending patterns, expectations and values. Again here is need for objectives which anticipate so as to enable the business to adapt and which at the same time aim at creating the most favorable conditions.

3. Then, of course, there is the area of the specific purpose of business, of its contribution. The purpose is certainly to supply an economic good and service. This is the only reason why business exists.
We would not suffer this complicated, difficult, and controversial institution except for the fact that we have not found any better way of supplying economic goods and services productively, economically, and efficiently. So, as far as we know, no better way exists. But that is its only justification, its only purpose.

4. There is another purpose characteristic which I would, so to speak, call the nature of the beast; namely, that this all happens in a changing economy and a changing technology. Indeed, in the business enterprise we have the first institution which is designed to produce change. All human institutions since the dawn of prehistory or earlier had always been designed to prevent change—all of them: family, government, church, army. Change has always been a catastrophic threat to human security. But in the business enterprise we have an institution that is designed to create change. This is a very novel thing. Incidentally, it is one of the basic reasons for the complexity and difficulty of the institution.

This means not only that business must be able to adapt to change—that would be nothing very new. It means that every business, to survive, must strive to innovate. And innovation, that is, purposeful, organized action to bring about the new, is as important in the social field—the ways, methods, and organization of business, its marketing and market, its financial and personnel management, and so on—as it is in the technological areas of product and process.

In this country industrial research expenditures have risen from a scant one-tenth of 1 per cent of national income to 1½ or 2 per cent in less than thirty years. The bulk of this increase has come in the last ten years; this means that the impact in the form of major technological changes is still ahead of us. The speed of change in non-technological innovation, for instance, in distribution channels, has been equally great. Yet many businesses are still not even geared to adaptation to change; and only a mere handful are geared to innovation—and then primarily in the technological areas. Here lies therefore a great need for a valid theory of business enterprise but also a great opportunity for contribution.

5. Finally, there is an absolute requirement of survival, namely, that of profitability, for the very simple reason that everything I have said so far spells out risk. Everything I have said so far says that it is the purpose, the nature, and the necessity of this institution to take risks, to create risks. And risks are genuine costs. They are as genuine a cost as any the accountant can put his finger on. The only difference is that, until the future has become past, we do not know how big a cost; but they are costs. Unless we provide for costs, we are going to destroy capital. Unless we provide for loss, which is another way of saying for future cost, we are going to destroy wealth. Unless we provide for risk, we are going to destroy capacity to produce. And, therefore, a minimum profitability, adequate to the risks which we, by necessity, assume and create, is an absolute condition of survival not only for the enterprise but for society.

This says three things. First, the need for profitability is objective. It is of the nature of business enterprise and as such is independent of the motives of the businessman or of the structure of the "system." If we had archangels running businesses (who, by definition, are deeply disinterested in the profit motive), they would have to make a profit and would have to watch profitability just as eagerly, just as assiduously, just as faithfully, just as responsibly, as the most
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Second, profit is not the "entrepreneur's share" and the "reward" to one "factor of production." It does not rank on a par with the other "shares," such as that of "labor," for instance, but above them. It is not a claim against the enterprise but the claim of the enterprise—without which it cannot survive. How the profits are distributed and to whom is of great political importance; but for the understanding of the needs and behavior of a business it is largely irrelevant.

Finally, "profit maximization" is the wrong concept, whether it be interpreted to mean short-range or long-range profits or a balance of the two. The relevant question is, "What minimum does the business need?" not "What maximum can it make?" This "survival minimum" will, incidentally, be found to exceed present "maxima" in many cases. This, at least, has been my experience in most companies where a conscious attempt to think through the risks of the business has been attempted.

Here are five dimensions; and each of these five is a genuine view of the whole business enterprise. It is a human organization, and we can look upon it only in that aspect, as does our human relations literature. We can look at it from its existence in society and economy, which is what the economist does. This is a perfectly valid, but it is a one-sided view.

We can, similarly, look at the enterprise only from the point of view of its goods and services. Innovation and change are yet another dimension, and profitability is yet another. These are all genuine true aspects of the same being. But only if we have all five of them in front of us do we have a theory of business enterprise on which practice can be built.

For managing a business enterprise means making decisions, every one of which both depends on needs and opportunities in each of these five areas and, in turn, affects performance and results in each.

THE WORK TO BE DONE

The first conclusion from this is that every business needs objectives—explicit or not—in each of these five areas, for malfunction in any one of these endangers the entire business. And failure in any one area destroys the entire business—no matter how well it does in the other four areas. Yet these are not interdependent but autonomous areas.

1. Here, then, is the first task of a discipline of business enterprise: to develop clear concepts and usable measurements to set objectives and to measure performance in each of these five areas. The job is certainly a big one—and a long one. There is no area as yet where we can really define the objectives, let alone measure results. Even in respect to profitability we have, despite great recent advances in managerial economics, figures for the past rather than measurements that relate current or expected profitability to the specific future risks and needs. In the other areas we do not even have that, by and large. And in some—the effectiveness of the human organization, the public standing in economy and society, or the area of innovation—we may, for a long time to come, perhaps forever, have to be content with qualitative appraisal making possible judgment. Even this would be tremendous progress.

2. A second conclusion is hardly less important: no one simple objective is "the" objective of a business; no one single yardstick "the" measure of performances, pros...
pects, and results of a business; no one single area "the" most important area.

Indeed, the most dangerous oversimplification of business enterprise may well be that of the "one yardstick," whether "return on investment," "market standing," "product leadership," or what have you. At their best these measure performance in one genuine survival area. But malfunction or failure in any one area is not counterbalanced by performance in any other area, just as a sturdy respiratory or circulatory system will not save an animal if its digestive or nervous system collapses. Success, like failure, in business enterprise is multidimensional.

3. This, however, brings out another important need: a rational and systematic approach to the selection and balance among objectives so as best to provide for survival and growth of the enterprise. These can be called the "ethics" of business enterprise, insofar as ethics is the discipline that deals with rational value choices among means to ends. It can also be the "strategy" of entrepreneurship. Neither "ethics" nor "strategy" is capable of being absolutely determined, yet neither can be absolutely arbitrary. We need a discipline here that encompasses both the "typical" decision which adapts to circumstances and "plays" the averages of statistical probability, and the innovating, "unique event" of entrepreneurial vision and courage breaking with precedent and trends and creating new ones—and there are already some first beginnings of such a discipline of entrepreneurship. But such a discipline can never be more than theory of composition is to the musical composer or theory of strategy to the military leader: a safeguard against oversight, an appraisal of risks, and, above all, a stimulant to independence and innovation.

Almost by definition the demands of different survival objectives pull in different directions, at least for any one time period. And it is axiomatic that the resources even of the wealthiest business, or even of the richest country, never cover in full all demands in all areas; there is never so much that there has to be no allocation. Higher profitability can thus be achieved only by taking a risk in market standing, in product leadership, or in tomorrow's human organization, and vice versa. Which of these risks the enterprise can take, which it cannot take, and what it cannot afford not to take—these risk-taking, value-decisions between goals in one area versus goals in others, and between goals in one area today versus goals in others tomorrow, is a specific job of the entrepreneur. This decision itself will remain a "judgment," that is, a matter of human values, appraisal of the situation, weighing of alternatives, and balancing of risks. But an understanding of survival objectives and their requirements can supply both the rational foundation for the decision itself and the rational criteria for the analysis and appraisal of entrepreneurial performance.

AN OPERATIONAL VIEW OF THE BUDGETING PROCESS

The final conclusion is that we need a new approach to the process in which we make our value decisions between different objective areas—the budgeting process. And in particular do we need a real understanding of that part of the budget that deals with the expenses that express these decisions, that is, the "managed" and "capital" expenditures.

Commonly today, budgeting is conceived as a "financial" process. But it is only the notation that is financial; the decisions are entrepreneurial. Commonly
today, "managed" expenditures and "capital" expenditures are considered quite separate. But the distinction is an accounting (and tax) fiction and misleading; both commit scarce resources to an uncertain future; both are, economically speaking, "capital" expenditures. And they, too, have to express the same basic decisions on survival objectives to be viable. Finally, today, most of our attention in the "operating budget" is given, as a rule, to other than the "managed" expenses, especially to the "variable" expenses, for that is where, historically, most money was spent. But, no matter how large or small the sums, it is in our decisions on the "managed" expenses that we decide on the future of the enterprise.

Indeed, we have little control over what the accountant calls "variable" expenses—the expenses which relate directly to units of production and are fixed by a certain way of doing things. We can change them, but not fast. We can change a relationship between units of production and labor costs (which we, with a certain irony, still consider "variable expenses" despite the fringe benefits). But within any time period these expenses can only be kept at a norm and cannot be changed. This is of course even more true for the expenses in respect to the decisions of the past, our "fixed" expenses. We cannot make them undone at all, whether these are capital expenses or taxes or what-have-you. They are beyond our control.

In the middle, however, are the expenses for the future which express our risk-taking value choices: the "capital expenses" and the "managed expenses." Here are the expenses on facilities and equipment, on research and merchandising, on product development and people development, on management and organization. This managed expense budget is the area in which we really make our decisions on our objectives. (That, incidentally, is why I dislike accounting ratios in that area so very much, because they try to substitute the history of the dead past for the making of the prosperous future.)

We make decisions in this process in two respects. First, what do we allocate people for? For the money in the budget is really people. What do we allocate people, and energy, and efforts to? To what objectives? We have to make choices, as we cannot do everything.

And, second, what is the time scale? How do we, in other words, balance expenditures for long-term permanent efforts against any decision with immediate impact? The one shows results only in the remote future, if at all. The development of people (a fifteen-year job), the effectiveness of which is untested and unmeasurable, is, for instance, a decision on faith over the long range. The other may show results immediately. To slight the one, however, might, in the long range, debilitate the business and weaken it. And, yet, there are certain real short-term needs that have to be met in the business—in the present as well as in the future.

Until we develop a clear understanding of basic survival objectives and some yardsticks for the decisions and choices in each area, budgeting will not become a rational exercise of responsible judgment; it will retain some of the "hunch" character that it now has. But our experience has shown that the concept of survival objectives alone can greatly improve both the quality and effectiveness of the process and the understanding of what is being decided. Indeed, it gives us, we are learning, an effective tool for the integration of functional work and spe-
cialized efforts and especially for creating a common understanding throughout the organization and common measurements of contribution and performance.

The approach to a discipline of business enterprise through an analysis of survival objectives is still a very new and a very crude one. Yet it is already proving itself a unifying concept, simply because it is the first *general* theory of the business enterprise we have had so far. It is not yet a very refined, a very elegant, let alone a very *precise*, theory. Any physicist or mathematician would say: This is not a theory; this is still only rhetoric. But at least, while maybe only in rhetoric, we are talking about something real. For the first time we are no longer in the situation in which theory is irrelevant, if not an impediment, and in which practice has to be untheoretical, which means cannot be taught, cannot be learned, and cannot be conveyed, as one can only convey the general.

This should thus be one of the "breakthrough" areas; and twenty years hence this might well have become the *central* concept around which we can organize the mixture of knowledge, ignorance, and experience, of prejudices, insights, and skills, which we call "management" today.