

Management by Objectives: As Developed by Peter Drucker, Assisted by Harold Smiddy

RONALD G. GREENWOOD

University of Wisconsin — La Crosse

In this article, I discuss the early development of the philosophy and concept of management by objectives (MBO) as it has been traditionally defined in the literature. Peter Drucker worked out the philosophic foundations of MBO with the assistance of Harold Smiddy of the General Electric Company, who was already putting the "manager's letter" concept into practice in the late 1940s.

Peter Drucker is often credited with "inventing" management by objectives. He himself has never claimed the distinction, but a perusal of the literature would lead one to a proper conclusion that Drucker was first to publish the concept and first to use the term. The history of MBO is clouded because it is a concept, and no concept or philosophy ever springs up full grown without a long period of germination. The seeds that later sprouted MBO were evident many times and in many places. Drucker's precursors who wrote about the need for objectives as a foundation for management, but did not use the term MBO, include James O. McKinsey [1922], Chester I. Barnard [1938, p. 233; Wolf, 1974, p. 114], Henri Fayol [1916], Mary Parker Follett [1941], Ralph C. Davis [1937, pp. 90-126; 1940, pp. 27-28; 1951, pp. 15-16], and Harry Hopf [1973]. Each hinted, some more strongly than others, about the importance of a philosophy such as MBO. Hundreds of unidentified managers probably even practiced systems with varying degrees of similarity to MBO, but the story of how Peter Drucker came to put it all together is worth telling.

MBO Defined

The writings of early management theorists could be interpreted as often hinting at MBO, if manage-

ment by objectives is simply defined as measuring work against stated objectives. I will use as a definition for MBO the often cited one of George Odiorne that it is "a process whereby the superior and subordinate managers of an organization *jointly* identify its common goals, define each individual's major areas of responsibility in terms of the results expected of him, and use these measures as guides for operating the unit and assessing the contribution of each of its members" [1965, pp. 55-56]. The key to this definition is that subordinates play a major role in setting their own objectives and not in merely receiving objectives from above. This would dismiss many of the claims made for previous use of MBO by such people as McKinsey, Barnard, and Fayol, or by such corporations as DuPont, General Motors, and Standard of New Jersey — firms that Odiorne claims used an early objective-based management style of organization [1978].

Drucker and Smiddy, Pre-GE Days

MBO as it is understood today was conceptualized by Peter Drucker and first put into practice by Harold Smiddy, a long-time vice president of the General Electric Company and a close personal friend of Drucker. Drucker even claimed that Smiddy was the godfather of his classic *The Practice of Management* [1954, p. ix].

Smiddy was Vice President of General Electric's Management Consultation Services and chief architect of that corporation's famous decentralized structure, which was so often copied in the 1950s and 1960s. Harold Smiddy had a lifetime commitment to both the theory and practice of management. He was Academy of Management president in 1963 and one of its original Fellows. Among his numerous awards are included The Taylor Key, Gantt Medal, and Wallace Clark Medal [Greenwood & Zimet, 1979]. It was Smiddy who designed the structure, and thought through and wrote a management philosophy that was the foundation for the decentralization reorganization General Electric put into operation in a five-year period beginning in 1951.

Smiddy's chief outside consultant was Peter Drucker. Drucker's association with Smiddy and his management consultation group was so close that during this reorganization time one might have mistakenly considered him to be on General Electric's payroll. Both men had similar experiences that led to Drucker's developing the MBO philosophy and to Smiddy's initial decision to try it in practice. Harold Smiddy, before coming to GE, had been a partner at Booz, Allen, and Hamilton. There he had learned the concept of the "manager's letter" from one of his associates. Simply put, the "manager's letter" required a job holder (manager or individual contributor) to write a letter to his or her superior indicating what the goals for the next period of time were, how the goals would be met, and what standards were to be expected. When the superior accepted this letter — usually after editing and discussion — it became the work "contract." When Harold Smiddy first came to the General Electric Company in 1948, he introduced the monthly letter concept to two operating divisions; but it was not until 1952, when he first began to have the corporate philosophy of management written, that Drucker was able to convince him of the ease with which the monthly letter concept could act as a foundation for an MBO philosophy of management.

Drucker had been invited to look at the political, social, and structural relationships at General Motors under Alfred P. Sloan, Jr., in the early 1940s [Drucker, 1946, 1979a.]. John Tarrant reports that it was here that Drucker picked up the phrase or concept "management by objectives." In his book on Peter Drucker, Tarrant quotes Drucker as saying "I

didn't invent the term 'management by objectives'; actually, Alfred Sloan used it in the 1950s" [1976, p. 77]. Tarrant now says that he misconstrued what Drucker said about Sloan using objectives as a key to his management style to mean he used the term; in fact Sloan used neither the term nor the MBO philosophy [1979]. Drucker reports that neither Sloan nor Donaldson Brown at GM "had [anything] to do with the term. . . [and] nothing to do with the concept as such" [1979b]. But Drucker also claims that Sloan "practiced managing by objectives without considering it central to his management philosophy or to his style [1979c].

Peter Drucker and Harold Smiddy first met after World War II, probably as early as 1946. As Drucker recalls it, Smiddy approached him after reading *The Concept of the Corporation* [Drucker, 1946]. Drucker was still teaching at Bennington College in Vermont and Smiddy was a partner of Booz, Allen, and Hamilton, heading the New York office. Between 1946 and 1948, the two met four or five times to discuss management. Drucker, in 1948, had taken on a consulting assignment with the Chesapeake and Ohio Railroad in Cleveland to study basic objectives and long-range planning. Drucker asked Smiddy to join him on this project, as both men had discussed the subject. Smiddy declined, having just decided to join General Electric, then he asked Drucker if he would be available to work with him once he moved over.

It was during this period that Drucker truly began to crystallize in his mind the concept of managing by objectives and self-control. Fundamentally, the basic difference between the philosophical development of Drucker and his predecessors Smiddy, Sloan, Fayol, Barnard, and the widely respected management consultant Harry Hopf, was that the others took for granted that the objectives were known, obvious, and given. What Drucker saw so clearly in his own mind, largely as a result of his consulting work, was that objectives are risk-taking decisions and are anything but known or given. In other words, to the earlier management theorists, objectives are something that somehow you use as a foundation for your planning or, at least, are inherent in your planning. To Drucker, objectives are something you look at first. Unless you do, you can do no planning, let alone any organizing, integrating, or measuring (to use the Smiddy functions of management [General Electric, 1954, p. 63]). The

earlier theorists (and most of the current crop) define the work of managing as planning, organizing, integrating, and measuring the work of the organization. To Drucker, these activities are the implementation of what he calls the real work of managing: setting objectives and deciding what the business is, what it should be, what it could be. For the last thirty years, Drucker has hammered on this point in almost every one of his management books; perhaps his point has not yet been understood. In summary, objectives to Sloan and Smiddy were obvious; to Drucker they were anything but obvious, yet are at the heart of real managing.

The Manager's Letter

Drucker did assist Smiddy at GE; indeed, he became an almost permanent fixture at GE's New York City corporate headquarters on Lexington Avenue. Drucker joined the faculty of New York University in 1950 and was able to act as a consultant to Harold Smiddy's Management Consultation Services Division on almost a daily basis during the period 1950-1954. Drucker and Smiddy shared many long hours of discussion on such GE problems and ventures as decentralization, operations research, manager development, and designing the famous GE Crotonville Training Center.

Because Drucker aided Smiddy in so many areas, specific topics would be pre-arranged for discussion when they met. One of the early subjects was the "manager's letter," which in 1952 was debated, discussed, and thought through over a period of many weeks. Smiddy frequently invited his associates to sit in on discussions of the principles behind this letter as he and Drucker thought it out. Once he asked one of his internal management consultants, William J. Greenwood, to sit in on an all-day discussion and to reduce their observations to a written document for further analysis. The write-up was carefully edited by Smiddy and Drucker [W.J. Greenwood, 1979; Smiddy, 1977].

From their rigorous analyses, the manager's letter developed into a monthly letter wherein one set goals, activities, and standards for each month and reported the results against the previous month's objectives. In this way, nothing was ever swept under the carpet. Targets were set, progress reported, and objectives with a specific time table were often

reset, with explanation. If the objectives spelled out in the monthly letter required another work relationship, then a copy of that letter was sent to the respective manager(s) to complete the full cycle and to allow others involved to incorporate the necessary agreed-on responsibility as part of their own monthly objectives. Once an objective was defined and scheduled in a monthly letter, it was never removed from future monthly letters until it was accomplished [Drucker, 1954, pp. 129-130; 1974, pp. 438-489; W.J. Greenwood, 1980; Smiddy, 1977].

Harold Smiddy always said that the monthly letter was actually written by the managers or "individual contributors" for their own personal guidance — not for the boss, but for self-measuring. Without it, the managers or individual contributors might not take the time to frequently measure their own performance and might therefore fail because of not having pursued timely accomplishment of their previously agreed-on objectives. Nevertheless, the scrutiny Smiddy gave to the monthly letters and his voluminous written comments led many of those who reported to him to say that "Smiddy manages by marginal notation" [W.J. Greenwood, 1979].

Early MBO Literature

Harold Koontz directs attention to the early use of MBO in his outstanding book, *Appraising Managers as Managers*, claiming that "if not indeed earlier than Drucker, the General Electric Company laid out the elements of managing by objectives in its extensive planning for decentralization in 1952-1954" [1971, pp. 45-46]. (Koontz was, at the time of his writing, unaware of the influence Drucker had in the GE philosophy and system [Koontz, 1980].) Koontz documents his contention by quoting from a GE publication of 1954 (released to the public a decade later), titled *Professional Management in General Electric, Book III: The Work of the Professional Manager*. (I will be selecting my own excerpts from that same publication.) But an earlier General Electric publication has some most interesting statements. At Smiddy's request and under his supervision, a book — *Dynamic Management Organization* — was drafted by L. Byron Cherry in early 1952 [General Electric, 1952]. Hardcover mock ups were produced, but the book was not published. The material was superseded by drafts

written by Hubert "Speed" Race and finally resulted in *Professional Management in General Electric, Book III* two years later.

Two quotations from this unpublished 1952 draft are of interest because they portray MBO and the self-control side of that concept — the most overlooked aspect of the Drucker philosophy. *Dynamic Management Organization* explains:

Effective control in every Operating Component depends on the establishment of definite goals in terms of specific dates and figures for the measurement of performances, as a stimulus toward complete achievement of stated objectives. The important factor is that every member of management should have specific goals which he agrees to attain by specific dates, and which will obligate him to examine and explain the reasons for variance or deviation. This produces the most effective form of control — self-control. [p. 78]

Later the book describes methods of control. Among the simplest, yet most effective, is:

The requirement that the management of each component formulate, for a period sufficiently long in advance, a comprehensive operating program and budget (including personnel and capital requirements) — *what* they propose to *accomplish* by *when*; *how* they propose to accomplish it; *what* it will *cost*; *what* it will *earn*; *what capital* and other resources are *required*, and their amortization. [p. 83]

This is a simple requirement for a manager to set objectives, time periods, costs, and standards against which to be measured.

It was during this period that Drucker wrote *The Practice of Management*, including the now classic chapter "Management by Objectives and Self-Control." Drucker comments:

I wrote the draft of *Practice of Management*, and especially of the parts that deal with objectives and with the manager's work, in 1951/52. In fact, I remember distinctly that "Speed" Race visited me in our summer place in Colorado in the summer of 1952, when I finished the first draft of that book. And it was then circulated among a few friends, especially Smiddy, [Fred] Borch, Cherry, and Race . . . at GE, before I started on the final revision, which was finished at Cape Cod in the summer of 1953. [1979b]

The Smiddy group, including Hubert Race and L. Byron Cherry, had read Drucker well before the Race manuscript was written. Almost every week Smiddy received drafts from first Cherry and later Race and he asked Drucker to rewrite them over the weekend. The two quotations from the 1952 Cherry draft not only are Drucker's concepts, but Drucker's words — they have his writing style. Cherry, Race, and Smiddy did not write with this flavor [W.J. Greenwood, 1979].

Shortly after the 1952 mock up was produced, the project was greatly altered and Smiddy decided that one book would not cover the material that needed to be disseminated as the General Electric Company moved from a highly centralized structure to a decentralized one. One of the reasons that Smiddy shelved the original project may have been that he had read Drucker's book in its first draft and concluded that what was developed in *Dynamic Management Organization* was simply not adequate. Smiddy clearly realized that more was needed than the traditional functional approach with which he had started the project. Drucker was pushing the GE drafts toward a conceptual structure that subordinated functions. It appears this was a direction to which Smiddy had a difficult time adjusting, because of his intense loyalty to the pioneers of management and their functional approach. The subordination of Fayol's approach and that of Smiddy's mentor Harry Hopf led to an approach with a far more rigorous conceptual framework, one that did not focus on process but on purpose. Therefore, the evolving philosophy was far removed from the engineering approach with which Smiddy had started out.

Smiddy planned a series of "texts" to explain the corporation's new philosophy. Ultimately four books were published and a fifth was written but had not reached its final stages when Smiddy retired in 1961 and the project was suspended. The series of books was entitled *Professional Management in General Electric*. The third book, mentioned earlier and subtitled *The Work of a Professional Manager*, was published in 1954. As in all the books, Smiddy wrote much of the material, led its direction, and approved every word. Hubert "Speed" Race acted as coordinator for the project and major contributions came from Smiddy's Management Consultation Services staff, then consisting of Fred Borch (later to

become Chairman of the Board and Chief Executive Officer), Paul Mills, Melvin Hurni, Tim Linville, Charles Clark, Hugh Estes, Byron Case, and William J. Greenwood. Also, contributions came from outside consultants Miles Mace of Harvard and Peter Drucker [W.J. Greenwood, 1979].

It is this third book of the series that speaks directly to the subject of MBO, but without using the actual term. A few quotations will lend support to this claim:

The manager of each division, of each department, and of each successively smaller component is responsible for seeing that objectives are established for his component which are consistent with previously stated . . . goals of the larger components of which his component is part [p. 26].

Whatever is worth planning is also worth measuring. Performance is the ultimate test. Even the most perfect planning is of little use unless it results in performance. [p. 38]

As a result of the work of planning and organization, the manager of a particular business component has established plans, forecasts, estimated schedules and budgets for the work of his component. These have been in quantitative terms with corresponding expected standards of performance specifically indicated. [p. 113]

Decentralization of managerial decision making requires that objective goals and objective measurement of progress toward these goals be substituted for subjective appraisals and personal supervision. Through a program of objective measurements, managers will be equipped to focus attention on the relevant, on trends, and on the future. To the extent, therefore, that we are able to develop sound, objective measurements of business performance, our philosophy of decentralizing authority and responsibility will be rendered more effective. [p. 133]

One does not need to be "controlled" or "commanded" if he knows what is to be done and why; if he knows, from continual measurement of results, whether the work is getting done as planned and on schedule, or if not, why not [p. 73].

William Greenwood, who worked on the project, claims that these are all Drucker rewrites [1979].

Drucker's Distinct Contribution To Management by Objectives

There seems to be some confusion as to who

authored the phrase "management by objectives." Harold Koontz believes he recalls Drucker saying Harold Smiddy may have first coined the expression. The uncertainty stems from a discussion of MBO and the manager's letter concept that Koontz and Drucker had, in which Drucker readily credited the manager's letter concept and term to Smiddy but *not* the MBO term [Koontz, 1980]. The term "management by objectives" was in fact coined by Drucker. Sometime between 1948 and 1951 the phrase evolved and Drucker often used it in his lectures.

Beyond coining the phrase, Drucker must be credited with numerous contributions to the MBO philosophy. He was intellectually first, and for a long time alone, in claiming that objectives are not given, are not obvious, are not something that everybody knows. He broke from the earlier writers who emphasized the process of management and who placed the setting of objectives within the element of planning. The basic assumptions of the traditional functional approach lacked intellectual and operational underpinning: the earlier writers *assumed* objectives. Drucker, on the other hand, found setting objectives to be the difficult, highly risk-taking aspect of the manager's job [Bonaparte, 1970, pp. 30-32; W.J. Greenwood, 1979; Ritchie, 1970, pp. 86-89].

It also appears that most earlier thinkers about objectives tried to find the *single* objective — this was Sloan's approach and for a long time Smiddy's. Drucker built management as a discipline and managing as a practice around the decision on objectives — something few others understood. Whereas the earlier systematic writers on management had talked of a process, Drucker talked of an intellectual and conceptual decision based on analysis, from which the process of managing would then flow [W.J. Greenwood, 1979].

Conclusion

In answer to the question "Did you know anybody who practiced MBO before you wrote about it?" Drucker replied:

A good many people in earlier times managed by objectives. Sloan was the first one I met, for the simple reason that he was the first significant figure in management I met personally. But I would imagine

that Pierre Du Pont, before him, started out with objectives — perhaps even more clearly than Sloan did. In those years, of course, I had not read Pierre Du Pont's papers and letters, which Chandler [1971] has made available only fairly recently. And there is no doubt in my mind that a difficult, but brilliant man — Donaldson Brown — had a very clear concept of management by objectives in mind, although he never wrote about it, to the best of my knowledge, never spoke about it, and certainly did not discuss it in his talks with me, which were focused almost entirely upon organization structure and especially on the role of staffs which, in Brown's

view, was the area in which Sloan had not really done his thinking and was woefully woolly. In other words, to manage by objectives is nothing new. [1979c]

Peter Drucker put objectives into center stage and made them the core of the structure of a discipline of managing. Many other managers probably "invented" and used an MBO concept before 1954, but it took Drucker to put it all together, think through its underlying philosophy, and then explain and advocate it in a form others could use.

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Ronald G. Greenwood is Professor of Management and Marketing at the University of Wisconsin — La Crosse.

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