The Benefits of Practicing 'Extreme Prioritization' in Your Business

By Gregory Milano

In school, many of us learned about the Pareto principle, sometimes known as the 80/20 rule, which states that roughly 20% of activities account for 80% of value created. It doesn't always hold exactly, but it generally applies in many situations, especially those involving capital markets. For example, in 2021, the top 20% of S&P 500 companies increased market capitalization by an aggregate of $7.3 trillion, which is 82% of the total for all the companies in the index, according to my own analysis of S&P's Capital IQ data. Over the past three calendar years, this figure was exactly 80%.

What does this mean for corporate leaders? If your company has 10 business units, statistically speaking, two of them likely create the vast majority of the value. As a result, companies should be deliberate about devoting outsized resources and attention to managing and growing these businesses. This is not to suggest one should ignore the other eight businesses, but rather that their needs should be subordinated to those that are doing most of the heavy lifting.

Similarly, if you only have one business, then maybe you have several product lines or customer types. In each case, I'd expect roughly 20% of them to create 80% of the value, and I believe these potential high-performers should receive more attention and resources so they can flourish and grow.

Unfortunately, I've found many leaders do the exact opposite: They devote more time and corporate resources to turning around underperformers. This is normal human behavior; as they say, "The squeaky wheel gets the grease." There is also another factor at play: the asymmetry of implications for good and bad business outcomes. Said differently, you probably won't get fired if your star business doesn't reach its full potential, as long as it generally performs well. But you might lose your job if you don't fix a poor performer. For this reason, I believe many companies are better off divesting their problematic businesses to make it easier to focus on the big winners.

What's more, many fail to understand that the opportunity cost of not reaching the star business's full potential tends to dwarf the value earned from turning around the struggling one. In a 2011 study, I found that top-quartile S&P 500 companies created an average of more than 20 times more value over a 10-year period than was destroyed, on average, in bottom-quartile companies. From my perspective, giving up only 10% of the potential success of the star is worth far more than the total value lost by the underperformer.

One of the most important corporate processes relates to the allocation of capital and other important resources, such as funds for innovation, brand building and employee training. Once again, the Pareto principle applies. I believe corporate leaders should seek to invest as heavily as they can in the investment projects that offer the biggest upside.

I use the phrase “strategic resource allocation,” or SRA, to describe this prioritization of investment projects. Managers should be encouraged to submit as many good ideas for investment as possible, and the SRA process helps navigate the returns and risks of each idea, as well as suggests an optimal set of approved investments. For the top initiatives, it can be helpful to ask what they could do if they were given even more funding than they have requested. Often, plowing more funding into desirable projects, to improve breadth and pace, can create more value than spending these same funds on an array of less beneficial investments.

The same principles can be cascaded down an organization. At the top of the house in a large company, prioritization decisions may relate to activities worth tens or hundreds of millions of dollars or more. As you delve deeper into the company, the impact of decisions generally shrinks, but the principle still applies. If there are 10 ideas on how to make a warehouse more efficient, two of them probably offer the lion’s share of the benefits. By prioritizing these two major initiatives, and not being distracted by the other eight, a team can save valuable time and increase its odds of, and payouts from, success.

There are a few telltale signs of poor prioritization. As an example, consider companies that reinforce the idea that one needs to be constantly busy to be effective. When I was an investment banker, the junior bankers went so far as to stay late into the night, even when they had no work, to create the impression of working hard. And, indeed, most of us have taken part in scores of pointless meetings, where the same talking points and analyses are rehashed time and again. When you eliminate busy work and wasteful meetings, your employees can focus on what is really important.

Extreme prioritization is important for everything from strategy development to portfolio optimization to planning and decision-making, and for all aspects of execution. Like investors who prioritize their best prospects in their investment portfolios, companies should consider better ways to prioritize their time and investment resources.

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