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THE

PERSONAL MBA



10th Anniversary Edition

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—JAMES CLEAR, author of *Atomic Habits*

JOSH KAUFMAN

Founder of PersonalMBA.com



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A NOTE TO THE READER

Clear language engenders clear thought,
and clear thought is the most
important benefit of education.

—RICHARD MITCHELL,
THE GRAVES OF ACADEME

Many people assume that they need to attend business school to learn how to build a successful business or advance in their career. That's not true. The vast majority of modern business practice requires little more than common sense, simple arithmetic, and knowledge of a few very important ideas and principles.

The Personal MBA is a foundational business book that focuses on the fundamentals. Its purpose is to give you a clear, comprehensive overview of the most important business concepts in as little time as possible.

Each idea in this book is presented in plain language. Connections between these ideas are highlighted for easy reference. Once you know the essentials, you're free to focus on building your career, secure in the knowledge that you're considering the most important matters first.

Most "MBA alternative" books try to replicate the curricula of top-tier business-school programs. That's not the focus of *The Personal MBA*. My aim is to help you build a solid understanding of general business practice from scratch, regardless of your current level of education or business experience.

Your time is valuable. I've made every effort to condense a large and

diverse topic into an approachable volume you can read in a few hours. If additional research into specific topics is prudent in your situation, you'll know what to look for and where to begin.

Knowing where to start in common business situations is valuable, whether you're an early-career professional, an entrepreneur, a skilled tradesperson, or an executive with decades of experience. Having a common language to think about what you observe opens the door to major improvements, no matter what you do for a living.

This revised and updated edition of *The Personal MBA* features many new concepts that make the book's coverage of fundamental ideas even more comprehensive. In addition, small edits have been made to improve the clarity of the concepts included in the first two editions, and additional index features have been added to enhance the book's value as a long-term reference.

If you combine reading this book with real-world experience, you'll reap the rewards for the rest of your life. I hope this book helps you make more money, get more done, and have more fun in the process.

PREFACE TO THE 2020 EDITION

It's wonderful when something that works in theory works in practice.

Fifteen years ago, I started *The Personal MBA* as a side project. I wanted to improve my business knowledge and skills in a direct, efficient, and cost-effective way. When I started the project, I was focused on pursuing a career at a large, multinational company. I had no intention of writing a book and no way of knowing that my research would go on to help hundreds of thousands of people worldwide—and change the course of my life in the process.

The Personal MBA has given readers from all walks of life—from early-career professionals just entering the workforce to skilled tradespeople, executives, and entrepreneurs—a more accurate and practical understanding of what businesses are, how they work, how to create a new business from scratch, and how to improve any existing business venture.

For better or worse, when adults decide to get serious about business education, they start looking into MBA programs. Business *degrees* are often a poor investment, but business *skills* are always useful, no matter how you acquire them.

One of the great pleasures of writing a book is hearing from readers who have benefitted from it in some way. In the ten years since *The Personal*

MBA was first published, I've heard from thousands of readers who have used the concepts in this book to start profitable businesses, land major promotions, and improve their personal and professional lives.

Dirk, who lives in Berlin, Germany, decided to learn business on his own instead of attending business school:

The Personal MBA saved me from a \$150,000 mistake and gave me a new perspective on my personal education. In 2014, I was no longer happy with my corporate career, and I was seriously considering an MBA from a top European university. Two days before I was scheduled to mail my enrollment paperwork and send my first payment, I read *The Personal MBA* . . . and I completely changed my mind. Instead of going into severe debt, I went on a personal education journey to pursue my desired career: working with start-ups. I traveled, attended conferences, and participated in programs while reading every book I could get my hands on. At a fraction of the cost and time of an MBA, I made the right contacts and learned what I needed to start my career. I've been successfully running my own company for the past five years, and I've worked with over three hundred start-ups.

Michael, who lives in the United Kingdom, used the book to advance his corporate career:

I came out of university expecting to be prepared for work . . . and I was not. I see *The Personal MBA* as the ultimate primer for continual learning. I read it at least once a month for over two years. I'm currently twenty-six, and I'm leading marketing and product management teams for one of the largest companies in the world. I'm the youngest person ever to have a seat at the leadership table. I recently passed *The Personal MBA* to a new graduate who joined the team. He read it cover to cover several times. Now, I hear a lot of feedback from the team saying that he is "wise beyond his years" and "knows how to ask the right questions." Thank you, Josh.

M. R. uses the book to manage hundreds of employees and deliver essential services to millions of people in Sri Lanka:

I purchased *The Personal MBA* from a bookstall in Malaysia three years ago. I do not have an MBA, but I am practicing management techniques I learned from your book. I have used your ideas about systems to control over \$20 million worth of inventory and ensure a smooth flow of materials. In addition, I guided a team to develop a customer support system that is now benefitting 6.2 million customers, and we have identified over 2,000 business processes to implement in a new Enterprise Resource Planning system. Congratulations, and thank you for the hard work you are doing for the benefit of millions of managers around the world.

Elizabeth in Minneapolis, Minnesota, USA is applying these ideas in her personal life:

I never thought I could become so smart without a college education. You showed me how to increase my knowledge and put that knowledge into practice, and you taught me how to succeed at nearly anything if I'm serious about it. I mentor four children, and I'm passing your legacy on to them. I'm very grateful for your work.

These stories are not unique: hundreds of thousands of readers around the world are using the ideas in *The Personal MBA* to advance in their careers, improve their lives, and make the world a better place.

It's an honor to introduce you to this essential body of knowledge, which will serve you well for the rest of your life. Learning these concepts makes it easier to do great work, make good decisions, and take full advantage of your skills, abilities, and available opportunities—no matter what you do (or would like to do) for a living.

Thank you for reading this expanded and revised tenth anniversary edition of *The Personal MBA*. I hope you find this book useful in your pursuits, and I wish you every success.

Josh Kaufman
Fort Collins, Colorado, USA
September 2020

THE PERSONAL MBA

TENTH ANNIVERSARY EDITION

Introduction

WHY READ THIS BOOK?

Just what the world needs—another business book!

—US CUSTOMS AGENT AT JOHN F. KENNEDY INTERNATIONAL AIRPORT,
AFTER ASKING ABOUT MY OCCUPATION

Life's tough. It's tougher if you're stupid.

—JOHN WAYNE, WESTERN FILM ICON

Since you're reading this book, chances are you want to make something important happen: you want to start a business, get a promotion, or create something new in the world. It's also likely that one or more things are holding you back from achieving your dream:

- ▶ *Business angst*—the feeling that you “don’t know much about business” and therefore could never start your own company or take more responsibility in your current position. Better to maintain the status quo than face your fear of the unknown.
- ▶ *Certification intimidation*—the idea that “business is complicated” and is a subject best left to trained “experts.” If you don’t have an MBA or similar expensive credentials, who are you to say you know what to do?
- ▶ *Impostor syndrome*—the fear that you’re already “in over your head” and it’s only a matter of time before you’re unmasked as a total fraud. No one likes a phony, right?

Here's the good news: everyone has these unfounded fears, and they're normal. Don't let them hold you back from pursuing what's important to you. Businesses are created, operated, and improved by ordinary people just like you; there's no magic or secret knowledge involved. All you need to do is learn a few simple concepts that will change the way you think about how businesses work and allow you to identify promising opportunities.

If you're an entrepreneur, student, tradesperson, executive, or professional who wants to master the fundamentals of sound business practice, this book is for you. No matter who you are or what you're trying to do, you're about to discover a useful new way of looking at business that will help you spend less time fighting your fears and more time doing things that make a difference.

You Don't Need to Know It All

As to methods, there may be a million and then some, but principles are few. The man who grasps principles can successfully select his own methods. The man who tries methods, ignoring principles, is sure to have trouble.

—HARRINGTON EMERSON, MANAGEMENT CONSULTANT
AND EFFICIENCY EXPERT¹

One of the most important things about learning any subject is the fact that *you don't need to know everything*—you need to understand a small set of important concepts that provide most of the value. Once you have a solid scaffold of core principles to work from, building upon your knowledge and making progress becomes much easier.

The Personal MBA is a set of foundational business concepts you can use to get things done. Understanding these fundamental principles will give you a set of tools you can rely on to make good decisions. If you invest the time and energy necessary to learn these concepts, you'll be in the top 1 percent of the human population when it comes to knowing

- ▶ How businesses actually work,
- ▶ How to start a new business,

- ▶ How to improve an existing business, and
- ▶ How to use business-related skills to accomplish your personal goals.

Think of this book as a filter. Instead of trying to absorb all of the business information that's out there—and there's a *lot* out there—use this book to help you learn what matters most, so you can focus on what's important: making things happen.

No Experience Necessary

People always overestimate how complex business is. This isn't rocket science—we've chosen one of the world's most simple professions.

—JACK WELCH, FORMER CEO OF GENERAL ELECTRIC

Don't worry if you're a complete beginner. Unlike many other business books, this book does not require any prior business knowledge or experience. I don't assume you're the CEO of a large company who makes multimillion-dollar decisions on a daily basis—but this book will still be useful if you are.

If you *do* have business experience, take it from many of my clients and readers from around the world who have MBAs from top schools—you'll find the information in this book more valuable and practical than anything you learned earning your degree.

Together, we'll explore 271 simple concepts that will help you think about business in a new and useful way. After reading this book, you'll have a more comprehensive and accurate understanding of what businesses actually are and what successful businesses actually do.

Questions, Not Answers

Education is not the answer to the question. Education is the means to the answer to all questions.

—BILL ALLIN, SOCIOLOGIST AND EDUCATION ACTIVIST

Most business books attempt to teach you to have more answers: a technique for this, a method for that. This book is different. It won't give you

answers—it will help you ask better questions. Knowing what's important in *every* business is the first step in making good business decisions. The more you know about the essential questions to ask in your current situation, the faster you'll be able to find the answers you need to move forward.

Mental Models, Not Methods

The limits of my language are the limits of my world.

—LUDWIG WITTGENSTEIN, PHILOSOPHER AND LOGICIAN

To improve your business skills, you don't need to learn everything there is to know—mastering the fundamentals can take you far. I call these foundational business concepts “mental models,” and together, they create a solid framework you can rely on to make good decisions.

Mental models are concepts that represent your understanding of how something in the world works. Think of driving a car: What do you expect when you press down on the right-side pedal? If the car slows down, you'll be surprised—that pedal is supposed to be the accelerator. The accuracy of your model of the world determines your expectations, decisions, behavior, and—in the long run—your results.

Your brain forms mental models by noticing patterns in what you experience each day. Very often, however, the mental models you form on your own aren't accurate—you're only one person, so your knowledge and experiences are limited. Education is a way to make your mental models more accurate by internalizing the knowledge and experiences other people have collected throughout their lives. The best education helps you learn to see the world in a new, more productive way.

For example, many people believe things like “Starting a business is risky,” “To get started, you must create a detailed business plan and borrow a lot of money,” or “Business is about who you know, not what you know.” Each of these phrases is a mental model, but they're not quite accurate. Correcting your mental models can help you think about what you're doing in a clear, comprehensive way, which will help you make better decisions.

INACCURATE MENTAL MODEL	ACCURATE MENTAL MODEL
Starting a business is risky.	Uncertainty is an ever-present but manageable part of business, and risks can be minimized.
In order to create a successful business, you must write a flawless business plan first.	A written plan is secondary to understanding the critical functions of your business, and no matter how much you prepare, there will <i>always</i> be surprises along the way.
You must raise large amounts of capital before you start building your business.	Raising money is necessary only if it allows you to accomplish something that would otherwise be impossible (like building a factory).
It's not what you know, it's who you know.	Personal connections are important, but knowledge is key if you want to use those connections to your best advantage.

After learning the mental models in this book, many of my readers have realized that their picture of what businesses are and how businesses work was inaccurate—getting their venture off the ground would be far easier than they originally imagined. Instead of wasting valuable time and energy feeling intimidated and freaking out, learning these concepts gave them the freedom to stop worrying and start making progress.

This book will help you learn the fundamental principles of business so you can focus your time and energy on doing useful things: creating something valuable, attracting attention, closing more sales, serving more customers, getting promoted, making more money, changing the world. Not only will you be able to create more value for others and improve your own financial situation, you'll have more fun along the way.

My Personal MBA

Self-education is, I firmly believe, the only kind of education there is.

—ISAAC ASIMOV, FORMER PROFESSOR OF BIOCHEMISTRY AT BOSTON UNIVERSITY AND AUTHOR OF MORE THAN FIVE HUNDRED BOOKS

This section describes the history of the Personal MBA as a project. You may find this context useful, but the primary value of this book is independent of my personal background. If you'd like to get to the business concepts, feel free to skip ahead to page 32.

funded via scholarships, and as a result I had the remarkable opportunity to experience most of what business schools teach without the crippling burden of debt.

I've also been on the fast track to corporate success. Through the University of Cincinnati's cooperative education program, I landed a management position at a *Fortune* 500 company—Procter & Gamble—during my second year of college. By the time I graduated in 2005, I had an offer to become an assistant brand manager in P&G's Home Care division, a role reserved for graduates of top MBA programs.

As I began my last semester of college, I started focusing less on my coursework and more on the future. My new job would require a solid understanding of business, and almost all of my peers and managers would have MBAs from top-tier schools. I briefly considered enrolling in an MBA program, but it made no sense to pursue an expensive credential to get the kind of job I already had, and my responsibilities would be demanding enough without adding a load of coursework by enrolling in a part-time program.

While considering my options, I remembered a bit of career advice that Andy Walter, the first associate director I reported to at P&G, had given me: "If you put the same amount of time and energy you'd spend completing an MBA into doing good work and improving your skills, you'll do

P

eople often ask me if I have an MBA. "No," I reply, "but I did go to business school."

As a student at the University of Cincinnati, I was fortunate enough to participate in the Carl H. Lindner Honors-PLUS program, which resembles an MBA at the undergraduate level. The program was

just as well.” (Andy doesn’t have an MBA—he studied electrical engineering in college. He retired as one of the company’s top global IT executives, responsible for leading many of P&G’s largest projects.)

In the end, I decided to skip business school, but not business *education*. Instead of enrolling in an MBA program, I hit the books, creating my own personal MBA.

A Self-Directed Crash Course in Business

Many who are self-taught far excel the doctors, masters, and bachelors of the most renowned universities.

—LUDWIG VON MISES, AUSTRIAN ECONOMIST
AND AUTHOR OF *HUMAN ACTION*

I’ve always been an avid reader, but before I decided to learn everything I could about business, most of what I read was fiction. I grew up in New London, a small farm town in northern Ohio where the major industries are agriculture and light manufacturing. My mother worked as a librarian, and my father was a sixth-grade science teacher, then an elementary school principal. Books were a major part of my life, but business was not.

Before getting my first real job, I knew next to nothing about what businesses were or how they functioned, other than that they were places people went every day in order to draw a paycheck. I had no idea that companies like Procter & Gamble existed until I applied for the job that swept me into the corporate world.

Working for P&G was an education in itself. The size and scope of the business—and the complexity of managing a business of that size—boggled my mind. During my first three years with the company, I participated in making decisions across every part of the business process: creating new products, ramping up production, allocating millions of marketing dollars, and securing distribution with major retailers like Walmart, Target, Kroger, and Costco.

As an assistant brand manager, I was leading teams of thirty to forty P&G employees, contractors, and agency staff—all of whom had competing projects, plans, and priorities. The stakes were huge, and the pressure

was intense. To this day, I can't help but marvel at the thousands of man-hours, the millions of dollars, and the complex processes necessary to make a simple bottle of dish soap appear on the shelf of the local supermarket. Everything from the shape of the bottle to the scent of the product is optimized—including the text on the cardboard boxes used to ship inventory to the store.

My work at P&G, however, wasn't the only thing on my mind. My decision to skip business school in favor of educating myself developed from a side project into a minor obsession. Every day I would spend hour after hour reading and researching, searching for one more tidbit of knowledge that would help me to better understand how the business world worked.

Instead of using the summer after graduation to relax and go on vacation, I spent my days haunting the business stacks at the local bookstore, absorbing as much as I could. By the time I officially started working full-time for P&G in September 2005, I had read books spanning every discipline that business schools teach, as well as disciplines that most business schools don't cover in detail, such as psychology, physical science, and systems theory. When my first day at P&G finally arrived, I felt prepared.

As it turned out, my self-education served me well—I was doing valuable work, making things happen, and getting good annual reviews. As time went on, however, I realized three very important things:

1. *Large companies move slowly.* Good ideas often died on the vine because they had to be approved by too many people.
2. *Climbing the corporate ladder is an obstacle to doing great work.* I wanted to focus on getting things done and making things better, not drafting memos, sitting in meetings, and positioning myself for promotion. Politics and turf wars are an inescapable part of the daily experience of working for a large company.
3. *Frustration leads to burnout.* I wanted to enjoy the daily experience of work, but instead I felt like I was running a gauntlet each day. It began to affect my health, happiness, and relationships. The longer I stayed in the corporate world, the more I realized I wanted out. I wanted to decide what to work on, who to work with, and what to prioritize—making entrepreneurship the best path for me long-term.

The Wheat and the Chaff

It is important that students bring a certain ragamuffin, barefoot irreverence to their studies; they are not here to worship what is known, but to question it.

—JACOB BRONOWSKI, WRITER AND PRESENTER OF *THE ASCENT OF MAN*

If there's one thing I'm good at, it's taking in an enormous amount of information and distilling it to the essentials. Even so, sifting through the massive amount of business information available was a huge challenge: thousands of new business books are published every year, and business periodicals, journals, and websites publish new research daily. Some of this information is useful, but most of it is not.

My early business research was haphazard—I went to a bookstore and picked up any book that looked interesting. For every great book I found, I had to wade through ten times as many low-quality texts written by authors who were more interested in creating a three-hundred-page business card than providing useful information.

I started to wonder how much of what's out there—and there's a *lot* out there—I *really* needed to know. How could I separate the valuable information from the rubbish? I only had so much time and energy, so I started searching for a filter: something that would direct me to the useful knowledge and keep me away from the chaff. The more I searched, the more I realized it didn't exist—so I decided to create it myself.

I began tracking which resources were valuable and which ones weren't, then publishing my findings on my website, both as an archive and for the benefit of anyone interested. It was a personal project, nothing more: I was just a recent college graduate doing my best to learn something useful, and publishing my research for others seemed like a good use of time and energy.

One fateful morning, however, the Personal MBA went public—and became much more than a personal project.

The Personal MBA Goes Global

Whoever best describes the problem is the one most likely to solve it.

—DAN ROAM, AUTHOR OF *THE BACK OF THE NAPKIN*

In addition to reading books, I was following several hundred business blogs. Some of the best business thinking was being published on the internet months (or years) before it ever appeared in print, and I wanted to read it all as soon as it was available.

One of the bloggers I followed was Seth Godin. A bestselling author (of books like *Permission Marketing*, *Purple Cow*, and *Linchpin*) and one of the earliest successful online marketers, Seth specializes in bold statements of big ideas designed to challenge you to do more, do better, question the status quo, and make a difference.

One particular morning, Seth was commenting on a recent news story: Harvard was rescinding the admission of 119 previously soon-to-be Harvard MBA students.² These prospective students had discovered a way to hack into the Harvard admissions website to view their application status before the official acceptance letters went out. The story became a media frenzy, devolving into a debate about whether MBA students were predisposed to lie, cheat, and steal, or if business schools made them that way.

Instead of being outraged at the bad behavior of the applicants, Seth had a different perspective: Harvard was giving these students a *gift*. By rescinding their admission, the university was returning \$150,000 and two years of their lives that would otherwise have been spent chasing a piece of paper. “It’s hard for me to understand,” he wrote, “why [getting an MBA] is a better use of time and money than actual experience combined with a dedicated reading of 30 or 40 books.”

I experienced a moment of unexpected validation, then got to work.

Over the next two days, I created a list of the books and resources I had found most valuable in my studies,³ then published it on my website with a link to Seth’s post, so anyone interested in figuring out how to do what Seth suggested would be able to find it. When it was done, I sent Seth an email with a note of thanks and a link to my post.

Two minutes later, a post went up on Seth’s blog directing people to my

reading list, and a flood of readers from around the world began visiting my website.

Popular personal-development and productivity blogs and sites like Lifehacker picked up the story, which then spread to social media websites and a wide variety of personal blogs. In the first week of the Personal MBA's existence, thirty thousand people visited my little corner of the internet to see what I was doing. Better yet, they started talking.

Some readers asked questions—where should they start? Others suggested great books they'd read, helping me with my research. A few told me the entire project was naive and that I was wasting my time. Through it all, I kept reading, researching, and developing the Personal MBA in my spare time, and the business self-education movement began to snowball.

In a very short time, the Personal MBA grew from a one-man side project into a global phenomenon. The site, personalmba.com, has been visited by millions of readers since it went live in early 2005, and the project has been featured by the *New York Times*, the *Wall Street Journal*, *Bloomberg Businessweek*, the *Financial Times*, *Time*, *Fortune*, *Fast Company*, and hundreds of other major news organizations and independent websites. In late 2008, I left P&G to focus on research, writing, and improving the Personal MBA full-time.

As much as I enjoyed the interest in my reading list, I soon realized that providing a reading list wasn't enough. People read business books to solve specific challenges or to improve themselves in some tangible way. They're looking for solutions, and a list of books—while valuable—could only do so much.

The books themselves aren't as important as the ideas and knowledge they contain, but many of my readers were missing out because it took hours of turning pages to get to the good stuff. Many readers started with enthusiasm, only to quit after reading a few books—it took too long to reap the rewards, and the demands of work and family life prevented many readers from completing the project.

To help them, I had more work to do.

Munger's Mental Models

I think it's undeniably true that the human brain works in models. The trick is to have your brain work better than the other person's brain because it understands the most fundamental models—the ones that do the most work.

—CHARLES T. MUNGER, BILLIONAIRE BUSINESS PARTNER OF
WARREN BUFFETT, FORMER CEO OF WESCO FINANCIAL, AND
VICE-CHAIRMAN OF BERKSHIRE HATHAWAY



My first glimpse into the future of the Personal MBA came when I discovered the work of Charlie Munger.

Charlie was born in Omaha, Nebraska, just before the Great Depression. As a young man, Charlie skipped high school athletics in favor of reading to satisfy his intense curiosity about how the world worked. His early business experience consisted of working in a family-owned grocery store for \$2 a day.

In 1941, Charlie graduated from high school. After two years of studying undergraduate mathematics and physics at the University of Michigan, he enlisted in the US Army Air Corps, where he was trained as a meteorologist. In 1946, after leaving the army, he was accepted to Harvard Law School, even though he had never earned a bachelor's degree, which wasn't required at the time.

Charlie graduated from Harvard Law in 1948 and spent the next seventeen years practicing as an attorney. In 1965, he left the law firm he had created to start an investment partnership, which went on to outperform the market by 19.8 percent compounded annually over fourteen years—an astounding record given his complete lack of formal business education.⁴

Charlie Munger isn't a household name, but most people have heard of Warren Buffett, Charlie's business partner. Munger joined Buffett at Berkshire Hathaway, a floundering textile manufacturer turned investment holding company, in 1978. Together, Buffett and Munger became billionaires.

According to Buffett, Charlie's mental model-centric approach to business is a major contributing factor in the success of Berkshire Hathaway and Buffett's status as one of the world's wealthiest business owners. In Buffett's words: "Charlie can analyze and evaluate any kind of deal faster

and more accurately than any man alive. He sees any valid weakness in sixty seconds. He's the perfect partner.”⁵

The secret to Charlie's success is a systematic way of understanding how businesses work. Even though he never studied business in college, his relentless self-education in a wide variety of subjects allowed him to construct what he called a “latticework of mental models,” which he then applied to making business decisions:

I've long believed that a certain system—which almost any intelligent person can learn—works way better than the systems most people use [to understand the world]. What you need is a latticework of mental models in your head. And, with that system, things gradually fit together in a way that enhances cognition.

Just as multiple factors shape every system, multiple mental models from a variety of disciplines are necessary to understand that system . . . You have to realize the truth of biologist Julian Huxley's idea that “Life is just one damn relatedness after another.” So you must have all the models, and you must see the relatedness and the effects from the relatedness . . .⁶

It's kind of fun to sit here and outthink people who are way smarter than you are because you've trained yourself to be more objective and more multidisciplinary. Furthermore, there is a lot of money in it, as I can testify from my own personal experience.⁷

By basing their investment decisions on their extensive knowledge of how businesses work, how people work, and how systems work, Buffett and Munger created a company worth more than \$500 billion—an astounding track record for a meteorologist-turned-lawyer from Omaha with no formal business education.

Discovering Munger's approach to business education was a revelation. Here was a man who, decades before, had decided to do what I was doing—and it had worked beyond all expectation. Munger's method of identifying and applying fundamental principles made much more sense to me than most of the business books I'd read. I decided to learn everything I could about the mental models Charlie Munger used to make decisions.

Charlie has never published a comprehensive collection of his mental models. He's given hints in his speeches and essays—even going so far as to publish a list of the psychological principles he finds most useful in *Poor Charlie's Almanack*, a 2005 biography—but there is no single text that contains Charlie's conception of “everything you need to know in order to succeed in business.”

If I wanted to understand the fundamental principles of how every successful businessperson works, I'd have to discover them myself. To do that, I had to rebuild my understanding of business from the ground up.

Connecting the Dots

In all affairs, it's a healthy thing now and then to hang a question mark on the things you have long taken for granted.

—BERTRAND RUSSELL, RENOWNED PHILOSOPHER AND
AUTHOR OF *THE PROBLEMS OF PHILOSOPHY*
AND THE PRINCIPLES OF MATHEMATICS

Most business books—and business schools—assume that the student already knows what businesses are, what they do, and how they work—as if it were the most obvious thing in the world. It's not. Business is one of the most complex and multidisciplinary areas of human experience, and trying to understand how businesses work can be difficult, even though they surround us every day.

Businesses are so much a part of daily life that it's easy to take the business world for granted. Day after day, businesses deliver what we want and need with little fanfare or fuss. Look around: almost every material good you're surrounded by right now was created and delivered to you by some sort of business.

Businesses create and deliver so many different things in so many different ways that it makes generalizations difficult: What do apple cider and airlines have in common? As it turns out, quite a bit—if you know where to look.

Here's how I define a business:

Every successful business (1) creates or provides something of value that (2) other people want or need (3) at a price they're willing to pay, in a way that (4) satisfies the purchaser's needs and expectations,

and (5) provides the business sufficient revenue to make it worthwhile for the owners to continue operation.

Take away any of these things—value creation, customer demand, transactions, value delivery, or profit sufficiency—and you have something other than a business. Each factor is both essential and universal.

As I researched each of those factors in detail, I found additional universal requirements. Value can't be created without understanding what people want (market research). Attracting customers first requires getting their attention, then making them interested (marketing). In order to close a sale, people must trust your ability to deliver on what's promised (value delivery and operations). Customer satisfaction depends on exceeding the customer's expectations (customer service). Profit sufficiency requires bringing in more money than is spent (finance).

These tasks aren't rocket science, but they're always necessary, no matter who you are or what business you're in. Do them well and your business thrives. Ignore them and you won't be in business very long.

Every business relies on two additional factors: people and systems. Every business is created by people and survives by benefiting other people in some way. To understand how businesses work, you must have a firm understanding of how people tend to think and behave—how humans make decisions, act on those decisions, and communicate with others. Recent advances in psychology and neuroscience are revealing why people do the things they do, as well as how to improve our own behavior and work in a more efficient and effective way with others.

Systems, on the other hand, are the invisible structures that hold every business together. At the core, every business is a collection of processes that can be *repeated* to produce a particular result. By understanding how complex systems work, it's possible to find ways to improve existing systems, whether you're dealing with a marketing campaign or an automotive assembly line.

Before writing this book, I spent several years testing its principles with my clients and readers. Understanding and applying these mental models of business has helped them launch new careers, land job offers from prestigious organizations in corporate and academic fields, land promotions and pay raises, start new businesses, and, in several cases, go through the entire product development process (from idea to first sale) in weeks instead of years.

These concepts are important because they *work*. Not only will you be able to create more value for others and improve your career, you'll find it easier to achieve what you set out to do—and you'll have more fun along the way.

For the Skeptics

You wasted \$150,000 on an education you could have got for a buck fifty in late charges at the public library.

—MATT DAMON AS WILL HUNTING, *GOOD WILL HUNTING*

This section examines the benefits and detriments of traditional business school programs versus learning business concepts outside of academia. If you have already enrolled in business school, have completed an MBA program, or don't care about the current state of business academia, this section won't be as valuable for you. Feel free to skip ahead to page 32.

This is a book about business concepts, not business schools. However, many people don't believe it's possible to reap the benefits of a comprehensive business education without forking over enormous sums of money for a name-brand diploma from an Ivy League school. This section, which will discuss the merits and downfalls of traditional MBA programs, is for the skeptics.

Should You Go to Business School?

There is a difference between (A) what an MBA does to help you prove your abilities to others and (B) what getting an MBA actually does to improve your abilities.

—SCOTT BERKUN, AUTHOR OF *MAKING THINGS HAPPEN AND THE MYTHS OF INNOVATION*

Every year, millions of individuals determined to make a name for themselves have the following thought: "I want to become a successful businessperson. Where should I get my MBA?" Since you're flipping through this book, you've probably wondered the same thing at some point in your life.

Here's the answer: five simple words that will save you years of effort and hundreds of thousands of dollars:

Skip business school. Educate yourself.

This book will show you how to succeed in business—without mortgaging your life.

Three Big Problems with Business Schools

College: two hundred people reading the same book. An obvious mistake. Two hundred people can read two hundred books.

—JOHN CAGE, SELF-TAUGHT WRITER AND COMPOSER

I have nothing against people who work in business schools: by and large, business-school professors and administrators are lovely people who try their best and want to see their students succeed. MBA programs, however, have three major systemic issues:

1. *MBA programs have become so expensive you must mortgage your life to pay the price of admission.* Return on investment is always related to how much you spend, and after decades of tuition increases, MBA programs have become a burden to their students instead of a benefit. The primary question is not whether attending a university is a positive experience: it's whether or not the experience is worth the cost.⁸
2. *MBA programs teach many worthless, outdated, even outright damaging concepts and practices*—assuming your goal is to build a successful business and increase your net worth. Many of my MBA-holding readers and clients come to me after spending tens (sometimes hundreds) of thousands of dollars learning the ins and outs of complex financial formulas and statistical models, only to realize that their MBA program didn't teach them how to start or improve a real, operating business. That's a problem—graduating from business school does not guarantee having a useful working knowledge of business when you're done, which is what you need to be successful.

3. *MBA programs won't guarantee you a high-paying job, let alone make you a skilled manager or leader with a shot at the executive suite.* Developing skills such as decision making, management, and leadership takes real practice and experience, which business schools can't provide in the classroom, regardless of how prestigious the program is.

Instead of spending huge sums of money to learn information of questionable value, you can spend your time and resources learning business concepts that matter. If you're ready and able to invest in improving your skills and abilities, you can learn everything you need to know about business on your own, without mortgaging your life for the privilege.

Delusions of Grandeur

The very substance of the ambitious is merely the shadow of a dream.

—WILLIAM SHAKESPEARE, *HAMLET*

It's easy to figure out why business school is attractive: it's sold as a one-way ticket to a prosperous and comfortable life. It's a pleasant daydream to think that after two years of case studies and happy-hour "networking," corporate recruiters will be shamelessly throwing themselves at you, each of them offering a prestigious and high-paying position at a top firm.

Your rise up the corporate ladder will be swift and sure. You'll be a CAPTAIN OF INDUSTRY, collecting huge bonuses and tabulating the value of your stock options while sitting behind an impressive-looking mahogany desk in the corner office on the top floor of a gigantic glass skyscraper. You'll be the big boss, telling other people what to do until it's time to go play golf or relax on your yacht. You'll be wined and dined all over the world, and the lowly masses will venerate you and your astounding achievements. Everyone will think you're rich, intelligent, and powerful—and they'll be damned right.

What price for the promise of riches, power, and glory? A few thousand dollars in application fees, an effortless scribble on a loan document, and you'll be on your way to the top! Not only that, you'll get a two-year vacation from your day job. What a fantastic deal!

Daydreams and reality are often quite different.

Your Money AND Your Life

There ain't no such thing as a free lunch.

—ROBERT A. HEINLEIN, AUTHOR OF *STRANGER IN A STRANGE LAND* AND *THE MOON IS A HARSH MISTRESS*

For the moment, let's assume you think business school is your ticket to everlasting success. You're in luck—getting into at least one business school is close to guaranteed. If you pay thousands of dollars in application fees, write enough personal statements that strike just the right balance of confidence and humility, and compliment the quality of the school's program in interviews, sooner or later some college or university will bestow upon you the chance to become the next Bill Gates.⁹

Here, though, is where the problems begin: business school is expensive and is getting more expensive each year. Unless you're already wealthy or you land a massive scholarship, your only option is to secure a loan against your future earnings to pay the tuition.

Most prospective MBA students have already graduated from college with an undergraduate degree, so they're often already carrying some level of student loan debt. According to the Institute for College Access and Success—a higher education availability and affordability nonprofit—the average cumulative debt of a student who completed an undergraduate degree in the United States in 2017 is \$28,650.¹⁰ For students who choose to pursue an MBA program after undergrad, the total average student loan balance is \$66,300.¹¹ Tuition isn't the only reason graduate students borrow money: day-to-day material needs like rent, groceries, and transportation costs are often funded via student loans.

Sixty-six thousand dollars is a significant chunk of change, assuming you go to an *average* school—but who wants to be average? If you're shooting for offers from top-tier financial-services companies like Goldman Sachs or major consulting companies like McKinsey and Bain (which are historically the highest-paying options for newly minted MBAs), you're going to have to attend a top-ten program, and that'll require a *lot* more than a measly sixty-six grand.

Breaking Out the Benjamins

Who goeth a borrowing, goeth a sorrowing . . . A fool and his money are soon parted.

—THOMAS TUSSER, SIXTEENTH-CENTURY ENGLISH FARMER AND POET

At the time of publication, top MBA programs charge \$50,000 to \$80,000 *per year* for tuition.¹² That amount doesn't include fees, student loan interest, or living expenses and is increasing by 5 to 10 percent each year.

It gets worse. According to data compiled by Poets&Quants, a business-school news website, nine business schools exceed \$200,000 in direct costs for their two-year, full-time program: Harvard, Stanford, Wharton, NYU, Columbia, Dartmouth, Chicago, MIT, and Northwestern.¹³ Tack on 1 to 3 percent in loan origination fees and a 6 to 10 percent compound annual interest rate on the loan balance, plus living expenses in a major metropolitan area and the money you're not earning while in school, and you've calculated the true cost of enrollment. Once you account for everything, the total cost of a top graduate-level business degree can exceed \$400,000. Even if you assume a six-figure salary after graduation, the total cost of the degree is a substantial percentage of your future career earnings.

That's assuming you get in, of course—business-school admissions are famous for their competitive selection processes for a reason. The reputation of a business school is built on the success of its graduates, so schools have a direct incentive to admit students who already have what it takes to succeed, MBA or no MBA.

In addition, top schools rely on high-profile donors, well-heeled graduates, and corporate connections to raise funds, recruit future students, and expand their campuses. As a result, wealthy and well-connected applicants are more likely to receive acceptance letters.¹⁴ According to a *Bloomberg Businessweek* survey that polled business graduates from 126 business schools, 44 percent of students reported that they did not borrow money to pay for their degree.¹⁵ That figure doesn't make sense until you consider other forms of financial support: preexisting family wealth, donor admissions, and corporate sponsorship.

Business schools don't *create* wealthy and well-connected people. They *accept* them, then take credit for their success.

If you get in, the school will do what it can to help you get a well-paying job within a few months of graduation, but making things happen will always be *your* responsibility. If you're successful in the years after graduation, the school will hold you up as a shining example of the quality of their program and will use the "halo effect" of your name to recruit more students. If you lose your job and go broke, you'll get neither publicity nor help, but the loan bills will keep rolling in. Sorry about your luck.

Here's what Christian Schraga, a 2002 graduate of the University of Pennsylvania's Wharton School, had to say about his MBA experience in an essay on his website:¹⁶

My been-there-done-that experience has taught me that a top MBA program provides some benefits, but at a steep price. If you are currently considering attending a full-time program, please stop to ask yourself whether or not you are willing to take the risk.

Business school is a big risk. Should you choose to enroll, the only certainty is that you will shell out about \$125,000. Such a figure correlates to a \$1,500/month non-deductible loan repayment and a ten-year period of time in which you will not be able to save a red cent.

If you think that this payment is worth it to earn the pedigree, the fraternity, the two years off, and a shot at the big bucks, then the MBA is right for you. If not, please do something else.

Wise words. If you don't need the sheepskin, don't enroll.

What an MBA Will Actually Get You

Hypocrisy can afford to be magnificent in its promises; for never intending to go beyond promises, it costs nothing.

—EDMUND BURKE, POLITICIAN AND POLITICAL THEORIST

In "The End of Business Schools? Less Success Than Meets the Eye," a study published in *Academy of Management Learning & Education*,¹⁷ Jeffrey Pfeffer of Stanford University and Christina Fong of the University of Washington analyzed forty years of data in an effort to find evidence that

business schools make their graduates more successful. Their hypothesis was straightforward:

If an MBA education is useful training for business, then the following should be true as a matter of logic: (1) having an MBA degree should, other things being equal, be related to various measures of career success and attainment, such as salary; and (2) if what someone learns in business school helps that person be better prepared for the business world and more competent in that domain—in other words, if business schools convey professionally useful knowledge—then a measure of how much one has learned or mastered the material, such as grades in course work, should be at least somewhat predictive of various outcomes that index success in business.

What Pfeffer and Fong found was astonishing and disturbing: business schools do almost nothing, aside from making money disappear from students' pockets.

Business schools are not very effective: Neither possessing an MBA degree nor grades earned in courses correlate with career success, results that question the effectiveness of schools in preparing their students. And, there is little evidence that business school research is influential on management practice, calling into question the professional relevance of management scholarship.

According to Pfeffer and Fong's study, it doesn't matter if you graduate at the top of your class with a perfect 4.0 GPA or at the bottom with a barely passing grade—getting an MBA has zero correlation with long-term career success. None.

There is scant evidence that the MBA credential, particularly from non-elite schools, or the grades earned in business courses—a measure of the mastery of the material—are related to either salary or the attainment of higher level positions in organizations. These data, at a minimum, suggest that the training or education component of business education is only loosely coupled to the world of managing organizations.

The disconnect between the classroom and the working world makes sense when you realize that the concepts, principles, and techniques most business schools teach were designed for a very different world. Graduate schools of business started popping up at the end of the nineteenth century, during the second Industrial Revolution. The intent of early MBA programs was to train managers to be more scientific in an effort to make large operations more efficient.

Frederick Winslow Taylor, the pioneer of “scientific management” techniques that now form the foundation of modern management training, used a stopwatch to shave a few seconds off the average time a workman took to load iron ingots into a train car. That should give you a good idea of the underlying mind-set of most business-school management programs.

Management was thought of as an exercise in getting people to work faster and do what they’re told. The philosopher-kings behind what passed for management psychology were Ivan Pavlov and, later on, B. F. Skinner, who believed that if you discovered and applied just the right stimulus, people would behave however you wanted. This mentality led to the widespread use of financial incentives to influence behavior: salary, bonuses, stock options, and so on, in an effort to encourage business professionals and managers to act in the best interest of corporate shareholders.

There’s an enormous (and growing) body of evidence that direct incentives often undermine performance, motivation, and job satisfaction in the real world.¹⁹ Despite more useful competing theories of human action,²⁰ the search for the magic stimulus continues in business-school classrooms to this day.

In Search of Distribution

Any technique, however worthy and desirable, becomes a disease when the mind is obsessed with it.

—BRUCE LEE, WORLD-RENNOWNED MARTIAL ARTIST

Marketing, on the other hand, was originally a way to get additional store distribution for physical products and keep expensive factory production lines busy. With the widespread adoption of radio and television in the

early twentieth century, it became possible to advertise to a large, national audience, paving the way for national brands and national retailers. More advertising resulted in more distribution, which, in turn, resulted in more sales and even more money to spend on advertising, continuing the cycle. As decades passed, this self-reinforcing feedback loop resulted in a few dominant behemoths in each industry. Business schools became obsessed with how to capture market share and create gigantic companies via ever-larger mergers, raising the financial stakes with each acquisition.

For entrepreneurs, venture capital became a must-have aspect of the business-creation process—how else could you afford to build a factory or a national brand in a few short years? Economies of scale in production meant large companies could outcompete smaller rivals by offering similar products at lower prices. Investors wanted to see huge returns on their money—prudence be damned—rewarding speculators who wrote business plans promising a huge exit in a short amount of time. Viable businesses were acquired and gutted in the name of conglomeration and “synergy,” all with the blessing of business academia. The sheer enormity of integrating these gigantic, complex business systems was ignored or overlooked, leading most of the companies that attempted such huge mergers to ruin.

Playing with Fire

Beware of geeks bearing formulas.

—WARREN BUFFETT, CHAIRMAN AND CEO OF BERKSHIRE HATHAWAY
AND ONE OF THE WEALTHIEST INDIVIDUALS IN THE WORLD

Finance, in the meantime, increased in complexity. Before the twentieth century, accounting and finance were a matter of common sense and relatively simple arithmetic. The widespread adoption of double-entry bookkeeping (a thirteenth-century innovation) brought many benefits, including increased accuracy and ease of detecting anomalies like theft, at the cost of simplicity.

The introduction of statistics to financial practice enhanced analytical capability at the cost of abstraction, increasing opportunities to fudge the numbers without anyone noticing. Over time, managers and executives

began using statistics and analysis to forecast the future, relying on databases and spreadsheets in much the same way ancient seers relied on tea leaves and goat entrails. The world itself is no less unpredictable or uncertain: as in the olden days, the signs only “prove” the biases and desires of the soothsayer.

The complexity of financial transactions and the statistical models those transactions relied upon continued to grow until few practitioners fully understood how they worked or respected their limits. As *Wired* revealed in a February 2009 article, “Recipe for Disaster: The Formula That Killed Wall Street,” the inherent limitations of financial formulas such as the Black-Scholes option pricing model, the Gaussian copula function, and the capital asset pricing model (CAPM) played a major role in the tech bubble of 2000 and the housing-market and derivatives shenanigans behind the 2008 recession.

Learning how to use complicated financial formulas isn’t the same as learning how to run a business. Understanding *what businesses do to create and deliver value* is essential knowledge, but many business programs have de-emphasized value creation and operations in favor of finance and quantitative analysis. In a *New Republic* article, “Upper Mismanagement,” journalist Noam Scheiber explores the reasons behind the downfall of American industry:

Since 1965, the percentage of graduates of highly ranked business schools who go into consulting and financial services has doubled, from about one-third to about two-thirds. And while some of these consultants and financiers end up in the manufacturing sector, in some respects that’s the problem . . . Most of GM’s top executives in recent decades hailed from a finance rather than an operations background. [. . .] But these executives were frequently numb to the sorts of innovations that enable high-quality production at low cost.²¹

Process improvements are easy to skip if you want the business’s short-term profit numbers to look good, even though they’re essential to long-term viability. By ignoring the things that make a business operate in an effective and sustainable way, MBA-trained executives have gutted viable companies in the name of quarterly earnings per share.

Meanwhile, the widespread practice of using large amounts of debt as leverage²² created enormous companies with even more enormous obligations, amplifying returns in good years but making the firms catastrophically unstable during the slightest downturn. The “leveraged buyout” strategy taught in many business-school classrooms—buying a company, financing massive expansion via debt, then selling the business to another company at a premium²³—turned formerly self-sustaining companies into debt-bloated monstrosities, and the constant flipping of businesses from one temporary owner to the next turned financial markets into a game of musical chairs.

When financial wizardry and short-term returns overshadow prudence and long-term value creation, customers and employees suffer. The only people who benefit are the MBA-trained, executive-level financiers and fund managers running the show, who extract hundreds of millions of dollars in transaction fees and salaries while destroying viable companies, hundreds of thousands of jobs, and billions of dollars of value.

Business is about creating and delivering value to paying customers, not orchestrating legal fraud. Unfortunately for us all, business schools have de-emphasized the former in favor of teaching the latter.

No Reason to Change

Schools teach the need to be taught.

—IVAN ILLICH, PRIEST, THEOLOGIAN, AND EDUCATION CRITIC

The world is changing, but business schools aren’t changing with it. With the advent of the internet and the widespread availability of new technologies, successful modern businesses tend to be smaller, require less capital to build, have less overhead, and require fewer employees. According to the US Small Business Administration, small businesses represent 99.9 percent of all firms in the United States,²⁴ employ close to half of all private-sector workers,²⁵ have generated 64.9 percent of net new jobs from 2000 to 2018,²⁶ and represent approximately 44 percent of US gross domestic product (GDP).²⁷ You wouldn’t know that from looking at business

school curricula: based on current standards, it seems that most MBA programs believe huge businesses are the only ventures worth managing.

Mass-market advertising is no longer able to convert pennies to dollars in a predictable and reliable way. Inventories (if they exist at all) tend to be smaller, businesses depend on others for critical functions, and industries change and adapt to new developments. Speed, flexibility, and ingenuity are the qualities that successful businesses rely on today—qualities that the corporate giants struggle to acquire and retain and business-school classrooms struggle to teach.

The demands of the stock market push executives to chase short-term earnings at the expense of long-term stability, creating waves of layoffs and severe budget cuts when times get tight or unexpected events occur. At the same time, employees are looking for a greater sense of autonomy, flexibility, and security from their work—and they're finding these things outside of the confines of the traditional corporate job. How do you manage someone who doesn't want to work for you in the first place?

MBA programs are trying to cope, but they're still teaching theories that are outdated, misguided, and even outright wrong, and they have little incentive to change. Why bother, when MBA programs are profitable status symbols for universities and in such high demand? As long as students are still signing up, don't expect business schools to change their approach to business instruction.

The Single Benefit of Business Schools

Institutions will try to preserve the problem to which they are the solution.

—CLAY SHIRKY, PROFESSOR AT NYU AND AUTHOR OF
HERE COMES EVERYBODY AND *COGNITIVE SURPLUS*

The one significant benefit that business schools *do* provide is better access to *Fortune* 500 recruiters, consulting firms, large accounting firms, and investment banks via on-campus recruiting and alumni networks. Upon graduating from a top-tier business school, you'll find it much easier to get an interview with a corporate recruiter who works for a *Fortune* 500 com-

provide most of the benefits of business education at a fraction of the cost. Instead of wasting your time and hard-earned money learning outdated theories you'll probably never use, it's far better to spend your time and energy teaching yourself what you need to know to succeed.

If you're the type of person who's capable of getting into a top MBA program and doing what it takes to succeed after graduation, skipping business school and learning the fundamentals of business by reading this book may be the best decision you ever make.

What You'll Learn in This Book

When you first start to study a field, it seems like you have to memorize a zillion things. You don't. What you need is to identify the core principles—generally three to twelve of them—that govern the field. The million things you thought you had to memorize are simply various combinations of the core principles.

—JOHN T. REED, REAL ESTATE INVESTOR AND AUTHOR OF *SUCCEEDING*

This book is designed to teach you the fundamentals of sound business practice. Here's a quick preview of what you'll learn:

How businesses work. A successful business, roughly defined, provides (1) something of value that (2) other people want or need at (3) a price they're willing to pay, in a way that (4) satisfies the customer's needs and expectations so that (5) the business brings in sufficient profit to make it worthwhile for the owners to continue operation. Together, the concepts in chapters 1 to 5 describe how every business operates and what you can do to improve your results.

How people work. Every business is created by people and survives by benefiting other people. To understand how businesses work, you need a firm understanding of how people make decisions, act on those decisions, and communicate with others. Chapters 6 to 8 introduce you to a few major concepts in psychology that describe how the human mind processes the world, how you can work in a more effective and efficient way, and how you can create and strengthen professional relationships.

How systems work. Businesses are complex systems with many moving parts that exist within even more complex systems like industries, societies, cultures, and governments. Chapters 9 to 11 will help you understand how complex systems work, as well as help you analyze existing systems and find ways to improve them without provoking unanticipated consequences.

Here are a few things you *shouldn't* expect:

Management and leadership overload. Many business resources (and all business schools) conflate management and leadership skills with business skills; *they're not the same thing.* While management and leadership are important in the practice of business, they aren't the be-all and end-all of business education: without solid business knowledge, it's possible to organize and lead a group of people toward the accomplishment of the wrong objectives. Business is about the profitable creation and delivery of valuable offers to paying customers; management and leadership are a means to this end. We'll discuss the essentials of effective management and leadership in chapter 8, but in their proper context.

CFA/CPA-level finance and accounting. Finance and accounting are very important topics, and we'll discuss the essential concepts and practices in chapter 5, including common mistakes and pitfalls. That said, we have many topics to explore, and finance is not the sole focus of this book. Deep examinations of financial analysis and accounting standards have filled thousands of books much longer than this one, and unless you plan on becoming a chartered financial analyst (CFA) or a certified public accountant (CPA), you should learn the basics of these topics, but leave the details to the specialists.

Fortunately, there's no need to reinvent the wheel: great books on finance and accounting already exist. If you're interested in exploring these topics in more detail after completing chapter 5, I recommend the following books:

Financial Intelligence for Entrepreneurs by Karen Berman and Joe Knight

Simple Numbers, Straight Talk, Big Profits! by Greg Crabtree

Accounting Made Simple by Mike Piper

How to Read a Financial Report by John A. Tracy

In addition, online courses like MBA Math (<http://mbamath.com>) and Bionic Turtle (<http://bionicturtle.com>) are available if you want to explore these topics in even greater depth. (Many business schools and corporate-finance training programs recommend or require these courses prior to enrollment.)

Quantitative analysis and modeling. We'll discuss the fundamentals of measurement and analysis in chapter 10, but this book won't turn you into a Wall Street "quant" or a high-flying spreadsheet jockey. Statistics and quantitative analysis are very useful skills when used appropriately, but the actual techniques are very situational and beyond the scope of this book. If you're interested in learning more about statistical analysis after reading chapter 10, I recommend:

Thinking Statistically by Uri Bram

How to Lie with Statistics by Darrell Huff

Turning Numbers into Knowledge by Jonathan Koomey, PhD

For an examination of more advanced methods of analysis, *Principles of Statistics* by M. G. Bulmer is a useful reference.

How to Use This Book

All truly wise thoughts have been thought already thousands of times; but to make them truly ours, we must think them over again honestly, until they take root in our personal experience.

—JOHANN WOLFGANG VON GOETHE, POET, DRAMATIST, AND POLYMATH

Here are a few tips that will help you get the most from this book:

Browse, skim, and scan. You don't need to read a book cover to cover to benefit: browsing can give you better results with less effort. Feel free to browse and preview concepts until you find a section that grabs your attention, then commit to applying that concept to your work for a few days.

You'll begin to notice significant differences in the quality of your work as well as in your ability to "think like a businessperson."

Keep a notebook and pen handy. The purpose of this book is to give you ideas about how to make things better, so be prepared to capture your thoughts as you have them; it'll make it easier to review the major concepts later. Your notebook will also make it easy to shift from taking notes to creating detailed action plans as they occur to you.²⁹

Review this book often. Keep it close to where you work so you can refer to it as you work, particularly before starting a new project. Repetition leads to mastery: the better you internalize these concepts, the more you'll improve your results. I also recommend setting a reminder in your calendar to review this book or your notes every few months to reinforce your understanding and spark new ideas.

Discuss these ideas with your colleagues. Great things happen when everyone you work with knows these concepts and uses the same language to discuss how they apply to your business. After every concept, I've included a link to an online reference page, which you can include in an email, proposal, blog post, or other communication. This helps ensure everyone is on the same page, particularly if the recipient isn't familiar with the concept you're referencing.

There's always more to explore. Each idea has many applications, and it's impossible to explore every ramification of these concepts in a single book. There are many great resources in the world of business literature that can deepen your understanding if you'd like to learn more about a particular mental model. Join me at personalmba.com to explore these ideas in more detail and learn how to apply them to your daily life and work.

Let's begin.

If these five things sound simple, it's because they are. Business is not (and has never been) rocket science—it's a process of identifying a problem and finding a way to solve it that benefits both parties. Anyone who tries to make business sound more complicated than this is either trying to impress you or trying to sell you something you don't need.

The **Five Parts of Every Business** are the basis of every good business idea and business plan. If you can define each of these five processes for any business, you'll have a complete understanding of how it works. If you're thinking about starting a new business, defining what these processes might look like is the best place to start. If you can't describe or diagram your business idea in terms of these core processes, you don't understand it well enough to make it work.¹

REFERENCE LINK: personalmba.com/5-parts-of-every-business/

Economically Valuable Skills

Don't go around saying the world owes you a living. The world owes you nothing—it was here first.

—MARK TWAIN, GREAT AMERICAN NOVELIST

If you want to improve your value as a businessperson, focus on improving skills related to the **Five Parts of Every Business**.

Not every skill or area of knowledge is **Economically Valuable**, and that's okay—there are many things worth pursuing for the sake of relaxation or enjoyment alone. You may enjoy white-water rafting, but it's very unlikely anyone will pay you to shoot the rapids unless you apply your skills for the benefit of others. Make the leap from personal enjoyment to **Products** and **Services**, however, and you'll find yourself getting paid—plenty of adventurous souls are willing to pay for rafting equipment and guides.

As Michael Masterson suggests in *Ready, Fire, Aim*, don't expect skills that aren't related to the Five Parts of Every Business to be economically rewarded. Find a way to use them to create Economic Value and you'll find a way to get paid.

Any skill or knowledge that helps you create value, market, sell, deliver

value, or manage finances is Economically Valuable—these are the skills we'll discuss in this book.

REFERENCE LINK: personalmba.com/economically-valuable-skills/

The Iron Law of the Market

Market matters most. And neither a stellar team nor a fantastic product will redeem a bad market. . . . *Markets that don't exist don't care how smart you are.*

—MARC ANDREESSEN, VENTURE CAPITALIST AND COFOUNDER OF NETSCAPE

What if you throw a party and nobody shows up? In business, it happens all the time.

Dean Kamen, a renowned and prolific inventor whose creations include the Stirling engine, the world's first wearable insulin pump, and water-purification devices, poured more than \$100 million into the development of the Segway PT, a \$5,000, two-wheeled, self-balancing scooter that he claimed would revolutionize personal transportation “in the same way that the car replaced the horse and buggy.” When the Segway was made available to the public in 2002, the company announced that it expected to sell fifty thousand units every year.

Five years into the business, the company had sold a total of twenty-three thousand units—less than 10 percent of the initial goal. (The company's financial records are private, but it's safe to say they didn't look good. In 2015, the company was sold to Ninebot, a competitor that sells inexpensive electric scooters, for an undisclosed sum.)

The problem wasn't that the product was poorly designed. The technology that makes the Segway work is sophisticated, and the benefits are significant: the Segway is a convenient, green urban car replacement. The problem was that very few people cared enough to spend \$5,000 on a goofy-looking alternative to walking or riding a bike—the massive market that Kamen expected didn't exist.

The same thing happens to new businesses every day. Without enough revenue to sustain it, any business will fail. Your revenue is dependent on people *wanting* what you have to offer.

Every business is fundamentally limited by the size and quality of the market it attempts to serve. The **Iron Law of the Market** is cold, hard, and unforgiving: if you don't have a large group of people who want what you have to offer, your chances of building a viable business are very slim.

The best approach is to focus on making things people want to buy. Creating something no one wants is a waste. Market research is the business equivalent of "Look before you leap." Books like *The New Business Road Test* by John Mullins can help you identify promising markets from the outset, increasing the probability that your new venture will be a success.

In the next few sections, we'll explore how to figure out what people want and need *before* investing your time and hard-earned money into creating something new.

REFERENCE LINK: personalmba.com/iron-law-of-the-market/

Core Human Drives

Understanding human needs is half the job of meeting them.

—ADLAI STEVENSON II, POLITICIAN AND FORMER GOVERNOR OF ILLINOIS

If you're going to build a successful business, it's useful to have a basic understanding of what people want. The most well-known general theory of what people want is Maslow's hierarchy of needs, proposed by the psychologist Abraham Maslow in 1943. Maslow's theory was that people progress through five general stages in the pursuit of what they need: physiology, safety, belonging/love, esteem, and self-actualization. Physiology represents the "lowest" level of human need, while self-actualization (the exploration of a person's innate potential) is the "highest."

In Maslow's hierarchy, each lower-level need must be met before a person can focus on higher-order needs. If you don't have enough food or you're in physical danger, you're probably not paying too much attention to how much other people like you or how much personal growth you're experiencing.

In practice, I prefer Clayton Alderfer's version of Maslow's hierarchy, which he called "ERG theory": people seek existence, relatedness, and growth, in that order. When people have what they need to survive, they move on to making friends and finding mates. When they're satisfied with

their relationships, they focus on doing things they enjoy and improving their skills in things that interest them. First existence, then relatedness, then growth.

ERG theory explains the general *priority* of human desires, but not the *methods* people use to satisfy them. For that, we must turn to other theories of human action. According to Harvard Business School professors Paul Lawrence and Nitin Nohria, the authors of *Driven: How Human Nature Shapes Our Choices*, all human beings have four **Core Human Drives** that have a profound influence on our decisions and actions:

1. *The Drive to Acquire*—the desire to obtain or collect physical objects, as well as immaterial qualities like status, power, and influence. Businesses built on the drive to acquire include retailers, investment brokerages, and political consulting companies. Companies that promise to make us wealthy, famous, influential, or powerful connect to this drive.
2. *The Drive to Bond*—the desire to feel valued and loved by forming relationships with others, either platonic or romantic. Businesses built on the drive to bond include restaurants, conferences, and dating services. Companies that promise to make us attractive, well-liked, or highly regarded connect to this drive.
3. *The Drive to Learn*—the desire to satisfy our curiosity. Businesses built on the drive to learn include academic programs, book publishers, and training workshops. Companies that promise to make us more knowledgeable or competent connect to this drive.
4. *The Drive to Defend*—the desire to protect ourselves, our loved ones, and our property. Businesses built on the drive to defend include home alarm system manufacturers, insurers, martial arts training programs, and legal services. Companies that promise to keep us safe, eliminate a problem, or prevent bad things from happening connect to this drive.

There's a fifth core drive that Lawrence and Nohria missed:

5. *The Drive to Feel*—the desire for new sensory stimuli, intense emotional experiences, pleasure, excitement, entertainment, and

anticipation. Businesses built on the drive to feel include movie theaters, arcades, concert promoters, and sports teams. Companies that promise to give us pleasure, thrill us, or give us something to look forward to connect with this drive.

Whenever a group of people have an unmet need in one or more of these areas, a market will form to satisfy that need. As a result, the more drives your offer connects with, the more attractive it will be to your potential market.

At the core, all successful businesses sell the promise of some combination of money, status, power, love, knowledge, protection, pleasure, and excitement. The better you articulate how your offer satisfies one or more of these drives, the more attractive your offer will become.

REFERENCE LINK: personalmba.com/core-human-drives/

Social Status

The society which scorns excellence in plumbing as a humble activity and tolerates shoddiness in philosophy because it is an exalted activity will have neither good plumbing nor good philosophy: neither its pipes nor its theories will hold water.

—JOHN W. GARDNER, FORMER PRESIDENT OF THE CARNEGIE CORPORATION

In addition to understanding **Core Human Drives**, it's important to understand that humans are social creatures. Like many other mammals, humans evolved to have a pecking order, a relative ranking of **Power** or status in a group. Competing with other people for status and power brought many benefits, including access to food, mates, resources, and the protection of other group members.

Status considerations are no longer as critical to survival, but our brains developed to place a very high priority on **Social Status**. As a result, status considerations influence the vast majority of a person's decisions and actions.

Social Status is a universal phenomenon: neurotypical human beings care about what other people think of them and spend a significant amount of energy tracking their relative status compared to other members of their

9. *Upsell Potential.* Are there related secondary offers that you could also present to purchasing customers? (Customers who purchase razors need shaving cream and extra blades as well; buy a Frisbee and you won't need another unless you lose it.)
10. *Evergreen Potential.* Once the initial offer has been created, how much additional work will you have to put in in order to continue selling? (Business consulting requires ongoing work to get paid; a book can be produced once and then sold over and over as is.)

When you're done with your assessment, add up the score. If the score is 50 or below, move on to another idea—there are better places to invest your energy and resources. If the score is 75 or above, you have a very promising idea—full speed ahead. Anything between 50 and 75 has the potential to pay the bills but won't be a home run without a huge investment of energy and resources.

REFERENCE LINK: personalmba.com/ten-ways-to-evaluate-a-market/

The Hidden Benefits of Competition

The competitor to be feared is one who never bothers about you at all, but goes on making his own business better all the time.

—HENRY FORD, FOUNDER OF THE FORD MOTOR COMPANY
AND ASSEMBLY-LINE PIONEER

One of the most common experiences of a first-time entrepreneur is discovering that your brilliant business idea isn't as original as you'd thought: other businesses are already offering similar products or services. This would shake anyone's confidence—after all, why bother when someone else is doing what you want to do?

Cheer up: there are ***Hidden Benefits of Competition***. When any two markets are equally attractive in other respects, you're better off choosing to enter the one *with* competition. Here's why: it means you know from the start there's a market of paying customers for this idea, eliminating your biggest risk.

The existence of a market means you're already on the right side of the ***Iron Law of the Market***, so you can spend more time developing your offer instead of proving a market exists. If there are several successful businesses

serving a market, you don't have to worry so much about investing in a dead end, since you already know that people are buying.

The best way to observe what your potential competitors are doing is to become a customer. Buy as much as you can of what they offer. Observing your competition from the customer's perspective can teach you an enormous amount about the market: what value the competitor provides, how they attract attention, what they charge, how they close sales, how they make customers happy, how they deal with issues, and what needs they aren't yet serving.

As a paying customer, you get to observe what works in your market and what doesn't before you commit to a particular strategy. Learn everything you can from your competition and then create something even more valuable.

REFERENCE LINK: [personalmaba.com/hidden-benefit-of-competition/](http://personalmba.com/hidden-benefit-of-competition/)

The Mercenary Rule

Make money your god and it will plague you like the devil.

—HENRY FIELDING, EIGHTEENTH-CENTURY NOVELIST AND SATIRIST

Becoming a **Mercenary** doesn't pay—don't start a business for the money alone. Here's why: starting and running a business *always* takes more effort than you first expect.

Even if you identify a business that will run itself, setting up the systems necessary to run the business requires persistence and dedication. If the only thing that interests you about an opportunity is the money, you'll probably quit well before you find the pot of gold at the bottom of the landfill.

Pay very close attention to the things you find yourself coming back to over and over again. Building or finishing anything is a matter of *starting* over and over again; don't ignore what pulls you. The trick is to find an attractive market that interests you enough to keep you improving your offering every single day. Finding that market is a matter of patience and active exploration.

That said, don't ignore "boring" businesses until you investigate them; if you can find some aspect of the work that interests you and keeps you

engaged, mundane markets can be quite attractive. “Dirty” businesses like plumbing and garbage collection aren’t sexy, but they can be quite lucrative because there’s a significant ongoing need combined with relatively few people willing to step up and meet the demand.

If you find a way to make a necessary but dull market interesting enough to pursue, you may have discovered a hidden vein of gold waiting to be mined.

REFERENCE LINK: personalmba.com/mercenary-rule/

The Crusader Rule

The zealous display the strength of their belief, while the judicious show the grounds of it.

—WILLIAM SHENSTONE, EIGHTEENTH-CENTURY POET
AND LANDSCAPE DESIGNER

Being a **Crusader** doesn’t pay either. Every once in a while, you’ll find an idea so fascinating it becomes hard to think about it objectively. The stars align, heavenly trumpets blare, and suddenly you have the unmistakable impression that you’ve found your calling.

In all the excitement, it’s easy to forget that there’s often a huge difference between an interesting idea and a solid business. In your optimism, forget ye not prudence: changing the world is difficult if you can’t pay the bills.

Some ideas don’t have enough of a market behind them to support a business, and that’s okay. That doesn’t mean you should ignore them: side projects can help you expand your knowledge, improve your skills, and experiment with new methods and techniques. I’m a huge advocate of pursuing side projects as long as you don’t rely on them to produce income. Once you have your financial bases covered, crusade all you want.

Before attempting to launch a business, take the time to do a thorough evaluation using the **Ten Ways to Evaluate a Market**. If you’re finding it difficult to be objective, find a trusted colleague or adviser to help you, then test the market before you fully commit. A few hours spent in evaluation can prevent months (or years) of frustration and misplaced effort.

REFERENCE LINK: personalmba.com/crusader-rule/

Twelve Standard Forms of Value

Value is not intrinsic; it is not in things. It is within us; it is the way in which man reacts to the conditions of his environment.

—LUDWIG VON MISES, AUSTRIAN ECONOMIST

In order for your business to successfully provide value to another person, that value must take on a form they're willing to pay for. Fortunately, there's no need to reinvent the wheel—**Economic Value** usually takes on one of twelve standard forms:

1. *Product.* Create a single tangible item or entity, then sell and deliver it for more than what it cost to make.
2. *Service.* Provide help or assistance, then charge a fee for the benefits rendered.
3. *Shared Resource.* Create a durable asset that can be used by many people, then charge for access.
4. *Subscription.* Offer a benefit on an ongoing basis and charge a recurring fee.
5. *Resale.* Acquire an asset from a wholesaler, then sell that asset to a retail buyer at a higher price.
6. *Lease.* Acquire an asset, then allow another person to use that asset for a predefined amount of time in exchange for a fee.
7. *Agency.* Market and sell an asset or service you don't own on behalf of a third party, then collect a percentage of the transaction price as a fee.
8. *Audience Aggregation.* Get the attention of a group of people with certain characteristics, then sell access to that group, in the form of advertising, to another business looking to reach that audience.
9. *Loan.* Lend a certain amount of money, then collect payments over a predefined period of time equal to the amount of the original loan plus interest at a predefined rate.
10. *Option.* Offer the ability to take a predefined action for a fixed period of time in exchange for a fee.

11. *Insurance.* Take on the risk of some specific bad thing happening to the policyholder in exchange for a predefined series of payments, then pay out claims only if the bad thing happens.
12. *Capital.* Purchase an ownership stake in a business, then collect a corresponding portion of the profit as a one-time payout or ongoing dividend.

Let's investigate these **Twelve Standard Forms of Value** in more detail.

REFERENCE LINK: personalmba.com/12-standard-forms-of-value/

Form of Value #1: Product

Business is not financial science . . . it's about creating a product or service so good that people will pay for it.

—ANITA RODDICK, ENTREPRENEUR AND FOUNDER OF THE BODY SHOP

A **Product** is a tangible form of value. To run a Product-oriented business, you must:

1. Create some sort of tangible item that people want.
2. Produce that item as inexpensively as possible while maintaining an acceptable level of quality.
3. Sell as many units as possible for as high a price as the market will bear.
4. Keep enough inventory of finished product available to fulfill orders as they come in.

The book you're holding right now is a good example of a Product. It had to be written, edited, typeset, printed, bound, and shipped to bookstores in sufficient quantities before reaching your hands. Leave out any of these steps and you wouldn't be reading this right now. To make money, a book must be sold for more than it cost to create, print, and distribute.

Products can be durable, like cars, computers, and vacuum cleaners. They can also be consumable: goods like apples, donuts, and prescription medications are products as well. Products don't have to be physical—even