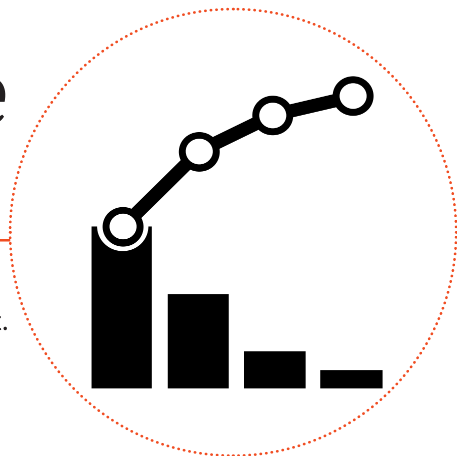
THE UNIVERSITY OF SYDNEY
Business School

CEMS

The 80-20 Rule



Intro

It is the little things we do that truly matter. The 80-20 rule, or "the Pareto principle", named after the concept's founder Vilfredo Pareto in 1848, has been a staple of contemporary management practices –the idea being that 20% of the work drives 80% of the outcome. Such a rule is frequently employed by management to allocate time effectively, maximise efficiency, and encourage strategic thinking, emphasising how small, focused actions can generate disproportional outcomes. Having an 80-20 mindset encourages managers to focus on what is important. After all, we only have so many minutes in a day, so identifying which actions have the biggest impact keeps us at our most productive. But how true is this rule in practice?

What's the evidence?

Originally, the 80-20 rule stems from an observation made by Pareto, where he noticed that 80% of the land in Italy was owned by 20% of the people. This conception of the 80-20 rule has since drifted in meaning, with the statistical 'rule' being visible in a range of domains. A classic example would be the adage that "80% of profit comes from 20% of customers". In fact, the 80-20 rule can be teased out in nearly everything. Some studies have even suggested that data can always be tweaked to fit into an 80-20 rule. And the ratio itself can often be tweaked and still broadly conform to the 80-20 principle: there are also 90-10 rules, 70-30 rules, and 60-40 rules, all reflected in different patterns and situations. So while there are frequently statistical correlations that support the existence of the Pareto principle, those correlations don't necessarily recommend a particular course of action. In addition to this, research has indicated that some domains where the 80-20 pattern was most visible – such as niche sales – increasingly see 'long tails' in the statistical distribution[1].

EVIDENCE BASE
Moderate

Why unlearn 80-20?

What is the problem with applying the 80-20 rule? Statistical 'principles' like Pareto may identify existing patterns in data, but understanding these patterns as a 'rule' can be dangerously reductive. The evidence points to an uncritical and improper usage of data reflecting 80-20 relationships, often emphasising short-term boosts over long-term stability and innovations. By focusing our attention on the 20% of activities we think have the highest impact, we are still neglecting a wide range of business critical factors which are also significant. An emphasis on the vital few can neglect many smaller critical factors which can have long term consequences. These small critical factors which fall in the 80% may also be significant dependencies on which the 20% rely. A reductive view that focuses on the high impact 20% - assuming those things can be identified in the first place – might miss these complex relationships and contexts in the whole of an organisation. Also important is the statistical 'long-tail' phenomenon: focusing on a pattern like 80-20 might be short-sighted, and miss a more accurate phenomenon. If managers wish to take the 80-20 rule seriously, it is important to stay curious and explore how these numbers come to be, and whether 80-20 is really an appropriate fit for the data.

HARM LEVEL
Moderate

ADAPTABILITY
High

Want to know more?

https://hbr.org/2012/05/the-unimportance-of-practicall

[1] Brynjolfsson, E., Hu, Y., & Simester, D. (2011). Goodbye pareto principle, hello long tail: The effect of search costs on the concentration of product sales. *Management Science*, 57(8), 1373-1386. https://doi.org/10.1287/mnsc.1110.1371