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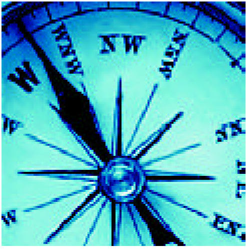
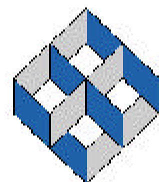


Enterprise Portfolio Management

A Primer for Managing Strategic Investments and Gaining Maximum Business Value

April 2003



Introduction

In any organization where projects are competing for resources, funding and priority status, significant controversy can occur. Each business unit has their own, individual list of important projects that may or may not be corporately shared. Which projects will truly support the business needs and objectives? How can you ensure the projects chosen for completion align with corporate objectives? More importantly, how can you continue to ensure you're working on the right projects as things change from day-to-day and new business opportunities arise?

The concept of portfolio project management refers to organizations managing their composite group of projects with the same rigor, balance, executive leadership and decision-making involvement as the company's financial portfolio. In a project-driven organization, projects are the single, most significant investment made. Investments of this nature must be managed from a corporate, strategic-planning perspective, not merely administratively.

Your Organization Already Has a Portfolio

An enterprise portfolio is simply this – organizational assets applied to more than one program or project initiative for a particular organizational outcome or objective. If your organization funds, manages, allocates resources or time to more than one initiative or investment, you already have an enterprise portfolio. You may not know what the portfolio comprehensively looks like, how it is strategically invested, or be managing it proactively, but it does exist.

Portfolio Management is a Process

Portfolio Management is an ongoing process that includes decision-making, prioritization, review, realignment and reprioritization.

Let's say you are taking a direct flight from Miami to San Francisco, which is scheduled to be a five-hour flight. Once you've reached cruising altitude, the pilot sets the heading coordinates to San Francisco and decides not to refine the heading coordinates again until ready to request landing in San Francisco. At the five-hour mark, the pilot and passengers may be shocked to find the plane is seriously off course and most definitely not in San Francisco. Does it mean that the coordinates set over Miami were wrong? Of course not, but changing flight conditions, wind velocity and weather conditions required realignment of the coordinates *while in progress* to ensure success. It is a *process* not a static, finite task.

Similarly, this is true of investments. If you gave all your retirement funds to an investment professional for management today, would you wait until just before retirement to check on progress or reevaluate how you're investments are doing? Would you wait for a year? What if a new great investment surfaced, which promised significant return on investment? Wouldn't you want to reevaluate new choices against your current investment strategies?

As with financial investments, the organizational goals, objectives and resulting tactical strategies are evolving on a daily basis. The competitive markets continually challenge our

plans and demand redirection and realignment of organizational focus. The first area of project misalignment is in the area of fiscal planning and budgeting. Most organizations do fiscal planning and budgets on an annual basis. Optimistically, these plans are reviewed quarterly for accuracy or revision; usually only to review actuals against planned work, resources and budget. This type of planning may seem "top-down" and organization-objectives focussed. However, it does not balance the evolving business dynamics and allow for much needed fine-tuning.

Setting an Investment Strategy and Objectives

Before an organization invests capital in any initiative it should first establish an appropriate strategy for measuring new proposals against the corporate objectives as well as other proposed ideas. To create a truly effective mix of initiatives, the organization must consider a wide range of factors that include the mission, vision, objectives, short-, mid-, and long-term goals of the organization, in addition to the size of the proposed portfolio and funding guidelines.

Additionally, organizations must establish an unbiased mechanism for monitoring initiatives for continued investment, how to measure the individual project return on investment, how to weight multiple initiatives appropriately within the enterprise portfolio, and how to ensure continued alignment with overall corporate objectives. It is essential to have an agreed-upon, unbiased prioritization process.

Once the organization has established their overall objectives and project investment strategy, they must create the optimal group of initiatives, or mix, to implement their strategy and achieve the objectives.

Classification of Project Investments

The highest level of analysis for your enterprise portfolio is project classification. This is necessary to decide where discretionary funding choices may be made versus non-discretionary. There are two primary categories all investments fall into: *Survival* and *Growth.* If a proposed project does not fall into one of these two categories, the business should immediately question the validity of investment funding.

Survival

These are the *must-do* initiatives. A project falls into this category if, and only if the project must be completed for the health of the business. In other words, if you don't do this initiative, during this fiscal planning period, your business will fail or suffer irreparable damage. Initiatives in the Survival category must be included as part of the enterprise portfolio and should be viewed as existing, non-discretionary investments.

Growth

All other initiatives fall into the growth category. Contrary to what the word *growth* implies, a growth project does not necessarily mean it produces revenue (directly or indirectly). Growth initiatives may be exclusively internal, support-oriented or external and financially-based. The real qualifier for a project in this category is that it is discretionary and has business value for the organization to excel and prosper.

Constructing an Enterprise Portfolio

Once you've identified the list of *survival* and prospective *growth* initiatives there are two main components in the construction of a enterprise portfolio:

Project Allocation — how the enterprise portfolio is spread among all its project types such as infrastructure, new initiatives, research and development, etc.

Project Selection — the selection of the best individual initiatives for investment within each project type.

Top-Down and Bottom-Up Project Allocation and Selection

Top-down analysis looks at the big picture economic themes and trends and how they affect the overall organization's growth, rather than analyzing, validating and approving individual initiatives.

By contrast, the bottom-up approach is driven by the "project benefits" as defined by the individual business units or project advocates and is based on the individual project's return-on-investment to the business unit and organization. This approach concentrates first on the likely out-performance of individual initiatives and thus the enterprise portfolio is constructed from the bottom up.

A combination of both allocation and selection analysis is required to formulate the appropriate project *mix* for the organization with corresponding importance weightings and prioritization.

The Appropriate Project Mix for Your Organization

One of the most important decision that any project organization must make is the selection of the appropriate project mix for the portfolio. Why is this so important? One answer is that for most project-driven businesses, the initiatives included in the portfolio are the single most important determinant of organizational success.

Historically, project mix decisions have tended to be unstructured without reference to a quantitative, analytical framework. A new method is required to emphasizes business assumptions, goals and objectives in all project decisions, including:

1. Some statement of the business objectives and constraints that will be used to select the appropriate mix. Constraints include time horizons, market windows, financial budgets, resource utilization and availability, and technology drivers.

2. Forecasts on return for each project
3. Estimates of risk for each project
4. Weighting and prioritization techniques for ordering initiatives

Who Should Make the Project Mix Decision

Since business objectives and constraints are such key considerations, the business must provide input to the decisions at a corporate level. The common practice at one time was for the organization to allocate project funds among the various business units and let the individual business units decide how to prioritize project spending. Of course each business-unit has their unique priority list and for the information systems (IS) group in particular, this has became a significant problem. As a central support organization with conflicting priorities, IS has been put in a no-win situation with infinite work possibilities and finite, many times overallocated resource pools. For any internal support organization to be successful, it must have a method for connecting daily project decisions to the overall corporate perspective, prioritizing, and escalating conflicting project priorities for corporate reevaluation. This means letting the *investor* (collectively) control the investment decisions. The individual business units are contributors to the process, but do not make decisions on their own without balance across organizational boundaries.

Elements for Weighting and Prioritizing Initiatives

Risk and Return

Unlike financial investments, higher project risk is not necessarily correlated with higher potential project return. Measuring project risk and return is much more complex and while some of the criteria are generic across all industries and organizations, much of the measurement is unique to the specific business. Generally speaking, risk is represented by the tangible and intangible impediments that may potentially cause the project to fail. Once the individual risk factors for each project are identified, the project may be weighted against the other initiatives for a relative comparison. Return on investment (ROI) is quantified by the tangible and intangible benefits, or returns, to the business.

Other Key Weighting Criteria

In addition to Risk and Return weightings, several other inputs are key to choosing the right mix of initiatives for your organization. Some of these items include:

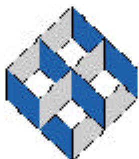
1. Project's success potential – specific measurement for probability of project success
2. Degree of correlation to business plans
3. Degree of correlation to market position
4. Degree of correlation to competitive pressures
5. Degree of correlation to financial objectives

Bringing it All Together

The above criteria can be measured, consolidated, weighted and compared by project for a complete portfolio perspective. Once a prioritized list of initiatives is corporately agreed upon, across business units and organizational boundaries, the enterprise portfolio is in place and measurement can begin as well as rebalancing if new priorities are introduced. Rebalancing is the process by which new initiatives enter the queue and are assessed against the current portfolio of project investments. The decision to change the portfolio by increasing project investment or replacing a project is made using the same weighting criteria.

Managing for Results

By taking a proactive approach to the selection of initiatives and managing actual performance against planned, organizations can dramatically improve the timeliness, quality, and completeness of their initiatives as well as ensure all initiatives enable overall business success.


SEMERON

Semeron Corporation
2815 Eastlake Avenue East
Suite 300
Seattle, WA 98102
United States
Tel: +1-206-686-1360
info@semeron.com
www.semeron.com

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