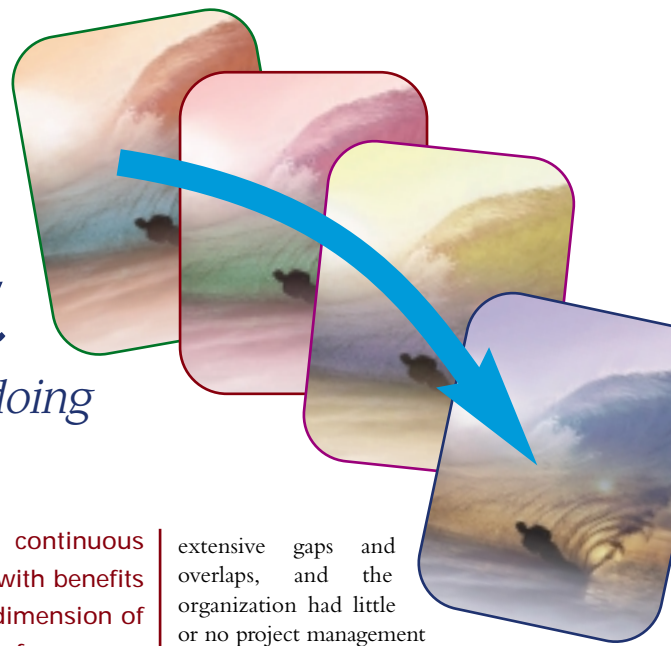


# Portfolio management

*Delivering business strategy through doing the right projects*



Previous articles by Terry Cooke-Davies have dealt with the continuous improvement of project management processes (October 2001), with benefits management (November/December 2001) and with the human dimension of project management (January 2002). In this article, Terry shifts his focus away from 'doing projects right' to 'doing the right projects' and considers the discipline that links business strategy with project management - portfolio management.

Every business organization is faced with resource constraints, and has to make choices about how to apply its resources to best implement its chosen business strategy. A share of the resources will be applied to the current mainstream operations of the organization ('business as usual') and a different share to initiatives that are designed to create new capacity or new capabilities to meet future challenges ('business change'). These choices typically become enshrined in approved budgets, which are then used as the basis for day-to-day operational control, with oversight being exercised by means of some form of governance structure.

For 'business as usual', there are tried and tested methods of establishing annual budgets, and reviewing performance against these. The problem occurs when dealing with implementing business strategy through change initiatives - either projects or programmes.

Since all change is, by its very nature, new and uncertain, it is very difficult to assess whether we are applying our resources in the optimum way. By that I don't just mean whether we are doing the right projects, I mean whether we are doing the right projects, in the right sequence, with the right timing and resourcing them adequately.

We will be able to rest content that we are doing this only when we are confident that we have developed excellent portfolio-management processes and systems that are both comprehensive and practical.

Unlike benefits management, portfolio management is widely established as a discipline, with four out of every ten members\* surveyed rating as 'high' both their approach and practice (See Figure 1). So there is a reasonable amount of excellent practice available to us.

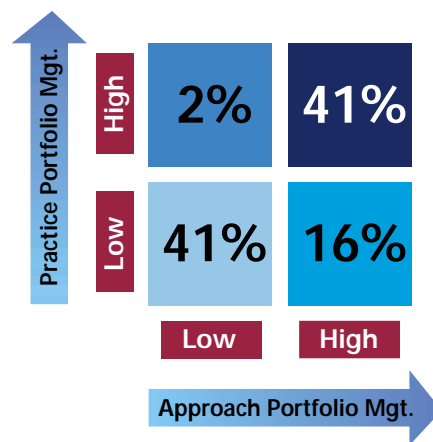


Figure 1: 'State of the Art' in Portfolio Management

## 1. The portfolio management system must be comprehensive

It is more than 20 years since I assumed executive responsibility for my first cross-functional portfolio of projects and programmes. As director of Development and Supply for the Graphics Division of Letraset International, I was charged with improving the effectiveness of our manufacturing and R&D operations. With considerable help from McKinsey, I undertook a comprehensive review of expenditure on both 'business as usual' and 'business change'.

I was horrified to learn that there were projects going on in all sorts of unlikely places. We counted well over 100 of them in an organization that employed only 600 people or so. If a departmental manager or supervisor wanted to initiate any change, then he (there were no 'she's, I'm ashamed to say) had only to find the room in his budget, and he would set people off doing things. Compared to the business' strategic objectives, there were

extensive gaps and overlaps, and the organization had little or no project management discipline.

As a result of the 'business change' review, we instituted three disciplines:

- Investment management - judging each project proposal against a specific business case, and then reviewing that business case at predefined stage gates during the life of the project.
- Pipeline management - maintaining a pipeline of projects at different stages of development, so that if projects were cancelled, there were others available to take their place.
- Portfolio management - matching the project spend to the chosen organization strategy and business objectives, for which we used the simple grid shown in Figure 2.

Such a system can often work well when it is first established, and for many of the 41% of organizations in the lower left quadrant of Figure 1 it may possibly be an improvement over their present situation. The trouble is, it soon starts to degrade! The second law of thermodynamics<sup>1</sup> is alive and well, and most definitely applies to the world of projects and programmes!!

This degradation can stem from a number of problems involved in maintaining the discipline of such a portfolio approach, particularly in organizations that have achieved a greater maturity of project, programme and portfolio management in some business areas than in others. (The difference between programmes and portfolios will be explored later, in topic 2 - Practicality.)

The two areas that seem to crop up most often are:

- Making ALL business change expenditure visible and subject to portfolio management disciplines, and
- Preventing excellent practice in specialised business functions from hindering the spread of best practice, and the applicability of portfolio management to all areas.

The first of these is a problem for any organization that has 'blind spots' where

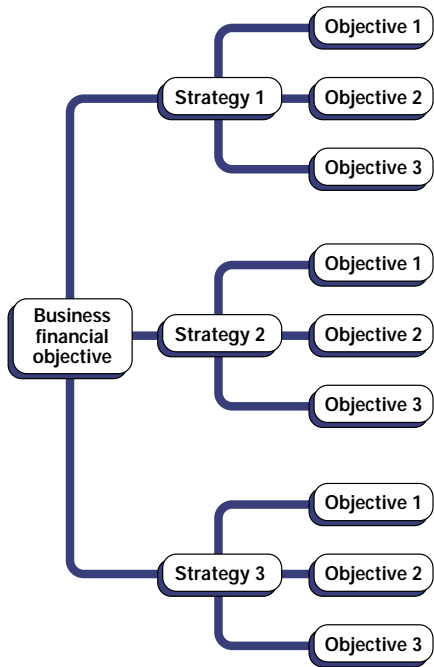


Figure 2: A simple project portfolio

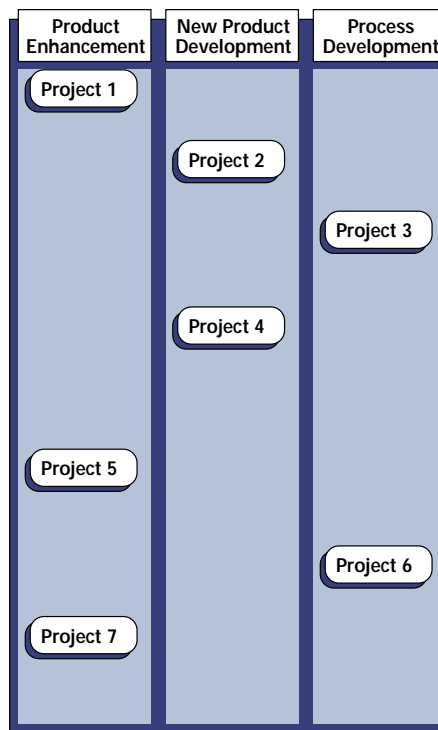
projects can be ‘sneaked into’ the portfolio, with a consequent ripple effect throughout the organization.

This may be because ‘business as usual’ is inadequately distinguished from ‘business change’ in organizations that are not sufficiently mature, for example, to recognise project management as a specialised discipline requiring professional expertise. This is a fairly common occurrence in organizations that are less mature than those taking part in our regular network surveys, as is illustrated by some current research at Athabasca University<sup>ii</sup> which indicates that as many as 40% of all projects in business organizations may be undertaken by people who spend less than 50% of their time in project management – so-called ‘accidental project managers’.

It might also result from loose budgetary control, with experienced executives who are well versed in playing games with the system to create ‘pockets of funds’ that they can then use to fund their own desired business improvements (or to buy new office furniture, for that matter).

A third source of these ‘blind spots’ is senior managers at each level ‘overriding’ the system, to authorize their favourite change initiatives. Any or all of these reasons can combine to create a ‘grey market’ in ‘business change’ that lies outside the visibility of formal portfolio control.

Where organizations have solved this problem, they have done so by developing a comprehensive investment management system through which all ‘business change’ expenditure must pass before being authorised, and that links seamlessly into the portfolio



management system.

The second problem area that can prevent ALL business change being within the scope of good portfolio management might not seem like a problem at first sight. The problem is the existence of pockets of excellent practice in specific business functions that are then seen as being too specialised to apply elsewhere. Examples might be:

- The allocation of capital for major plant investment in mature industries such as petrochemicals
- The maintenance of a well-defined portfolio of R&D projects in pursuit of a coherent R&D strategy, for example, within pharmaceutical R&D, or the commercialisation departments of manufacturing organizations. Figure 3 illustrates the kind of portfolio review tool that enables such portfolios to be managed.<sup>iii</sup>
- The prioritisation of IT projects within a central IT department, especially where such a department has a capped headcount, and the instructions are to deliver the optimum portfolio using the allocated head count.

Each of these, admirable though it is in its own business area, can turn the business or functional

unit into an impenetrable ‘silo’ that restricts the spread of good portfolio-management practice to other parts of the organization.

## 2. The portfolio-management system must be practicable

This second characteristic is the one that gives rise to dissatisfaction in organizations in the top right-hand quadrant of Figure 1. Once there is a portfolio management system in place that covers all ‘business change’ expenditure, it must facilitate the effective management of that business change, and its adoption into ‘business as usual’. This requires attention to five interlinked challenges.

a) The system must encourage trade-offs to be made, such that resources can be optimised in support of the corporate strategy. This means, for example, that ‘in flight’ data must be kept for the performance of each project or programme, and related to the relevant current and forecast ‘business as usual’ data, so the business case for each project or programme can be continually reviewed.

This sounds simpler than it is. For example, if an organization does not keep accurate timesheet records for large numbers of employees who work on ‘business change’, but record them as FTEs (full-time equivalents) in ‘business as usual’ departments, both sets of data may be sufficiently inaccurate to prevent accurate comparisons to be made between different projects or programmes competing for the same funds.

There is also a relationship between the credibility of the decision-making, and the extent to which managers throughout the organization will support the system with accurate data. This calls for a transparency of decision analysis, and an absence of corporate ‘game playing’ that eludes most organizations.

b) The system must be compatible with the actual management practices of the ‘business change’ organization. It is appropriate at this point to distinguish between portfolios and programmes. Using the terminology of the Association for Project Management, a

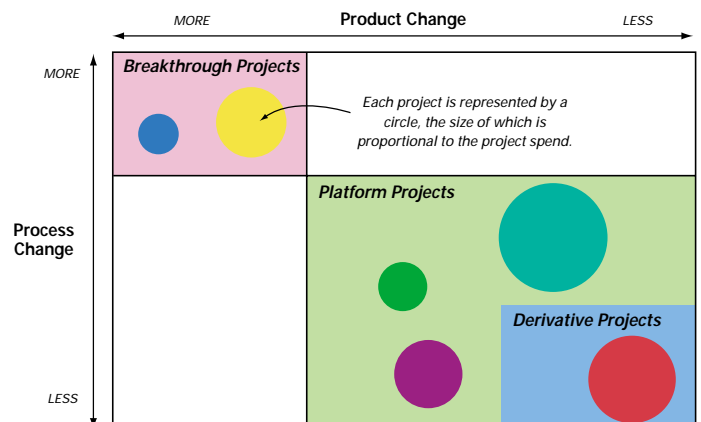


Figure 3: A product development portfolio

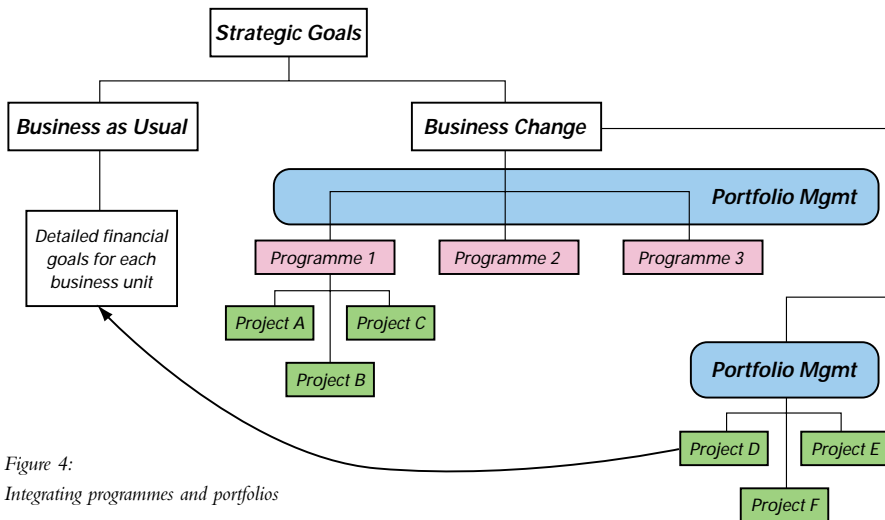


Figure 4:  
Integrating programmes and portfolios

portfolio is 'a grouping or bundle of projects gathered together for management convenience. They may or may not have a common objective, they are often related only by the use of common resources.'

A programme, on the other hand, is 'a broad effort encompassing a number of projects and/or functional activities with a common purpose.'

Under these definitions, it is clear that programmes and portfolios complement each other rather than being alternative approaches. As Figure 4 illustrates, even where an organization adopts an explicit programme management approach, there will still be at least two levels within which portfolio management is likely to be required.

At the first level, the organization as a whole will need to decide what resources are to be applied to competing programmes within the 'business change' arena.

At a lower level, there will inevitably be some 'business change' projects that are worth undertaking, but which do not fit comfortably within programmes. In this case, they can be conveniently grouped together as a portfolio both for management purposes, and to optimise resource allocation. Projects D, E and F have been dealt with in this way.

c) The system must integrate project control with benefits realisation so as to facilitate informed decisions for the benefit of the business as a whole.

'Business change' projects and programmes do not contribute direct improvements in organizational performance, unless the project is being run as a new venture. What they do is to deliver a capability, that can be exploited by 'business as usual' to achieve organizational strategic goals. This is what the arrows from Programme 1 and Project D in Figure 4 represent.

Thus, the portfolio management system will be effective only if it relates the 'business as usual' performance in exploiting new capability to the project or programme performance that delivers the same capability.

Increasingly, organizations are resolving this problem by aligning the programme

management structure with the 'business as usual' structure, so that each programme manager reports both to the 'business change' organization and to the 'business as usual' executive whose business unit will exploit the capability for business benefit. Many pharmaceutical companies, for example, are introducing 'therapeutic areas' as a discrete business unit that can provide an appropriate level of portfolio management aligned with discrete strategic business objectives.

d) The system must recognise that project management is fundamentally different from ongoing process management, and allow for project or programme governance to be exercised quite distinctly from operational control.

In spite of the ubiquity of 'business change' projects and programmes in business today, many organizations in which 'business as usual' is dominated by transactional business or continuous operations, reveal a lack of understanding about just how different the management of projects is from the management of ongoing operations.

There is insufficient room to examine this topic in detail in this context, but I am convinced that it is one of the main contributors to organizational immaturity in the management of projects and programmes.<sup>iv</sup>

It shows up as a problem in the portfolio management system by failing to recognise the impact on project performance of continual juggling of priorities, and failing to allow the project or programme manager sufficient authority to deliver the capability required with the available resources. At its worst, it encourages 'micro-management' by portfolio managers who are too far removed from the project front line to make sensible decisions, to the consequent detriment of project performance.

e) The system must incorporate data in formats that are appropriate to many different constituencies.

As the four points a) to d) above make clear, people in many different positions in organizations contribute to effective decision-

making about priorities within a portfolio. What this means is that the data on which the decisions are based must be derived from common and compatible raw data, but presented in a variety of different formats that are relevant to strategists, line managers, capacity planners, project and programme managers, and project and programme support offices.

Sadly, evidence from surveys that are currently being conducted on behalf of the Human Systems' networks indicates that few organizations have management information systems that are yet up to this challenge.

## In conclusion

Portfolio management is a crucial topic to any organization that seriously aspires to world-class project management or 'business change' management. Project management literature contains little on the topic, but there is some evidence that much good practice exists. On the other hand, as this discussion has indicated, there is still much room for improvement, and this promises to be a fruitful area for development over the next few years.



Terry is the Managing Director of Human Systems International Limited, a company with operations in UK, USA and Australia, that supports a global network of organisations that are committed to working together to improve their own organisation's results through projects. People representing member organizations work together in workshops, in working parties and in targeted benchmarking study teams. Terry can be contacted at [cooke-daviest@humansystems.co.uk](mailto:cooke-daviest@humansystems.co.uk).

i The second law of thermodynamics states, for example, that energy always flows from a hot object to a cooler one, so that the amount of entropy in a system is always increasing.

Put more simply - chaos always emerges from order, unless an outside source of energy acts to impose or maintain order.

ii Dr. Janice Thomas et. al., (2001), 'Selling PM to Executives - Phase II', PMI Symposium, Nashville, Tennessee.

iii Adapted from Steven C. Wheelwright and Kim B. Clark, (1992), 'Creating Project Plans to Focus Product Development', Harvard Business Review, March-April 1992.

iv For a discussion of the issue of governance on projects, readers are directed to J. Rodney Turner and Anne Keegan (1999), 'The Versatile Project-based Organization: Governance and Operational Control', European Management Journal, Volume 17, No. 3, pages 296-309.