Strategic portfolio management

How governance and financial discipline can improve portfolio performance

Portfolio Management

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The heart of the matter

Despite an uncertain business environment, organizations today remain under pressure to innovate and grow by successfully executing their business strategies. At the same time, they are expected to maintain existing operational efficiencies and costs – a daunting challenge in the wake of an economic downturn that forced businesses to eliminate project managers and other resources.

As businesses gear up for growth, many find they are hobbled by inadequate portfolio management (PM) practices and resources.

Some businesses, for instance, invest significant capital spending on programs and portfolios that do not directly align with strategic corporate objectives. Others struggle to balance risk with the opportunities required to achieve these objectives. Many are unable to accurately assess their portfolio's performance, yet they must continuously justify funding requests for both new and existing projects.

While there is no single solution, many organizations realize they can improve performance, curtail costs, reduce risk, and earn a greater return on investments (ROI) through better portfolio management. A successful portfolio management strategy must comprise an end-to-end framework that methodically guides organizations from project selection through execution.

The payoff can be substantial. Companies that excel at portfolio management typically complete projects on time and under budget while increasing ROI, according to Aberdeen Research. In fact, an effective portfolio management program can enable companies to achieve up to 25% more revenue from new products when compared with less successful competitors, according to Aberdeen. These "best in class" organizations typically improve project ROI by as much as 28%.[1]

Robust portfolio management is essential – but only a start. A rigorous governance model is critical to help enforce accountability, optimize cross-functional alignment, and escalate issues to the appropriate decision makers. Strong governance also can help align communications, calendars, and strategies across business units.

Beyond governance, an unwavering financial discipline and regular reviews of portfolio performance throughout the entire process are necessary to guide informed decisions. This level of discipline will demand standardized key performance indicators (KPIs) and powerful analytics to deliver objective insight for proactive decisions. Also essential is a benefits-realization process that enables organizations to ensure projects yield the expected benefits and stop underperforming projects early.

To deliver the full business value in this era of doing more with less, Enterprise Project Management Offices (EPMOs) must become strategic players in the quest for improved performance, innovation, and revenues. Doing so will require PM tools and processes that are built upon a sound foundation of governance and financial discipline.

[1] Aberdeen Group, "Project portfolio management: Selecting the Right Projects for Optimal Investment Opportunity," March 2011

An in-depth discussion

Portfolio management is much more than simply managing multiple projects. It is the management of the entire project portfolio in a way that maximizes the impact of projects to the overall success of the organization.

Effective portfolio management aligns a company's investments, people, and programs with its overall strategic objectives. It is a continual process that integrates business strategy with operational performance to synchronize resources, strategies, and schedules.

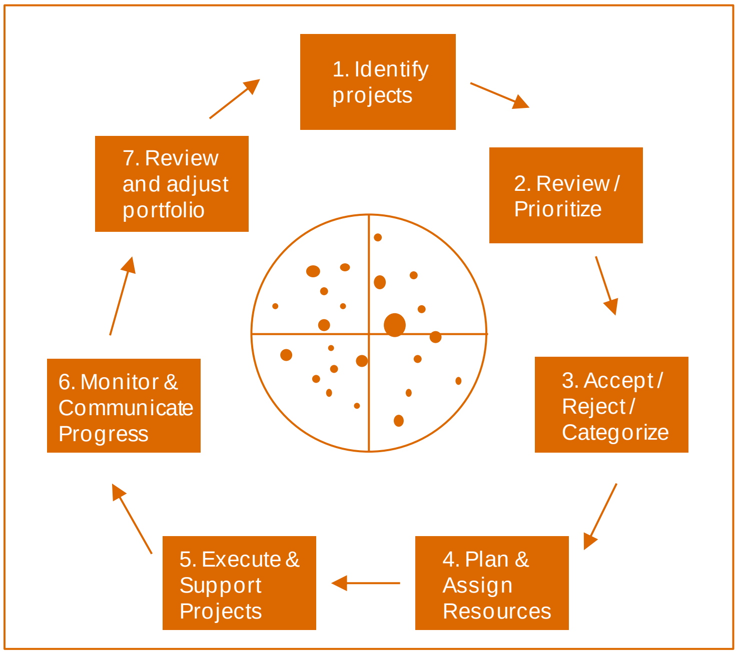

Figure : Seven steps to a portfolio framework

The fundamental challenge of portfolio management is that a strong methodology will only take you so far. What's needed is a set of best practices layered on top of a strong framework to ensure execution excellence and an optimized ROI. Although there is no standard framework for portfolio management, certain elements form the foundation of any successful portfolio management framework.

High-performing portfolio management requires a framework that identifies the processes for selection, prioritization, authorization, management, and control of a project portfolio. It also must optimize the return on investment to the business at the enterprise level. Most large organizations (or individual business units) develop a framework that follows seven basic steps identified in Figure 1.

While this framework provides a good idea of what a comprehensive project management strategy might entail, every organization has different needs and objectives. Consequently, each will need a customized set of tools, processes, and methodologies to help realize the most effective portfolio. This framework must help control portfolio costs and ensure that strategy, execution, and results are properly aligned.

Each organization must design a singular portfolio management strategy that takes into account unique complexities and interdependencies. For instance, budget and internal resources to conduct projects may not be included in the planning cycle or they may not be aligned with corporate strategy. At the project-execution level, cross-functional coordination may not be optimized, resulting in disparate programs with similar objectives that can drain corporate resources.

Portfolio leaders must understand these unique interdependencies, but they must also assess the key drivers that make a comprehensive portfolio management strategy essential for the organization.

It will also be necessary to understand the maturity of portfolio management processes. We have seen that, while many organizations are willing to invest people and infrastructure to create an EPMO, they frequently do not spend the time and budget to advance their processes and methodologies to best-in-class status.

The risks of ineffective portfolio management

In response to challenging economic conditions, CEOs are looking to innovation to gain competitive advantage, and they're focusing on expansion into developing markets. This shift in the geographic market makes the need for excellence in portfolio management more acute.

PwC's 15th Annual Global CEO Survey 2012 found that half of CEOs based in developed markets believe that emerging economies are more important to their company's future.2 With opportunity comes risk, however: This type of organizational change can easily impede projects. In fact, respondents to a survey conducted by the Project Management Institute reported that a change in organizational priorities was the most frequently cited reason for project failure.3

The impact of project failure can be quite costly. The same PMI study found that an average of 36% of projects did not meet their original goals – at a cost of 12 cents for every dollar spent on projects in the US.

Why do so many projects fail to meet their goals? Many organizations cannot balance resources across the portfolio, properly assess risk in the portfolio, or understand portfolio trade-offs, Aberdeen has found.

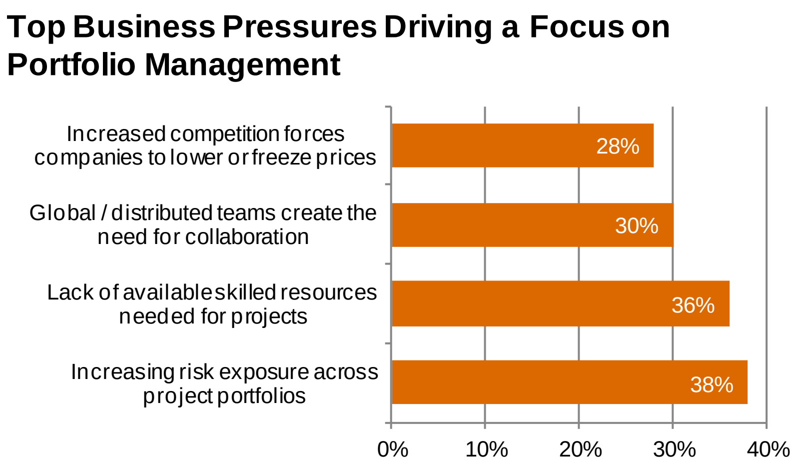

Figure : Top drivers of portfolio management; Aberdeen Research

A further challenge to portfolio leaders is the tendency for senior managers to change priorities as a project is being implemented, according to Aberdeen. What's more, inconsistent processes and a lack of coordination of resources among departments may further complicate portfolio management – particularly if the projects are cross functional and employ disparate tools and methodologies. Often, dissimilar systems for measuring and managing the portfolio, financial impact, and proper project execution create an uncoordinated portfolio management system.

How effective performance management delivers results

The benefits of a mature portfolio management system are myriad.

Organizations with best-in-class portfolios typically complete projects on time and under budget, while increasing ROI in portfolio management. The benefits increase as a company matures its portfolio management capabilities. Businesses that have achieved a mature PM system can gain improved organizational performance through common, integrated processes, architecture, and tools. Communications become streamlined and aligned across stakeholders, enabling leaders to more effectively manage expectations and change readiness.

In a mature PM environment, transparent portfolio standards and methods to prioritize and compare projects – and their benefits – are embedded within the culture. What's more, decision making is enhanced by clear visibility into planning, performance, costs, and results.

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[2] PwC, 15th Annual Global CEO Survey 2012, March 2012
[3] Project management Institute, Pulse of the Profession, March 2012

Mature organizations typically are better able to efficiently manage resources, thanks to centralized strategic sourcing for internal and external resources. Indeed, effective portfolio management can enable an organization to track project status today as well as deliver an analytic snapshot of where the company and its resources will be in the future.

Why investing in governance is essential

A well-designed portfolio management framework alone will not be enough to ensure these benefits, however. Robust governance is critical to the success of an effective portfolio management organization. In fact, an inability to implement effective governance is a primary reason why companies fail to achieve best-in-class portfolio status, according to Aberdeen.[4]

Proper governance will enable an EPMO to achieve better alignment with the business strategy and goals, along with an increased portfolio ROI and project success rate. It can help ensure the portfolio is managed optimally, from project selection to project closure.

- **Issue escalation:** One of the most important – and often most challenging – processes in PM governance is the issue-escalation process. To escalate and resolve issues in a timely and efficient manner, portfolio leaders must develop an easy-to-follow issue-escalation process. They must also ensure that all stakeholders are aware of this process and agree to follow it.

  In doing so, organizations must clearly identify stakeholders who have responsibility for making decisions and define the escalation path for each particular type of issue. An effective issue-escalation process also requires that the organization identify escalation dependencies such as tools, processes, and people who must be involved. Predictability and repeatability should be incorporated into the process so issues are resolved within a specific timeframe with proper resolution communications.

- **Culture of accountability:** Portfolio leadership also must create a culture of accountability. It is critical that objectives are aligned with the organization's annual (and quarterly) performance goals and that portfolio success criteria are based on business value.

  Accountability must empower the governance steering committee with the authority to make decisions and hold people answerable. It is important to ensure that position-based roles and responsibilities sufficiently encourage personal accountability. At the same time, incentive structures – ROI and percentage of projects on budget, for example – must be properly aligned with overall portfolio goals.

- **The role of communications:** To ensure that portfolio accountability is embedded in the corporate culture, portfolio leaders should develop an enterprise-wide communications plan that promotes the performance and business value of portfolio management. Communication is critical because the scope of most portfolios is distributed throughout the organization and is often global.

  Consequently, it is imperative that communications receives due consideration in portfolio governance planning. An effective communications strategy must consistently articulate portfolio management goals, mission, and vision. Communications plans, while centralized, should be customized for disparate stakeholder audiences and communicated via the appropriate channels.

- **Cross-functional coordination:** Just as communications must be centralized, the global nature of portfolios requires that EPMOs are fully aligned and coordinated across functions and divisions.

[4] Aberdeen Group, "Project portfolio management: Selecting the Right Projects for Optimal Investment Opportunity," March 2011

Cross-functional coordination is best achieved by establishing strong portfolio bylaws and a charter that governs portfolio management among disparate business functions and teams. The first step is to assess the maturity of EPMO processes across the enterprise. Once a baseline state is established, portfolio leaders must perform gap assessments as well as understand the desired future state; doing so is critical to standardizing the PM processes across all functions.

Cross-functional coordination typically presents certain challenges. For instance, organizations often find it difficult to manage differing levels of maturity in portfolio management processes across the organization. Similarly, multiple programs from disparate groups must be merged into a single EPMO, and resources must be centrally coordinated and managed. These issues are critical because a lack of cross-functional coordination often results in duplicative spend on systems, people, and processes.

- **Calendar alignment:** Another common challenge is managing the "rhythm" of portfolio projects across multiple business units. Often, projects and programs are delayed because business unit calendars are not aligned.

  Aligning calendars and timing across business units is a complex exercise that must be carefully planned. Portfolio leaders should identify – and enforce – cross-functional principles that guide when, where, and how groups work together. To ensure success, we recommend that EPMOs create and practice calendar-alignment exercises across business units.

  At the same time, project leadership must also ensure that the business requirements are in synch with those of IT. Doing so will require cross-functional service-level agreements (SLAs) that take into consideration multiple hand-off points and dependencies.

- **Process automation:** Effective governance requires automation of processes. All too often, significant efforts are made to develop, negotiate, and settle on a governance process, but the process itself exists only on paper and not in practice. The policies must be conveyed automatically through standard PM communications tools such as a regularly updated FAQ policy portal. An investment in IT solutions may not be necessary because these processes can be automated using existing workflow platforms such as Microsoft SharePoint.

How financial discipline can pay off

Successful portfolio managers understand they must go beyond financial "engineering" to achieve true financial "discipline."

Financial engineering begins by incorporating the design elements and controls that, in theory, create an optimized portfolio. For example, a project-acceptance process must be developed, approved, and implemented. A core element of that acceptance process includes considerations such as net present value, payback, and internal rate of return. From a finance perspective, managers should determine thresholds for acceptance or rejection, then build models for evaluation and determine the appropriate weighting of project attributes.

But when the engineering is complete, portfolio leaders need proven best practices to help provide the right level of discipline to manage the portfolio. Following are some of PwC's best practices for ensuring necessary discipline.

For many organizations, design of the project/program acceptance criteria presents a challenge. In fact, research has proved that a poorly defined portfolio decision criteria for acceptance is the third largest challenge for today's PMOs (resources and risk are first and second, respectively).[5] Including financial benchmarks such as net present value in the decision-making process seems intuitive, yet dollars tell only part of the story.

[5] Ibid.

A well-designed project/program acceptance criteria will impact, at the minimum, four disciplines: strategy, financial, risk, and technical. Other areas that might be impacted include time to implement and people and resources. To ensure effective project/acceptance criteria, portfolio leaders should consider:

- Proper program alignment with corporate strategy
- Financial parameters and milestones for acceptance
- Risk parameters
- Structural architectural changes
- Appropriate weighting for each of these considerations

These factors should be considered in a matrix that includes, at a minimum, strategy, financial, risk, and technical considerations that are unique to each business.

It is critical that organizations employ standardized financial benchmarks as part of the acceptance criteria during business-case reviews. Indeed, research shows that financial discipline at the beginning of the portfolio-acceptance process pays off downstream. Organizations with best-in-class project management review the potential for revenue or return 35% more than others before accepting or approving new projects. And when compared with other firms, companies that get portfolio management right tend to assess past performance as an indicator of future efficacy.[6]

Leading EPMOs also tend to frequently measure KPIs. Performance management tools such as scorecards (both balanced- and revenue-based), dashboards, and reports are effective methods for reviewing a portfolio's relative health. Do keep in mind that financial reviews should occur at all levels of the portfolio.

The benefits of standardized KPIs include improved consistency across projects, better managed expectations, and closer alignment of goals and accountabilities. Metrics can help ensure that appropriate levels of consistency and objectivity are applied when making decisions about an organization's portfolio. Standardized, simplified KPIs also provide proactive insight into underperforming projects that enable management to take action during implementation. Because they are standardized, they can help PMO managers articulate to senior leadership the "big picture" rationale for portfolio decisions.

Many companies find it enormously challenging to align metrics and standardize how they're calculated. Often, they do not agree on the right KPIs to measure performance; when they do concur, many organizations cannot reach consensus on thresholds for action. Research demonstrates that investing adequate time upfront to standardize KPIs will bring substantial benefits later. For instance, Aberdeen has found that 67% of best-in-class EPMOs standardize performace metrics to assess portfolio health and value, compared with an industry average of 39%.[7]

Invest in benefits-realization metrics and manage it closely

Most companies implement a rigorous process to review and accept projects based on financial benchmarks and business cases that promise enhanced productivity and cost savings. But many companies fail to follow through by accurately assessing and articulating the value that projects generate after implementation.

A careful assessment can help stop underperforming – and ineffective – projects early. This step is key because, once a project or program has been approved, the unexpected can (and very often does) happen. Resource challenges, unforeseen technology problems, and shifting strategies are common. Such impediments are often detected late in the cycle, and EPMOs typically are unwilling to halt projects in progress.

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[6] Ibid.
[7] Ibid.

This is where benefits-realization success metrics prove their value. EPMOs that continuously track and manage the progress of benefits realization can more easily identify poorly performing projects early on. And that makes it easier to manage risk and -stop programs before wasting additional resources.

A careful benefits-realization process should be embedded throughout the life cycle of each project. It is critical that the organization implement a benefits-realization process with regular reviews prior to acceptance of a project. Thereafter, it is essential to maintain an unwavering focus on benefits realization, whether the metrics are based on ROI, revenue generation, cost savings, quality, user adoption or some other value. Also necessary is a consistent and comprehensive framework for portfolio reporting.

What this means for your business

The forecast for business remains uncertain, but many organizations are preparing for innovation and growth, particularly in developing markets. These changing priorities and increasingly complex projects have magnified the risk of project failure and business efficiency.

Today, many organizations are responding by attempting to improve the efficacy of portfolio management. A framework that ensures end-to-end portfolio management, from idea to execution, is a necessary start, but only the beginning.

Successful project management requires a renewed focus on governance and financial discipline. Implementing these added dynamics is not a one-size-fits-all proposition, however. Each business will require a customized set of tools, processes, and methodologies to help realize the most effective portfolio management.

Many organizations lack the expertise necessary to take a step back and critically assess their project management strategy for proper governance and financial responsibilities. PwC can help project leaders understand their PM risks and needs, and then design a project management strategy that addresses the complex issues involved with governance and financial discipline.

Our experienced portfolio management team provides the tools, methodologies, and people to ensure accurate assessment, design, and delivery of an effective PM strategy. We have helped leading businesses develop and mature their strategy to achieve excellence in portfolio management and the business benefits that come with it.

In today's tentative economic environment, a renewed focus on effective portfolio management can bring competitive advantages, reduce costs, and lower risk. It can make your company a top performer, and we can help.

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