

Portfolio Management



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Overview

Most enterprises want to improve and grow. They commit resources – people and money – to make it happen. Often, though, the decisions about how to deploy those resources are ad hoc and made intuitively. Too often the result is buyer's remorse. The investments made turn out in hindsight not to have been the most effective at reaching the organization's goals. A portfolio management system establishes a reasoned and thoughtful decision-making process and provides a frame of reference for exercising discipline in making these decisions.

Allocation of Resources

All organizations must allocate resources into a collection of high level "buckets." This starts with differentiating between two major categories: the unavoidable costs of operation and the cost of discretionary activities. The former includes doing the work, paying the bills, getting paid, etc. Decisions about how to spend this money are, essentially, determined from the bottom up. The organization asks itself, "How many people do we need to do these things and what are they going to cost." This is usually called "budgeting."

The latter category includes a variety of possibilities: capital expansion, research and development, acquisitions, reorganization, reengineering, etc. These are all opportunities to innovate in the interests of the organization's long term future. Making decisions about how to deploy resources across this array of possibilities is often also called budgeting, but this is where portfolio management starts to be useful. Is it better to spend money on developing a new product or to spend it on expanding capacity for the existing product line? Is it better to reorganize or to reengineer the organization? Is it better to increase the size of the advertising department or to acquire an advertising agency? Expanding the decision-making to recognize the "pairs" just mentioned is good, but consider the notion that everything should go through a master "funnel" so that all the candidates get equal consideration and a fair opportunity to utilize discretionary funds. This does result in a budget, but it emerges from portfolio management thinking.

At this point, the major resource allocation decisions have been made and a more detailed portfolio management approach becomes useful.

Portfolio Selection Critical Success factors

Within each of the discretionary spending domains, there are usually a lot of candidates vying for access to funding. Which R&D projects ought to get attention? Which capital projects will deliver the most value? What sort of organizational improvement efforts are most likely to produce truly beneficial results? To make decisions that will not later turn out to be unfortunate, a systematic approach is needed.

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First, the organization needs a vision and a supporting business strategy that acknowledges and commits to the relative importance of the particular domain in question. How important is technology development to fulfilling the business strategy and achieving the vision? What about capital projects? How about organizational efficiency? Establishing these mandates at a high level provides a context for innovation planning. Without such a vision and strategic plan, innovation advocates will not have the credibility they need to get their opportunities into play.

Second, the organization needs a domain strategy which supports the business strategy and vision and provides a framework for prioritizing and selecting projects within the domain. What's the best way to spend available capital funds to support the business plan? How should the R&D budget be spent to reach the vision most expeditiously? In many of these domain decision-making situations, there is an initial resource allocation step. For a capital project domain, how much should be spent on "replace in kind / keep it running" projects (to reduce maintenance costs) versus projects that actually increase capacity/capability? In an R&D/technology development domain, how much should be spent on customer support versus incremental improvements versus breakthrough developments? Although it is not uncommon for organizations to have these domain strategies, the strategies frequently do not connect directly to the over-arching vision of the business.

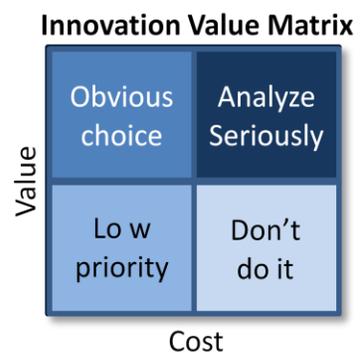
Third, the organization needs a methodology for collecting and screening innovation ideas to harvest the best prospects. This includes having a specific methodology for viewing the data, looking both at new ideas and the potential users. Not only should there be a methodology for identifying the prospects, but for identifying the alternatives as well. Then, in the context of the business vision, the company must delineate operational advantages for each candidate.

Fourth, the organization must have a methodology for ranking/prioritizing the prospective innovation projects. The purpose is:

1. To provide a balance across the cost, risks and rewards spectrum and
2. To incorporate consideration of resource availability (e.g., bud
3. get, personnel, facilities) for development and implementation.

In addition, the prioritization system must be able to accommodate different types of justification. For instance, in a capital projects domain, how to you compare a capacity expansion to building a new office building? How do you compare a discretionary safety improvement project to a discretionary environmental protection project? (One way to do this is to establish a dimensionless scale for each type of project so that the dimensionless scores can be compared directly.)

In this context, the internal lines of business are the "customers" and they need support to help them understand what it is reasonable to want or expect from new initiatives versus what it is possible to get.



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Fifth, the company needs innovation project selection criteria that ensure one of the following two situations:

1. Business/asset customers (i.e., users) are committed and ready to implement each successful innovation project.
2. The potential for rapid acceptance of a new technology by asset managers is substantial.

Commitment Required

Business user “commitment to implement” a new initiative, as evidenced by a written implementation plan, is an absolute threshold requirement for commencing a project.

In recent times, the business management concept has changed globally from a centralized decision-making process to today’s decentralization, which transfers the decision-making to regional business management.

Instead of an organized deployment of the initiative, local business managers are being given tacit permission to “adopt the innovation” or to “opt out” if they wish, resulting in an uncertain value proposition as well as a lengthy adoption cycle that extends over years. Regardless of an initiative’s potential, it cannot succeed without a user willing to put forth a clear commitment to implement. In terms of time, people and money, what will be required? And that “commitment to implement” must be a critical determinant of whether or not the project commences.

Sixth, for each innovation project, the organization must have formally identified and charged a Sponsor – or business Executive in Charge (EIC) -- who sets comprehensive objectives for the project, connects the objectives to the organization’s vision and business plan, explains the project rationale and clearly establishes both measures of success, and sensible constraints and boundary conditions. The EIC should be from the “business” side, representing the business that will benefit from the initiative and provides the project funding.

Portfolio Governance

A good investor does not spend a lot of care in deciding which stocks to buy and then go to sleep and hope for the best; the good investor watches the performance of the purchased stocks and makes adjustments as appropriate. Similarly a good portfolio management system does not end with deciding which initiatives to fund. It includes a system for monitoring the initiatives to make sure they are evolving as expected and that the initiatives still makes sense in an evolving business environment.

This is where portfolio management system intersects with a program/project management system. In an optimum situation, the program/project management system is based on a stage and gate approach and the gatekeepers provide the portfolio governance. They are the ones who “watch the stock”, making sure that the initiative is developing appropriately, that the objective is being properly honored, that the constraints and boundary conditions are being respected and that the expenditures and deployment schedule are on track. In addition, the gatekeepers ensure that the business environment continues to justify

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continuation of the project; the project may be proceeding flawlessly, but if the business case is falling apart, the project should be terminated.

Implementation

Portfolio governance continues into implementation. When development is complete, the “new thing” must make it into the real world. The new capital facility must be operated, the new product must be marketed and sold, the new IT system must be used. There are four key success factors in implementation:

First, the organization’s top management should take two specific actions.

1. They should set clear usage/compliance expectations
2. They should thoroughly and effectively communicate these expectations to all affected managers and employees who are expected to support and utilize the innovation.

It is not necessary that all potential users adopt the new innovation; however, it is necessary that sufficient users sign up to be consistent with the original project justification.

Second, the organization needs to keep affected personnel informed about, and mobilized around, an innovation’s implementation schedule including milestones, required training, support systems and deadlines.

Third, the organization should insist that all affected personnel participate in awareness, system use, and work process training as relevant to their various roles, learning how to operate with the new innovation and how to make money with it.

Fourth, the company needs to measure outcomes of innovation projects in terms of both project results and the effectiveness of the portfolio/project management system itself. Again, the real test is whether or not the innovation makes money. Is it a technical success but a business failure?

Summary and Call to Action

There are always a lot of proposals to use discretionary funds for a variety of purposes. Mature business processes like Portfolio Management are needed to ensure that the available funds are distributed in a way that optimally supports the corporate vision and business strategy. Otherwise, organizations are left with mushy projects that actually decrease business results and limit careers.

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About Endeavor

Endeavor Management, is an international management consulting firm that collaboratively works with their clients to achieve greater value from their transformational business initiatives. Endeavor serves as a catalyst by providing pragmatic methodologies and industry expertise in Transformational Strategies, Operational Excellence, Organizational Effectiveness, and Transformational Leadership.

Our clients include those responsible for:

- Business Strategy
- Marketing and Brand Strategy
- Operations
- Technology Deployment
- Strategic Human Capital
- Corporate Finance

The firm's 40 year heritage has produced a substantial portfolio of proven methodologies, deep operational insight and broad industry experience. This experience enables our team to quickly understand the dynamics of client companies and markets. Endeavor's clients span the globe and are typically leaders in their industry.

Gelb Consulting Group, a wholly owned subsidiary, monitors organizational performance and designs winning marketing strategies. Gelb helps organizations focus their marketing initiatives by fully understanding customer needs through proven strategic frameworks to guide marketing strategies, build trusted brands, deliver exceptional experiences and launch new products.

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