Catalyst PMO: Driving Innovation & Business Value

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The facts are sobering. According to a recent McKinsey & Company survey, 81 percent of global executives surveyed see technological innovation as a critical global trend. Unfortunately, 79 percent of CIOs and CTOs, but only 71 percent of their business counterparts, believe that innovation makes their companies more profitable.[1] This gap reflects a frustration among non-IT executives about the IT organization's perceived inability to deliver tangible value to business.

Eighty one percent of global executives surveyed see technological innovation as a critical global trend.

Another study by Aberdeen Group[2] found that new products at companies defined as "best in class" in terms of meeting product-development targets returned substantially higher profit margins than was the case at other companies. The research showed a vital connection between product portfolio management implementation and achieving "best-in-class" status.

A majority of firms have unbalanced product portfolios in which less than 5% of products account for more than 90 percent of profits

The research additionally looked at the intensity of adoption, and found leading companies suggesting "80% reporting adoption of production innovation processes by more than half of their intended users."

Most importantly, these leading firms delivered the goods and the profits. Forty-three percent reported profit-margin improvements of at least 75% vs. older products on products less than two years old. Innovation seems to pay well!

Still other studies suggest that a majority of firms have unbalanced product portfolios in which less than 5% of products account for more than 90 percent of profits. This suggests risk-averse behavior by organizations, as well as a failure to cultivate a culture of innovation.

The Project Management Office (PMO) can play a vital role in making a significant and clear contribution to business innovation, helping to improve performance, reduce risk and enhance value. By integrating and driving processes surrounding culture, visibility, credibility, collaboration and governance, the PMO can leverage its strengths in planning, execution and toolset automation, while driving the innovation process for the enterprise.

[1] McKinsey Quarterly Global Survey of Business Executives, Fall 2005
[2] New Product Development: Profiting from Innovation, Jim Brown, Aberdeen Group

Why Innovate?

Innovation is the successful exploitation of new ideas and is a vital ingredient for competitiveness and productivity within businesses and organizations. Innovation involves the successful exploitation of new ideas in any setting. Indeed, it can be anything from changing a daily business procedure and designing a new product for sale to discovering a new drug that eliminates heart disease. Innovation is also an attitude, a state of mind, and a creative process, as much as a specific task or action. As a result, innovation is a source of competitive advantage and a necessary component for the going concern of the enterprise.

A handful of very obvious reasons exist for companies to develop a repeatable innovation culture. These are provided below.

- General Progress
- Organizational value synergy
- Customer intimacy
- Opportunity advantage
- Organizational development
- Employee enrichment

When properly managed, corporate resources can make a significant and clear contribution to the business, helping to improve performance, reduce risk and enhance value.

Business value and innovation are intricately tied together. In the pharmaceutical industry, it costs $802 million, on average, to develop and win market approval for a new drug in the United States. Improving discovery program productivity or using better pre-clinical screens to increase success rates from the current 21.5% to one in three could reduce capitalized total cost per approved drug to $242 million.[3]

Other examples include $100M in savings from a specification management system handling artwork and packaging at a large consumer packaged goods manufacturer and the simultaneous shortening of vehicle development cycle time while increasing engineering productivity at a global automotive manufacturer.

The examples cited illustrate the business value gained (reduced costs, enhanced savings, and accelerated time to market) as a result of the proactive involvement of the technology function in delivering innovation. Clearly, when properly managed, corporate resources can make a significant and clear contribution to the business, helping to improve performance, reduce risk and enhance value.

Role of the PMO in Driving Innovation and Value

The Program Management Office (PMO) plays a vital role in making a significant contribution to innovation and driving business value. The PMO is the final arbiter in ensuring that companies manage their portfolios effectively. The portfolio can consist of new products in development, on-going operational/tactical projects, as well as other regulatory/compliance initiatives.

[3] Tufts Center for the Study of Drug Development

Within IT as an example, it is a well-established fact that demand far out-strips supply. At a business level, a best practice organization will have more ideas than capacity for development. In this case, it is the PMO's role to judiciously determine which ideas merit further investment and which should be discarded. In an IT setting, this translates into a portfolio management exercise with key business stakeholders providing input and feedback into the process. In a business innovation setting, the process remains the same, albeit the stakes may be significantly higher.

It should be noted that the PMO (whether as part of IT or the business) does not own the innovation or the idea, rather it should function as a mechanism to deliver the innovation within the confines of the defined process. To this end, the PMO function must understand how the organization innovates. Companies may pursue multiple alternatives to find and market new products including strategic acquisitions, external networks using partners and the academic community, internal skunk works, and even affiliated idea factories. Rather than treating all ideas equally, understanding the innovation's genesis helps the PMO in determining the appropriate process to follow in bring it to market. For example, a breakthrough idea (developed internally via a skunk works initiative) may be treated differently than a product line extension (developed at an idea factory).

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A Six-Step Approach to PMO-Driven Innovation

The PMO is also the key mechanism for ensuring that the basic tenets of innovation and business value are delivered. These include accelerating speed to market, reducing costs, and creating new competitive categories that result in market advantage. The specifics with respect to how the PMO drives business value via innovation are provided via the six-step process below.

Culture of Innovation– A strong innovation-oriented culture is the end result of resilient product-development links and relationships between technology, business units, and the PMO. Start with engineers who have the clout to lead the product-development process. Then provide the right incentives to ensure lasting impact and continued cultural advancement within the PMO.

In order to participate equally in the business innovation process, the PMO must speak the language of business, rather than the language of programs and technology.

Maintain Visibility - Business executives tend not to see the overall results and impact of spending and activities outside their business units. The PMO must make the business value of its constituents more visible and transparent. This translates into full disclosure on budgets, actuals, timing, resource constraints, etc. with key stakeholders.

Language of Business – In order to participate equally in the business innovation process, the PMO must speak the language of business, rather than the language of programs and technology. This may require a vastly different skillset than is currently available, yet it is a reality already affecting the CIO today. A thorough knowledge of market conditions, geo-political concerns, the competitive

environment, as well as corporate financials, objectives, and perspectives, are all key requirement areas.

Land and Expand - Establish credibility on a departmental level and leverage it for the greater corporate goals and objectives. Celebrate the successes, no matter how small they appear. Early notification is critical and is a primary contributor to building credibility and ensures that all parties are fully aware of any risks and their potential mitigation plans.

Nearly 85 percent of product costs are committed during the conceptual, project definition, requirements and constraints gathering, and prototype creation and testing phases of a product's life cycle.

Collaborate and Communicate – Corporate talent pools tend to be geographically dispersed. The organization's ability accelerate its best ideas to market is directly related to building a collaborative team-based environment. A variety of tools are available to assist in location agnostic team building, intellectual knowledge capture, document management, etc. Marrying technology to the process in this case will be a key success factor.

Plan, Align & Govern – Nearly 85 percent of product costs are committed during the conceptual, project definition, requirements and constraints gathering, and prototype creation and testing phases of a product's life cycle. The PMO has a tremendous opportunity to positively impact the process surrounding these areas.

This is what the PMO does best. The role of the PMO in innovation involves taking advantage of technology to create new products and services, or to take the company into new markets. The PMO must be strong on planning, ensuring alignment with strategic objectives, effective risk assessment, management and mitigation, and allowing for early notification of issues.

PMO leaders looking to play a greater role in the corporate innovation process should look to the six-step process prescribed above as a starting point in their involvement and also use the guide as a way to influence other business unit executives.

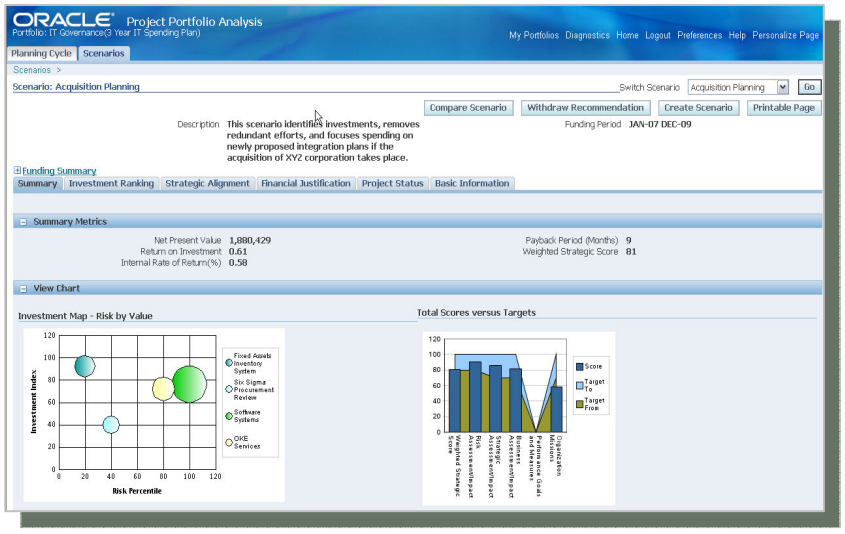
The Role of Project Portfolio Management Tools

Project Portfolio Management (PPM) tools are increasingly becoming the chosen method in delivering the business value and fact-based decision making required to instill an innovation oriented environment. These tools, steeped in project and resource management, and process based functionality, can help organizations determine cost and benefit drivers, provide visibility into early warning signals, and also deliver perspective and analysis into the right mix of innovation, products and/or investments.

Prioritization and the PMO

Starting at the top, it is critical for the PMO to understand how to prioritize investment requests to align with strategic initiatives, key business requirements, available resources, and available funding. Fundamental questions must be answered including:

- Why should this initiative be funded?
- What are the best possibilities of initiatives, or portfolios of projects, that an organization can implement given the available budget and organizational capabilities?
- Are we over-investing one particular product/program/area?



This depth of analysis helps managers and executives from product, engineering, and the business unit side of an organization understand the tradeoffs between portfolio value and cost.

Specifically this analysis can help organizations understand:

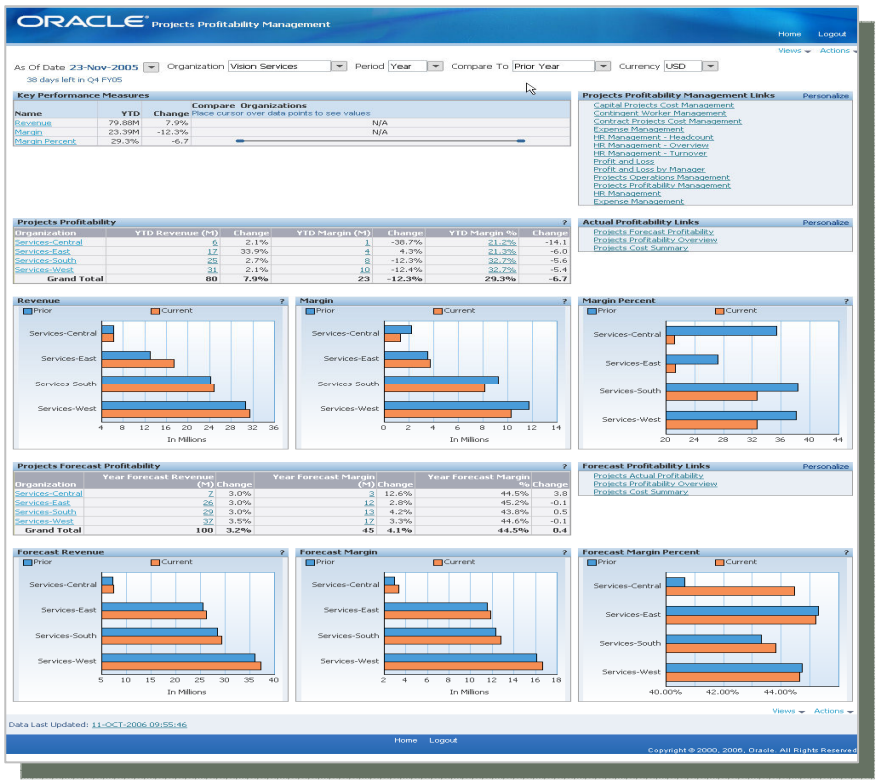
- The concept of "scarcity" and its consequences

- "Value and Cost" and its graphical presentation
- Concepts of and relationships between value, cost and current operating practices
- "Breaking the Constraints" and its impact on the organization's innovation potential

Perhaps most importantly, once a portfolio is agreed upon, it can help executives understand whether the organization is getting the best from its potential portfolio of projects, and if not, why.

Understanding Profitability

It is important for the PMO to understand the constraints under which it operates. Similarly, the automation engine assisting in the selection process must be able to accurately convey these constraints and present meaningful data for improved decision-making.



The graphic above illustrates a dashboard view into the profitability equation for a particular scenario. This kind of insight allows PMO's to analyze scenarios with the objective of avoiding being blind-sided. In the case above, insight is provided into:

- Portfolio profitability by region

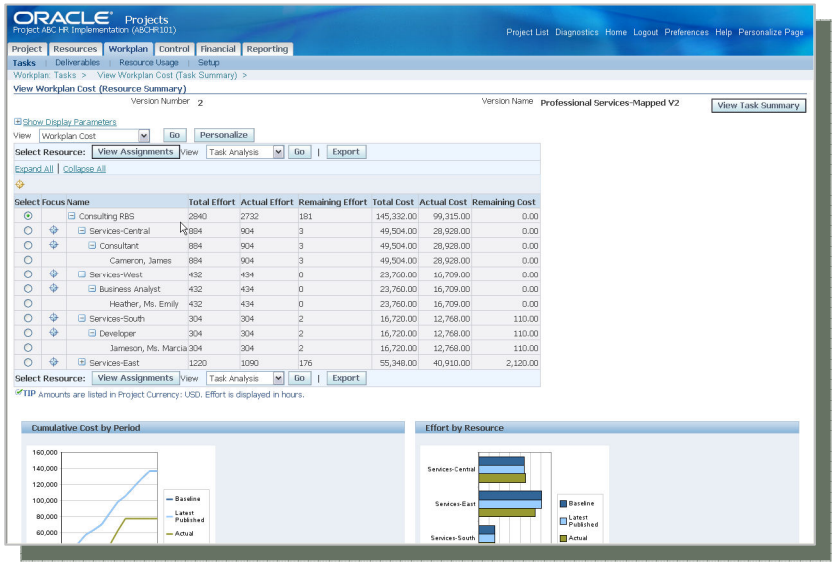
- Comparison of forecast vs. actual margins
- Drill downs for additional detail

Depth of detail into revenue and margins are vital components of the catalyst PMO and can be a key driver to help bridge the credibility gap that many PMO's face with the business. This analysis assists the PMO and the business units they serve to:

- Monitor actual & forecast project profitability by numerous dimensions
- Drill to detail and monitor profit margin on each type of project cost
- And importantly, determine which investments succeeded, which did not, and why?

The Resource Dimension

The resource dimension plays an important role in the creation of the innovation mind-set. While a traditional project management approach is to assign available resources to a particular task, the best practice innovation minded organization will ensure that the "right" resource is allocated to a high-value, business aligned investment initiative.

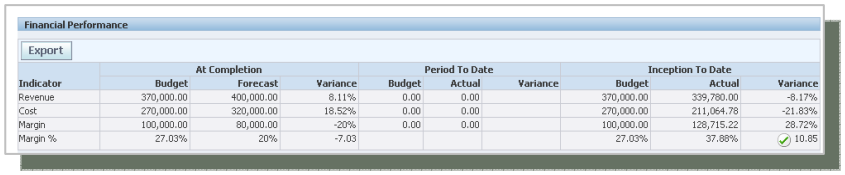


This nuance is represented via the dashboard above, where cost and effort of resources is made available.

Budgets and Profits

A common mistake in innovation driven processes is to overlook to the financial dimension. The language of business revolves around money. As a result, it is

critical that the PMO understand and share insights into the budget and forecasts of an investment. Successful PMO's understand the power of number and use them to ensure fact-based decision making. This is especially true in innovation oriented efforts where return on investment is tied to the overall costs of an initiative.



Financial Performance

Export

	At Completion			Period To Date			Inception To Date		
Indicator	Budget	Forecast	Variance	Budget	Actual	Variance	Budget	Actual	Variance
Revenue	370,000.00	400,000.00	8.11%	0.00	0.00		370,000.00	339,780.00	-8.17%
Cost	270,000.00	320,000.00	18.52%	0.00	0.00		270,000.00	211,064.78	-21.83%
Margin	100,000.00	80,000.00	-20%	0.00	0.00		100,000.00	128,715.22	28.72%
Margin %	27.03%	20%	-7.03				27.03%	37.88%	10.85

At a finer financial analysis level, automating the budgeting process around the investment ensure that the effort is kept on track and allows for mid-course corrections if necessary. In particular, it can help answers questions including

- How does the organization effectively budget, track and forecast the financial impact of its investments?
- How does the organization maximize the benefits achieved from its investment in a particular portfolio?

BOTTOM LINE RECOMMENDATIONS

To succeed in today's challenging innovation environment, create the innovation mindset, and deliver business value via profitable growth, organizations must ensure that the PMO plays a catalytic role. As a result, organizations must:

- *Build an innovation oriented culture.* Ensure strong product-development links and relationships. Start with engineers who have the clout to lead the product-development process.
- *Organize for innovation success.* Best-in-class performers are more likely to have centralized control. Consider organizing new product development across departments underneath a key executive such as a chief product officer or chief innovation officer and operating projects under a central project manager or project management office (PMO).
- *Motivate.* Provide the right incentives to ensure lasting impact and continued cultural advancement.
- *Understand how the organization innovates.* Companies may pursue multiple alternatives to find and market new products. These include strategic acquisitions, external networks using partners and the academic community, internal skunk works, and affiliated idea factories.
- *Keep an eye on early costs.* The Defense Advanced Research Projects Agency (DARPA) finds that nearly 85 percent of product costs are committed during the conceptual, project definition, requirements and constraints gathering, and prototype creation and testing phases of the product life cycle. An improvement in the process surrounding these areas, enhanced communication and executive visibility as well as a reduction in related costs are a vital link to gaining a competitive edge.
- *Communication & Collaboration.* A variety of tools can help facilitate these processes and help to shorten the product development lifecycle by involving internal and external constituencies regardless of geographic location.
- *Effectively Use Toolsets at their Disposal.* A variety of powerful engines can provide the depth of analysis, project and portfolio strengths, and optimization capabilities needed to deliver business value.

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