Portfolio Risk Management

Whilst many organisations undertake a risk-based assessment when determining which projects or programmes to include in their portfolio of work, this assessment tends to be static rather than dynamic. That is, the risk-based assessments are only undertaken at the beginning of the funding cycle and those assessments are not revisited at anytime during the life of a project or programme. Thereafter portfolio risk management is typically relegated to a simple administrative task of collecting, collating and summarising the risks facing the individual projects and programmes that make up the portfolio.

Such an approach can lead organisations to loose sight of the forest because it has been focussing on the trees. Organisation can focus on the statistics and forget the bigger picture.

Portfolio risk management should be more than the summation of risks to its component projects and programmes. Portfolio risk management should be about looking at projects and programmes that pose a high risk to the portfolio or organisation rather than looking at projects or programmes that have a large number of high risks.

Using the International Standard for Risk Management (ISO 31000) as a guide, lets look at how portfolio risk management might look at under the paradigm of focussing on projects and programmes that pose high risks rather than focussing on projects and programmes with high risks.

Establishing the Risk Management Context

Risks posed by a project or programme are the potential for damage to organisational capability and/or objectives due to the failure of the project or programme. This damage will be the greater of:

- the direct cost of the project or programme;
- the expected benefits from the project or programme; or
- the expected benefits from another project or programme that would have been undertaken but for the fact that the resources were allocated to this project.

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- the expected benefits from any dependant projects or programmes; and/or
- the impact on business should the performance of any production system be degraded by the establishment and embedding of the project.

Unfortunately, many of the expected benefits claimed for projects and programmes are not expressed in fiscal terms. Therefore it is not possible to compare direct costs of a project or programme with its expected benefits to determine whichever is the greater. That said, given the rigour most organisation undertake in selecting projects and programmes in the first instance it should be reasonable to assume that:

- the expected benefits outweigh the direct costs of the project or programme; and
- the ratio of expected benefits vs costs of a project or programme are better than the same ratio for any other project or programme that has not been undertaken due to resources being expended on this project.

Therefore, for the purpose of determining the risk posed by a project or programme, the expected benefits from the project or programme could be used as the basis for determining the potential damage caused by the failure of the project or programme.

Indentifying Risks

As stated at the outset, the form of portfolio risk management proposed by this paper treats each project or programme as a risk to the portfolio or organisation. Hence, just as each project or programme has individual risks that pose a threat to their success, the projects and programmes pose a threat and are hence the risk to the success of the portfolio or organisation.

Accordingly, each project and programme is a risk to the portfolio or organisation.

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Analysing Risks – likelihood

In the context or portfolio risk management, risk likelihood is akin to the likelihood a particular project or programme will fail.

Enter now the dynamic element of portfolio risk management because the likelihood of project or programme failure may vary over time. Furthermore, there is more than one factor that contributes to likelihood of project failure. Whilst the literature is replete with material on why projects fail, a portfolio manager could do far worse than look at the following to provide likelihood ratings for portfolio risks:

Event	Likelihood
One or more of a project's cost, schedule or scope are outside tolerance	Almost Certain
More than one of a project's cost, schedule or scope are outside plan but within tolerance	Likely
A project's cost, schedule or scope are outside plan but within tolerance AND There are at least two other KPIs that are outside normal bounds	Possible
Any one KPI is outside normal bounds	Unlikely
All KPIs are within plan / normal bounds	Rare

Analysing Risks – consequence

As stated previously, it is reasonable to assume that for the consequence of project failure is the loss of expected benefits. To enable a comparative analysis between the risks each project or programme poses to the portfolio, each of these consequences need to be graded or ranked in the same manner that the consequences of individual events are rated for a project or programme.

For consistency across risk management approaches used within an organisation's project, programme and portfolio management environment, it is recommended that portfolio risk consequence (ie. the loss of benefits from projects/programmes) be ranked as either Severe, Major, Moderate, Minor or Insignificant.

Now the description/quantification of each of these rankings will differ between organisations. However, it is suggested that they align to the same categories used when the organisation undertook its risk-based assessment of risks when it was first determining what projects or programmes would form part of the portfolio.

Analysing Risks – risk rating

As with the rating of risks in other environments, the following matrix of risk likelihood and consequence can be used to determine a rating for the level of risk a project or programme poses to the portfolio or organisation.

	Insignificant	Minor	Moderate	Major	Severe
Almost Certain	Medium	Medium	High	High	Extreme
Likely	Medium	Medium	Medium	High	Extreme
Possible	Low	Medium	Medium	High	High
Unlikely	Low	Low	Medium	Medium	High
Rare	Low	Low	Low	Medium	High

Evaluating Risks

Portfolio risk ratings do not lend themselves to the evaluation and treatment of risks per se. Rather, portfolio risk ratings are used to rank/order projects and programmes for consideration and/or review at an organisation's governance forums. In this way, governance forum members will be encouraged to focus their attention on projects and programmes that pose a high risk to the organisation rather than projects and programmes with high risks.

Treating Risk

As noted previously, as projects and programmes progress their likelihood of failure, and hence their portfolio risk rating may change. In response to changes in a project/programme's portfolio risk rating an organisation's governance forum should reconsider the ongoing viability of that project or programme and may elect to:

- choose an alternative, lower risk, approach for delivering the project /programme outcomes;
- place the project /programme on hold until existing/new technology becomes 'proven'. In this way a project/programme will reduce its risk rating by stepping back from the 'bleeding edge';
- reduce the scope of the project/programme to reduce risk exposure, acknowledging that

there may be a consequential reduction in costs and expected benefits; or

- terminate the project/programme and accept the loss associated with the expenditure incurred to date.

Monitor and Review Risks

In accordance with an organisation's normal project and programme governance processes, project and programme managers would be expected to provide regular (typically monthly) status reports. The performance information (eg. schedule, cost) can be used to recalculate a project's likelihood of failure (see above) and hence a project's new portfolio risk rating. The recalculation of the portfolio risk rating for all projects and programmes within a portfolio may result in some project and programmes rising up in the order of priority for consideration by the organisation's governance forum.

Conclusion

The above portfolio risk management approach will ensure than organisations' governance forums focus on projects and programmes that pose the greatest risk to its success, rather than the projects and programmes that have the greatest number of high risks.