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Portfolio decision-making genres: A case study

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ABSTRACT

This article addresses the portfolio management practices and challenges of contemporary firms. Based on a review of the extant literature on project selection, termination and deletion decisions, we conducted an in-depth interview study with 19 key informants in 11 multinational firms. We identified three genres of portfolio management decision making: formalist-reactive, intuitive, and integrative. Each genre can be described by a unique set of portfolio management practices. For example, formalist-reactive firms rely on quantitative criteria while intuitive firms prefer qualitative criteria. In addition, each genre has to overcome a unique set of challenges. We discuss the three genres in detail and provide several implications for portfolio management decision making.

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1. Introduction

In today's competitive environment, continuous innovation is necessary to sustain long-term business growth (Hauser et al., 2006). The proliferation of new products is often seen as a prerequisite of innovation; however, if not managed proficiently and in line with the firm's strategy, the negative impact of poor portfolio decisions on performance can be significant (Cooper et al., 2001b; Chao and Kavadias, 2008). A search of the news archives of the popular business press provides various examples of firms losing money due to poor portfolio management decisions. For example, optical gear developer Nortel experienced substantial holes in its product portfolio in 2001, and subsequently lost considerable market share to its main competitor Cisco. Bayer, a global enterprise in health care, nutrition and high-tech materials, experienced such delays in their pipeline in 2002 that long-term

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growth was at risk. Also Bill Ford stated in 2006 that it was due to the failure of management to make the right portfolio decisions that Ford Motor got into trouble.

The portfolio management challenges that companies experience should not be underestimated as they can have severe consequences for a firm's long-term competitive position. Recent research shows that within many firms the new product development (NPD) focus has shifted from radical to incremental innovation, and that portfolios have become unbalanced and not in line with the aspired strategic direction (Barczak et al., 2009; Cooper et al., 2004a, 2004b, 2004c). In addition, NPD project portfolios have become overloaded, leading to situations such as fire fighting (Repenning, 2001), in which portfolio managers are constantly occupied resolving urgent problems, thereby losing the 'big picture'.

Today's successful companies across many industries recognize the importance of proficient portfolio management and emphasize it in their business vision. For instance, Novo Nordisk, a Danish pharmaceutical company, states that it is their "*broadest diabetes portfolio in the industry*" that makes them world leader in diabetes care. Hewlett Packard (HP), a global technology leader, claims that "*No other company offers as complete a technology product portfolio as HP*"; and Nestlé pronounces as one of their key business principles that they do not "*favor short-term profit at the expense of successful long-term business development*" (Nestlé annual report 2007).

There have been regular calls in the literature to attend to the importance of developing effective portfolio management processes for business success (Cooper et al., 1999, 2004a, 2004b, 2004c; Hauser et al., 2006). However, to date, the focus has primarily been on methods for individual NPD project selection (Englund and Graham, 1999; Cooper et al., 2001a; Blau et al., 2004), on strategies for product deletion (Avlonitis et al., 2000; Saunders and Jobber, 1994), and on investigations into the role of human limitations in termination decisions (Balachandra et al., 1996; Biyalogorsky et al., 2006). Despite these efforts to investigate NPD decision making at the individual project level, insights that prevent or resolve challenges in the daily practice of portfolio management do not abound (Eggers, 2006). This is unfortunate as it is a far bigger challenge to maintain an overview of the entire portfolio and to make decisions from a strategic perspective than to make individual project selection, termination or deletion decisions (Cooper et al., 2000).

Following Cooper et al. (2001a), we do not view portfolio management as a singular process but as a span of interrelated decision-making processes that aim to refine and implement the firm's strategic goals by allocating the available resources. The decisions that have to be made in the portfolio management system occur at various levels in the firm involving different departments, and thus manifold decision makers pursuing various divergent goals. Taking this into account, it is undesirable to model portfolio management as a one-dimensional linear system (McCarthy et al., 2006). Therefore, we conceptualize portfolio management as a complex system of interrelated and recursive decision-making processes. The objective of the portfolio management system is to translate the business strategy into a dynamic set of NPD projects and products, that:

- have not yet started and are subject to project selection decisions;
- are in development and subject to project continuation or termination decisions; and
- are launched into the market and subject to product continuation or deletion decisions.

This case study is organized into five sections. Section 2 provides a literature review on portfolio decision-making in which we discuss the existing streams of research. Section 3 describes the methodology and date collection strategy. The research results are provided in Section 4. Discussion, implications, and research limitations are articulated in Section 5.

2. Portfolio decision-making

Portfolio decisions (i.e., selection, termination, and deletion decisions) deal with uncertain information and require a long-term vision. These decisions should not only be based on individual project characteristics but they should also be placed in the context of the whole portfolio and the achievement of strategic goals. Three wide-ranging goals for obtaining strong portfolios have been identified (Cooper et al., 2001a): *strategic alignment*, i.e., the alignment between the firm's business

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