

ROI Metrics in Governance and BPM

A discussion about what metrics to use in project valuation in Governance and Business Performance Management

Abstract

A research study conducted by Glomark-Governan indicates that over 70% of the Fortune 1000 companies have already implemented a Corporate and/or IT Governance function, and over 45% have implemented a Business Performance Management (BPM) system—also known as Corporate Performance Management (CPM), or Enterprise Performance Management (EPM).

While the majority of these companies have been able to improve their overall business results with the use of a Governance function and a BPM system, Glomark-Governan found that 80% of the managers and executives in these companies are still not sure what metrics to use to best assess and measure the ROI and economic value of specific projects, such as the case of information technology initiatives.

In many companies Corporate and IT Governance demands the use of projects' ROI assessments. At the same time, using KPIs, BPM systems are effective for tracking the performance of managers and professionals throughout an organization, and in some cases aligning employees' goals to corporate strategic goals. Nonetheless, we found that business and technology professionals in many of these organizations still need to know which metrics to use in order to best assess and measure the economic value of specific technology projects.

In order to assist managers and executives that are using Governance and BPM systems, this paper presents and discusses a Glomark-Governan's three-tier model for organizing metrics to best measure the economic value of individual projects.

Note: The model presented in this paper includes elements of the Economic Value Creation™ (EVC™) methodology developed by Glomark-Governan, and available through the Glomark-Governan's Genius software.

Defining Metrics –Art or Science?

For many, the use of metrics is an art—these are individuals that do not know how to align and organize metrics in different types. To others— like individuals that have been exposed to BPM systems or use the Glomark-Governan EVC methodology— metrics are a science.

In the BPM or Business Performance Management world, there are various metrics-oriented methodologies currently available and widely used, such as the Balanced Scorecards. These methodologies are designed to measure the performance of people and business units; but are not necessarily structured to assess the ROI of specific projects in a structured and practical way.

Our definition of Governance:

“Governance specifies the decision-making authority to communicate and track desirable performance, accountability and behavior throughout the organization”

To assess the value of technology or non-technology projects it is important first to understand that people use metrics according to their job function, and the level they work in an organization. For example, c-level executives tend to use financial metrics, plant managers use operational metrics, and engineering professionals use technology-oriented metrics. For a more specific example consider that when assessing the value of a mainframe project a CFO will use a financial metric, such as Internal Rate of Return (IRR),

At Glomark-Governan we are often asked... “What is the best metric to assess and measure the ROI of individual projects?”

while an IT manager may use a technology metric such as MIPS (millions-of-instructions-per-second).

The Science of Metrics in Project Performance Management

There are thousands and probably millions of different metrics and KPIs used in the business world. After 15 years of enhancing and implementing the *Economic Value Creation (EVC™)* methodology, Glomark-Governan has determined that to effectively measure ROI of individual projects and initiatives, people need to use, organize and “link” project metrics at three levels:

- Financial Metrics
- Operational Metrics
- Technical Metrics

Financial Metrics

In order to assess the “financial” return and economic value of a project, executives use financial metrics; such as:

- Payback
- Simple ROI
- Cash Flow and Discounted Cash Flow
- Internal Rate of Return (IRR)
- Net Present Value (NPV)
- Economic Value Added (EVA)

There are other financial and economic metrics, but the ones listed above are the most commonly used by c-level officers and financial executives to measure the return of individual projects. ROE (return on equity) and ROA (return on assets) are also common financial metrics but these are generally used to measure the overall performance of a “company or business unit”. ROA and ROE are generally not used to measure the return or value of individual projects.

Financial metrics are also often used as KPIs (Key Performance Indicators) to track the performance of business units, departments, and projects. KPIs often are “calculated” metrics; where two or more metrics need to be tracked and used to calculate a KPI. Take “EVA” as an example, which is often used as a KPI, and is calculated by dividing net profits minus the cost of capital employed; or “Current Ratio”, which is calculated by dividing current assets by current liabilities.

Additionally, some executives desire to use only “one” indicator in their companies for valuing projects and initiatives. In these cases, using only one financial metric makes the financial valuation job easier; however, executives also know that there are non-quantitative areas that need to be factored when comparing, prioritizing, and selecting projects. Some of these non-quantitative factors often include things like:

- Strategic Value or Strategic Alignment
- Impact on Customer Satisfaction
- Project Risk (e.g., skills of implementation personnel)
- Operational Risk (e.g., impact on business process downtime)
- Technology Risk (e.g., maturity of an application)
- Internal Employee Satisfaction
- Among others

Glomark-Governan assisted the CIO of one of the world’s largest petrochemical companies—that has been using a BMP system for several years—in defining one composite indicator to compare, select and measure the value of new IT projects.

Using a “composite” indicator, made of two or more financial metrics plus qualitative factors, is more challenging for valuing projects but certainly is more objective.

Operational Metrics

The challenge when determining the economic value or ROI of project is not in calculating a Financial Metric, but in linking the Financial Metrics to the technology or initiative under consideration.

In order to effectively value a project (technology or non-technology) it is necessary to first link the characteristics, features, and capabilities of the technology or project under consideration, to Operational Metrics. If Operational Metrics are clearly mapped to the features and capabilities of the technology or service initiative, then the Operational Metrics can be quantified in annual benefits. Subsequently, the Operational Metrics can be then compared to the costs of the initiative and Financial Metrics can be calculated and projects valued. Operational Metrics is at the end what is measured to determine if the investment produced the expected results or not.

Operational Metrics vary considerable from project to project, and industry to industry. It is not possible to define one or a few metrics that can be used across any project. Some projects are aimed at improving the supply chain, and Operational Metrics on those cases can be things such as Tons per Day, Inventory Turnover, Production Cycle Time, etc. Other projects for example can be geared to improving sales process efficiencies; and in those cases Operational Metrics can be things such as proposals-per-month, close-rate, revenue-per-order, etc. In the healthcare industry, as another example, Operational Metrics are things like patience-visits-per day, surgeries-per-month, prescriptions-per-year, etc. These are just a few examples, but there are thousands and hundreds of thousands Operational Metrics that can be used.



Enterprises use Operational Metrics as KPIs to determine company-wide improvements (e.g., a glass containers manufacturing company uses as a KPI the number-of-bottles-produced-per-day); however, projects vary widely, and therefore each project has to have its own set of Operational Metrics in order to determine the project ROI.

In order to define the Operational Metrics for individual projects the Glomark-Governan EVC methodology suggests using a mapping approach using the cause-effect technique. In other words, mapping the features of the initiative (or

technology) to operational impacts (measures) in business functions or business processes.

Note: The Glomark-Governan EVC Methodology includes a more detailed benefits assessment model, called TBO or Total Benefit of Opportunity, designed to identify, assess and quantify Operational Value and Operational Metrics.

Technological Metrics

In technology-oriented projects, the mapping has to clearly identify the Technological Metrics (causes), which are things such as features and functions of the technology or project at hand (e.g., megahertz, number of screens, time to start an application, data transfer time, etc.). Like in Operational Metrics, there are hundreds or thousands of Technological Metrics; and while some Technological Metrics can be used in multiple projects, trying to use only a few to assess “all” projects is not realistic and is ineffective. Each technology project will have a set of Technological Metrics. For online businesses as another example, Technological Metrics include factors such as page-viewed, server-load, network traffic, and transactions-per-second.

Defining, linking and tracking Technological and Operational metrics is a necessity in order to objectively determine if the expected financial performance and ROI of a technological project has been achieved or not after implementation.

The reason why ROI studies often lack of credibility is because of lack of an objective and clear link between the Financial Metric(s) used and the operational impacts (benefits) and the specific features and characteristics (causes) of the technology or initiative implemented.

Summary of Recommendations

1. The use of Metrics must be considered as a Science and not an Art.
2. Companies and organizations must adopt a method for categorizing and grouping different types of Metrics.
3. Glomark-Governan recommends to group and link metrics using a three-tier approach: Financial, Operational and Technological Metrics.
4. Since there are thousands of Operational and Technological Metrics, companies need to define and assess Operational Metrics for “each” project.
5. Defining a weighted consolidated “Financial Metric” that considers qualitative factors is helpful for comparing and prioritizing projects.
6. Companies can use a single or a consolidated Financial Metric to select projects; but in order to measure a project ROI, the operational value must be measured using “Operational Metrics”.
7. As in the case of Corporate Governance, the review of the Projects’ ROI must be done by c-level executives, and should not be delegated.

About Glomark-Governan

Glomark-Governan helps technology providers and buyers assess the value of technology solutions and services by giving them the methodology, training, advisory and software tools they need to effectively assess risk and economic value. Glomark-Governan has tested and refined the Economic Value Creation™ (EVC™) methodology for more than a decade, bringing to market a proven, complete solution that allows buyers and vendors to organize a technology project, define each component's value, and quickly create situation-specific business cases. The suite of Glomark Genius software tools allows vendors and buyers of technology do from simple to comprehensive TCO, TBO and TRO studies of technology assets and services.

For more information, please visit our Website www.glomark.com or contact our main office in Columbus, Ohio U.S.A. at (614) 761-2400.

About the EVC Methodology

The Economic Value Creation™ (EVC™) methodology from Glomark-Governan—which is often mentioned in this white paper and is contained in the Glomark Genius tools—includes models and processes to assess the Total Benefit of Opportunity™ (TBO™), the Total Cost of Opportunity (TCO) and the Total Risk of Opportunity™ (TRO™) of investments in technology and non-technology initiatives.

Total Benefit of Ownership, TBO, Total Risk of Ownership, TRO, Economic Value Creation, EVC, Genius Pro and Genius Analyzer are registered marks of Governan LLC, d.b.a. Glomark-Governan.

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