

INVESTMENT MANAGEMENT STANDARD

Guideline

Understanding and Evaluating a Potential Investment

Investment Management
Department of Treasury and Finance
1 Treasury Place
Melbourne Victoria 3002 Australia

Tel: +61 3 9651 1880
Website: www.dtf.vic.gov.au/investmentmanagement

© Copyright State of Victoria 2010

This publication is copyright. No part may be reproduced by any process except in accordance with the provisions of the Copyright Act 1968.

Published February 2010

This Service Logic and Investment Prioritisation document is part of the Investment Management Standard.

The publications in the 2009 series are:

Overview v3.5
Problem Definition v3.5
Benefits Definition v3.5
Solution Definition v3.5
Business Case v3.5
Investment Reviews v3.5
Benefits Reports v3.5
Service Logic and Investment Prioritisation v1.0
Understanding and evaluating a potential investment v 0.1

More information at: www.dtf.vic.gov.au/investmentmanagement

Contents

1	Purpose of this Guideline	4
1.1	Background.....	4
1.2	Information provided by an Investment Logic Map.....	4
2	Using this Guideline.....	5
2.1	Who can benefit.....	5
2.2	Questionnaire - 'Understanding a potential investment'	6
2.3	Three steps	6
2.4	Understanding the term 'Strategic intervention'.....	6
2.5	Prioritising competing investments	7
3	Appendix A: Glossary	8
4	Appendix B: Example of an Investment Logic Map.....	9
5	Appendix C: Questionnaire - Understanding a potential investment	10
6	Appendix D: What is a 'Strategic Intervention'	12

1 Purpose of this Guideline

This guideline has been developed primarily to assist two groups of people - those people who are involved in shaping potential investments, and the decision-makers who will decide whether a potential investment should be funded.

It provides a way to quickly gauge their level of understanding of a potential investment as the basis for making informed judgements.

1.1 Background

The ability to shape and select those investments that will provide the most value to society is fundamental to good government. This can be a complex exercise that requires the contribution of many different people who each bring their specialist knowledge or viewpoint.

Irrespective of their viewpoint, the basic questions that need to be answered when shaping and selecting investments are:

- What is the problem?
- What is the best strategic response to the problem?
- What benefits need to be delivered?
- What is the preferred solution?

1.2 Information provided by an Investment Logic Map

It is not necessary to have an Investment Logic Map for a potential investment in order to use the approach outlined in this guideline. However, if one does exist it will help significantly.

An Investment Logic Map (ILM) is part of the Victorian Government's Investment Management standard. This standard has been evolving since 2003 and defines a set of common sense practices that have aimed to eliminate unnecessary process in shaping investments. As an alternative to a process-driven approach, it centres on holding a series of 2-hour, structured and facilitated 'intelligent discussions' with those senior people who understand the need and can best shape an investment to respond to the need. The outcome of this discussion is an agreed 'investment story' in the form of an Investment Logic Map.

The Investment Logic Map is a single page visual response to the above questions. It uses plain English and should be able to be read and understood by anyone. It is effectively a summary of the business case. It allows anyone wanting to understand or to make judgements about the validity of an investment to do so with a clarity that was not previously available.

Since 2005 several thousand Investment Logic Maps have been developed across Australia and New Zealand. An example of an Investment Logic Map is at Appendix B.

2 Using this Guideline

2.1 Who can benefit

Depending upon your role and interest in an investment, different aspects of the investment story will have most relevance to you. An example of people who have an interest in understanding the logic underpinning an investment and their particular foci follows:

Investment decision-maker	Someone who will be deciding whether a proposed investment should be funded	<p>Is there a need to do anything?</p> <p>What benefits will be delivered?</p> <p>Is the solution both strategic and innovative?</p> <p>What will be the cost of the investment to the organisation?</p> <p>Does the existing scope miss any opportunities?</p>
Stakeholder	A person who will be significantly affected by a potential investment	<p>Is the problem really understood?</p> <p>What changes will need to be made and how will these affect me?</p> <p>How valuable are the benefits that will be delivered?</p>
Analyst	Someone responsible for confirming that the assumptions underpinning an investment are valid	<p>Is there evidence that the problem really exists?</p> <p>Are the strategic interventions that have been selected the result of a broad and robust analysis?</p> <p>Is it clear what are the claimed benefits and will the solution really deliver them?</p> <p>Is the solution complete and is it consistent with the strategic interventions?</p> <p>Have the costs and risks of the proposed solution been properly understood?</p>
Project Manager	The person responsible for delivering all or part of the solution	<p>Is the solution practical?</p> <p>Have all the changes needed to deliver the solution been identified and properly considered (costs, risks, etc)?</p> <p>Will the solution deliver the KPIs required as evidence that the benefits have been delivered?</p>

Your interest in an investment may align with one of the categories above but it may be different again. In any case, you are considering this investment with your particular interest and having your specific base of knowledge. This knowledge may be the result of access to an ILM, an Investment Concept Brief, a business case, some other documentation or personal knowledge.

2.2 Questionnaire - 'Understanding a potential investment'

The questionnaire at Appendix C ("Understanding a potential investment") comprises 16 questions. These questions have been selected to explore the four main facets of any investment - the Problem, the Strategic Interventions, the Benefits and the Solution. This questionnaire forms the basis of a three-step approach aimed at understanding an investment in the context of whatever your needs may be.

The 16 questions of the questionnaire do not imply they are of equal importance or would require equal effort to establish the basis for a response. As an example, for a major investment the last of the questions, "Can the solution really be delivered?", may require substantial work in validating the reasonableness of the costs, timeframes, governance and stakeholder arrangements, and the risks and how they will be managed. The questionnaire is merely a logical progression of questions that will establish the need, ensure that the benefits expected are well understood, and provide some assurance that the solution is the best reaction to the problem and is likely to be successfully implemented.

2.3 Three steps

Step 1: Indicate your understanding of the investment

Using your knowledge base, work through the questions answering each one by circling the "Yes", "Maybe", "No" or "?" (you are unable to answer). This should take no longer than 15 minutes.

Step 2: Do you understand the investment sufficiently to make a judgement?

Your completed questionnaire will probably be a mix of all four possible responses. Analyse your responses to obtain a sense of how closely what you NEED to know compares to what you DO know of the investment.

Step 3: What is your judgement?

Based on your role and purpose for analysing this investment, make a judgement or draw a conclusion. Examples of conclusions an analyst might make are at the second page of Appendix C.

Note: Appendix C can be used within an organisation to provide a standardised way of understanding and comparing the merits of individual investments. If it is being used for this purpose, the two pages comprising Appendix C should be printed back-to-back as the second page provides guidance in completing the questionnaire and some possible assessment conclusions. Details of the 3 steps (above) have been duplicated on the back of the form so it can be used without needing to reference this guideline.

2.4 Understanding the term ‘Strategic intervention’

The Investment Management standard recognises the importance of selecting the most suitable Strategic Interventions when responding to a defined problem. This is a term that has not previously been well used or understood in relation to shaping the investments of business or government. Appendix D aims to provide some clarification.

2.5 Prioritising competing investments

While this guideline will assist in understanding individual investments it provides no guidance as to the relative merit of one individual investment against another. The guideline of the Investment Management standard titled “Service Logic and Investment Prioritisation” defines an approach that will allow the individual merits of a number of investments to be compared based on the overall priorities of the organisation.

3 Appendix A: Glossary

Asset

Any physical asset that must be built or purchased to enable the identified changes to occur. These may be a hospital, a pipeline or an IT system.

Benefits

The value that the investment will provide to the organisation or its customers. Benefits are normally a positive consequence of responding to the identified Problem. Each claimed Benefit must be supported by Key Performance Indicators that demonstrate the investment's specific contribution to the identified Benefit.

Change

The things that must be done by the business if the Benefits are to be delivered. The changes provide detail of how the strategic intervention defined will actually happen.

Strategic Intervention

The high-level strategic action that is proposed as the response to the identified Problem. It should clearly state the strategic direction without locking in any solution.

Investment Logic Map

A simple single-page depiction of the 'investment story'. It provides the foundation for an investment and is modified to reflect any changes to the logic of an investment throughout its lifecycle.

Investment Management Standard

A best practice approach applied over the life of an investment that aims to reduce the risk of investment failure, provide greater value-for-money and drive better outcomes. It has been designed to enable the *investor* to shape and control investments throughout their lifecycle.

Key Performance Indicator (KPI)

The measure that has been selected as evidence that an expected Benefit has been delivered. The KPI must be directly attributable to the investment.

Problem

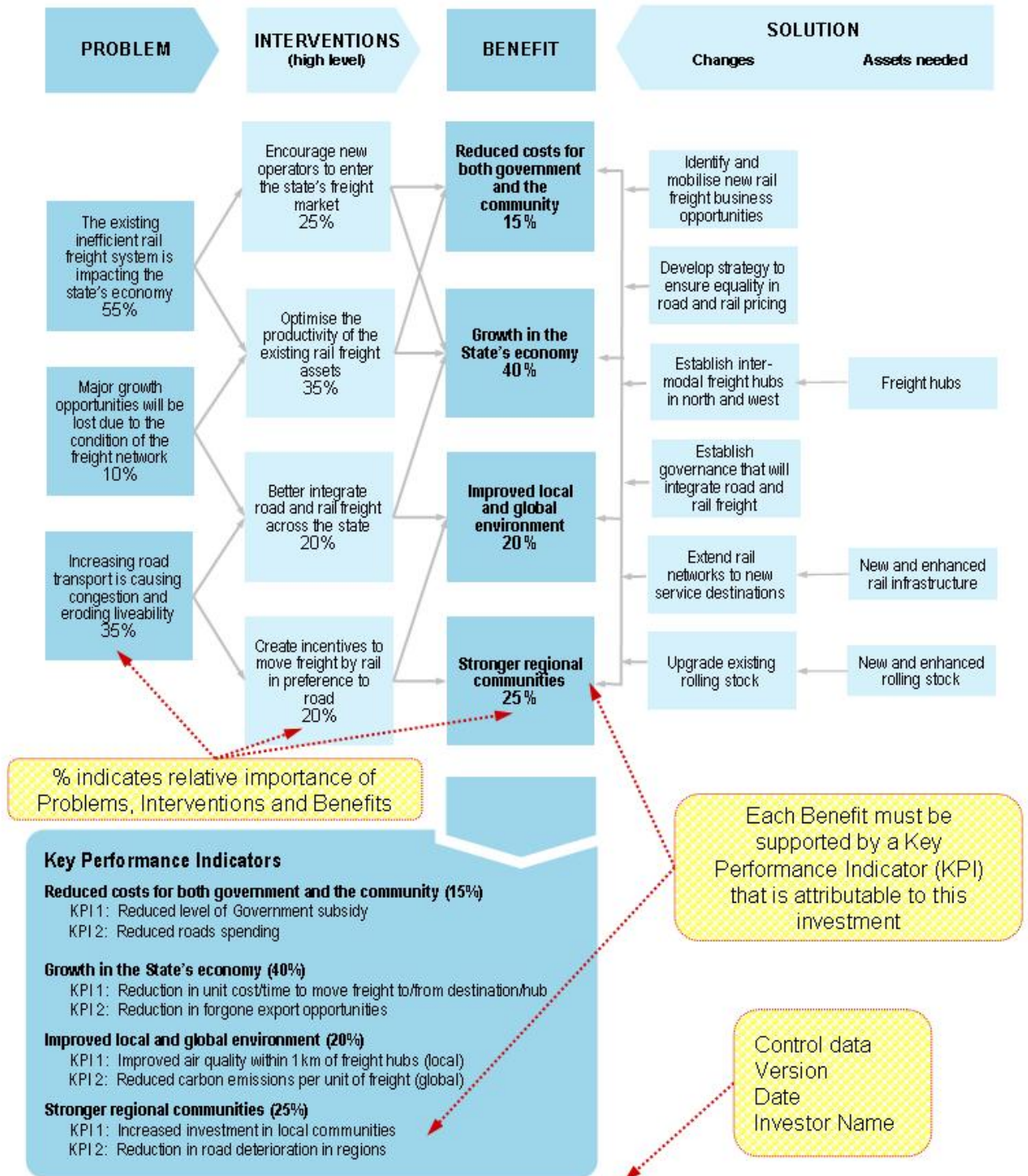
The reason that action needs to be considered at this time. Problems are normally couched in negative terms but can also be an opportunity that will be lost. The statement of a problem should capture the essence of what is broken (the cause) and the consequence (the effect).

4 Appendix B: Example of an Investment Logic Map

Name of Investment

Rail Freight - Policy and Strategy (Fictional)

Department of Transport Investment Logic Map



5 Appendix C: Questionnaire - Understanding a potential investment

Investment Name	
Organisation Name	
ILM version (if one exists)	

PROBLEM	STRATEGIC INTERVENTIONS	BENEFITS	SOLUTION
Is it clear what is the Problem/s that needs to be addressed (both the <i>cause</i> and the <i>effect</i>)?	Is it clear what strategic Interventions are proposed in response to the Problem?	Have the Benefits that would result from fixing the Problem been defined?	Has the options analysis genuinely explored a range of alternative solutions consistent with the Strategic Intentions?
Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?
Is there <i>evidence</i> to support the cause and effect of each problem?	Have these Interventions explored both <i>demand and supply side</i> responses?	Are these Benefits of high value to the organisation?	Is the proposed Solution the best way to respond to the Problem and deliver the Benefits?
Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?
Is the Problem/s something that needs to be addressed <i>at this time</i> ?	Is each action truly strategic <i>without committing too early to a particular Solution</i> ?	Would the KPIs provide reasonable evidence that the benefits were delivered?	Have all the business changes needed to deliver the Benefits been identified and are the identified Assets really needed?
Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?
Is this a problem that is being experienced by other organisations?	Are the selected interventions the best response to the problem?	Are the KPIs both <i>measurable</i> and totally <i>attributable</i> to this investment?	Can the Solution really be delivered? (cost, risk, timeframes, assumptions)
Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?	Yes Maybe No ?

Conclusion / recommendations:

Person assessing /Name:

/Position:

/Date

How to use this checklist

Step 1: Indicate your understanding of the investment

Using the knowledge you have of the investment, work through the questions answering each by circling the “Yes”, “Maybe”, “No’ or ‘?’ (you are unable to answer). This should take no longer than 15 minutes.

Step 2: Do you understand the investment sufficiently to make a judgement?

Your completed questionnaire will probably be a mix of all four possible responses. Analyse your responses to obtain a sense of how closely what you NEED to know compares to what you DO know of the investment.

Step 3: What is your judgement?

Based on your role and purpose for analysing this investment, make a judgement or draw a conclusion. The box below provides examples of the conclusions an analyst might draw.

Some examples of assessment conclusions

- ➔ The logic for this investment is clear and is supported by evidence. Funding should be considered.

- ➔ Whereas the need for this potential investment has been established, it is not necessary to take action at this time.

- ➔ The investment should not be considered further until:
 - ▶ the Problem is properly articulated and supported by evidence
 - ▶ more strategic / innovative Interventions are explored
 - ▶ the Benefits (and KPIs) have been better defined
 - ▶ the Solution better reflects the Interventions
 - ▶ the Solution can be shown as able to deliver the Benefits (KPIs).

- ➔ The need for this investment has not been demonstrated. It should not be considered further.

6 Appendix D: What is a ‘Strategic Intervention’

The practices of the Investment Management standard aim to improve the impact of Government investments by providing a focus on those things that really matter when shaping investments and making investment decisions.

One of these things is what has been termed ‘Strategic Interventions’. A Strategic Intervention is defined as:

“The high-level strategic action that is proposed as the response to the identified Problem. It should clearly state the strategic direction without locking in any solution.”

When properly applied, Strategic Interventions are pivotal in driving solutions that are effective, efficient and innovative. They are chosen following an exploration of the possible supply-side and demand-side responses to the identified cause of the Problem.

The following example places Strategic Interventions in context to the Problem and what are termed ‘project options’.

