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The Funnel That Isn't

Portfolio management promises selection. In most organizations the budget is spent before selection begins.

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EXECUTIVE SUMMARY

Project portfolio management is sold as a funnel. Many ideas enter, weak ones are filtered, the strongest get funded. The premise is that money follows the choice. In most organizations it runs the other way. The budget is set top down, by department and by calendar, before the projects it will fund have been defined or compared. Selection then hands out a number that was already fixed.

This paper argues that the funnel is mostly theatre and that the cause is structural rather than weak discipline. Corporate finance says the budget constraint should reflect the set of available projects and that set is knowable only once the projects exist (Brealey, Myers and Allen). Practice does the opposite. McKinsey's study of capital allocation found that the amount each unit receives correlates **0.92** from one year to the next and the median firm shifts about **one percent** of capital between units annually (Hall, Lovallo and Musters, 2012). Freeze the envelope before the contest of ideas and there is nothing left for a funnel to select.

The popular frameworks do not reach this layer. Stage-gate templates and the scaling frameworks govern execution, not the funding model. The approaches that do reach it are old and proven. Firms that fund value streams continuously and move money as evidence arrives have outperformed the firms that ration once a year and defend the result.

0.92	~1%	1 in 6	46/47
Stickiness	**Reallocated**	**Overruns**	**Years ahead**
Year-to-year capital (McKinsey)	Median firm, per year (McKinsey)	Run 200%+ over budget (Flyvbjerg)	No annual budget (Handelsbanken)

The pages that follow trace the money through one budget year. They show where the envelope is set, what pre-commitment destroys, why the popular frameworks cannot reach it and what a portfolio that actually moves money looks like. Every number is sourced. The conclusion is uncomfortable. Most portfolio governance is a ritual built around a decision that was already made.

01 What the funnel promises

The funnel intuition has a clear lineage. Robert Cooper formalized the idea-to-launch funnel as the Stage-Gate system in 1990, then refined it through the 1990s. Ideas pass through gates. At each gate weak candidates are killed and survivors earn the next tranche of resource. The portfolio sits on top of the gates and decides which streams deserve funding at all (Cooper, Edgett and Kleinschmidt, 1999).

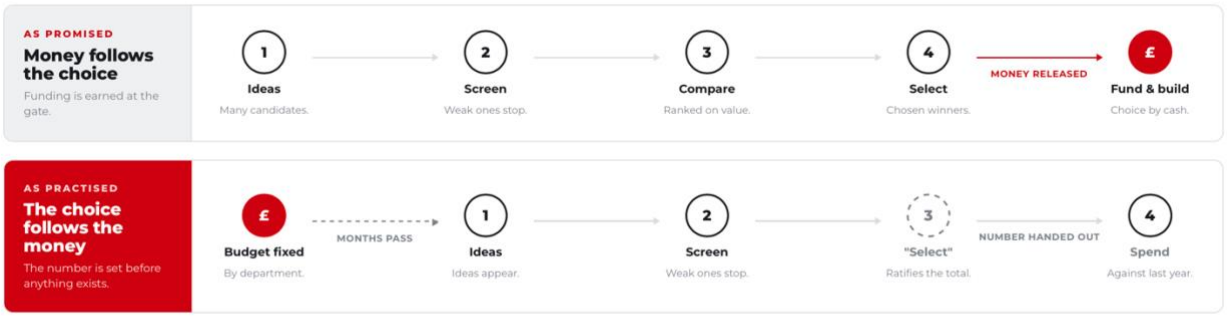
> THE CANON ALREADY CONCEDES THE POINT
>
> *Cooper's own survey of 205 firms found that the most common selection method, financial ranking, produced the worst-performing portfolios. The better performers leaned on strategic and scoring methods instead. The funnel underperforms even where it is run by the book.*

The official standards inherit this picture and read closely, they all assume that funding is a portfolio-level variable allocated against the chosen components. PMI's Standard for Portfolio Management frames the work as continuous alignment of components to strategy and to available funds. The UK Management of Portfolios guidance splits the

job into a definition cycle and a delivery cycle. ISACA's Val IT wraps the same logic around IT investment. None of them tells you to fix departmental budgets before the candidate set exists. They assume budget follows selection.

FIGURE 1 **Money follows the choice or the choice follows the money**

The funnel promises that funding is the prize for winning selection. In practice the envelope is fixed first, so selection only hands out a number that was already set. Watch the red money-marker move from the end of the track to the start.



The real selection happened in spring, in a room with no projects in it. The autumn gate is a reconciliation, not a decision.

02 Where the money actually comes from

Walk into a real planning cycle and the sequence is reversed. The board hands down the budget envelope between March and June, as a number, before the projects it will fund have been described. Assessment starts only afterwards, because building the actual project plans takes time.

FIGURE 2 **The annual governance cycle**

The board fixes the envelope in spring. The projects it funds aren't written until autumn. The red stretch is money already committed running months before any candidate exists to compare.

Read the order: the number is set at the top, the projects appear bottom-right. The December sign-off ratifies a total decided ~5 months earlier.

Those plans develop through the summer and are reported back to the board around October for sign-off and the

year is closed out by December. Read that order again. The money is fixed in spring. The projects are not defined until the autumn. By the time anyone scores a project, the envelope it competes for was set months earlier.

This is the heart of the problem and it is a sequencing problem rather than a discipline problem. Nobody in the cycle is lazy. The board needs a number early to plan the year. The teams need the summer to write credible plans. The trouble is the order. A budget set in spring cannot reflect projects that do not exist until autumn, so the October sign-off ratifies a total that was decided before the work was understood.

The evidence for this stickiness is quantitative and hard to argue with. McKinsey examined how firms allocate capital across business units and found a year-to-year correlation near 0.92, meaning this year's allocation is mostly last year's allocation. A third of companies moved only about one percent of capital between units from one year to the next (Hall, Lovallo and Musters, 2012). Graham and Harvey's survey of 392 chief financial officers had already shown the mechanics behind this, including the widespread use of a single firm-wide hurdle rate rather than project-level risk (Graham and Harvey, 2001).

Joseph Bower explained the deeper reason half a century ago. Resource commitments are shaped from the middle of the organization and structured long before senior management formally decides anything (Bower, 1970). Cohen, March and Olsen described the same disorder from another angle. In their garbage-can model, solutions and budgets circulate looking for problems to attach to, which is the opposite of an orderly funnel (Cohen, March and Olsen, 1972).

The funnel does not even govern all the work. Blichfeldt and Eskerod studied 30 firms and found that large parts of the real project load never enter the formally managed portfolio at all (Blichfeldt and Eskerod, 2008).

The order also trains behavior. A unit that underspends its envelope watches the surplus get clawed back and next year's number cut, so the rational move is to spend the whole allocation whether the projects deserve it. The incentive is to defend the base, never to surrender it to a stronger idea in another team. The cycle does not merely fail to reallocate. It quietly punishes the people who try.

> **THE OCTOBER SIGN-OFF IS A RECONCILIATION**
>
> *It looks like a decision. The board approves a stack of project plans against a total that was fixed in spring. The gap between the plans and the number is closed by negotiation rather than by evidence and the projects that win are the ones whose sponsors argued hardest. The real selection happened months earlier, in a room with no projects in it.*

03 What pre-commitment destroys

Spending the money up front is not a neutral act of planning. It throws away something valuable. Dixit and Pindyck showed that the opportunity to invest behaves like a financial option and that the ability to wait, learn, then commit carries real worth that a discounted cash-flow number ignores (Dixit and Pindyck, 1994). A lump budget committed in advance spends that option premium. Rita McGrath and Ian MacMillan made the managerial version of the case with discovery-driven planning, which funds the next stage only as its assumptions survive contact with reality (McGrath and MacMillan, 1995).

There is also a simpler point from finance. When capital really is scarce in a period, the textbook rule is to rank projects by value per unit of capital and fund down the list (Brealey, Myers and Allen). That ranking cannot exist until the projects do. Setting the constraint first, by department, guarantees that the money is committed against last year's shape of the business rather than this year's best ideas.

Behavior then locks the arrangement in place. Barry Staw's experiments on escalation of commitment showed that people who feel responsible for a course of action put in more after bad news, not less (Staw, 1976). Richard Thaler's work on mental accounting explains why money assigned to a departmental pot is treated as non-fungible and

defended (Thaler, 1985). The optimism in the original estimate is the planning fallacy, which Lovallo and Kahneman traced into executive investment decisions (Lovallo and Kahneman, 2003).

The visible symptom is the project that will not die. Isabelle Royer documented RCA's SelectaVision, which absorbed about 580 million dollars over fourteen years on the strength of a champion's conviction (Royer, 2003). Anthony and colleagues at Innosight found that roughly one in five initiatives inside one IT company were zombies, consuming resource with no real prospect of mattering (Anthony, Duncan and Siren, 2015).

04 Why the frameworks miss it

The popular fixes operate downstream of the problem. Stage-gate templates, generic PMO playbooks and the scaling frameworks all assume the money question is settled and treat their job as execution hygiene. Process discipline cannot reach a decision that was made before the process started.

The Scaled Agile Framework attracts the sharpest criticism and the honest reading is that the critiques are expert opinion rather than controlled evidence. Ken Schwaber, co-creator of Scrum, called it a repackaging of an older method and told organizations to measure the return on what they were about to spend (Schwaber, 2013). Dave Thomas, one of the Agile Manifesto's signatories, argued that the word agile had been hollowed out into a market for consultants and tools (Thomas, 2014). Take them as informed skepticism.

There is a simpler tell. Every one of these frameworks can be adopted in full while the budget calendar stays exactly as it was. A company can run quarterly increments, daily stand-ups and a wall of cards and still hand down the same fixed envelope every spring. The ceremony changes and the funding model does not. When a method can be installed without touching the one decision that determines what gets money, it is working on the wrong layer.

05 What real portfolio management does

The alternative is documented and not new. Svenska Handelsbanken has run without a traditional annual budget since 1970. It replaced the central plan with decentralized authority and resource requests made as they are needed and it has beaten its peer group on return on equity in 46 of 47 years (Bukovinsky and Talbott, 2019). This is the anchor case for Beyond Budgeting, the argument that Jeremy Hope and Robin Fraser set out for breaking the annual performance trap (Hope and Fraser, 2003).

FIGURE 3 **What a portfolio that actually moves money does**

The alternative is old and proven: fund value streams, not fixed projects, and move the money as evidence arrives. Three mechanics carry the whole idea.

~30% higher total shareholder returns over fifteen years for the firms that reallocated capital most aggressively (Hall, Lovallo & Musters, McKinsey, 2012).

In software the same logic appears as Mik Kersten's shift from funding projects to funding products. Money backs a long-lived value stream against business results and arrives incrementally as outcomes appear, rather than approving a fixed scope once and then starving it (Kersten, 2018). The financial case for moving money is the strongest part of the record. The McKinsey study found that the third of firms that reallocated capital most aggressively delivered around **30 percent** higher total shareholder returns over fifteen years than the firms that left the allocation alone (Hall, Lovallo and Musters, 2012). Good portfolio management funds bets, watches the evidence and moves the money. The annual envelope is built to do none of those things.

THE TEST OF A REAL PORTFOLIO

A portfolio without a credible mechanism for stopping work is not a portfolio. It is a queue. Ask one question of any governance body. When did it last move funded money away from a live project, mid-year, toward a better one? If the answer is never, the funnel is decoration.

06 Evidence from the wreckage

The public record shows what pre-committed money does at scale. Each of the following programs locked a large sum against a fixed multi-year scope, then kept feeding the commitment rather than reallocating away from it.

PROGRAM	SPAN	COST TRAJECTORY	OUTCOME
NHS National Programme for IT	2002-2011	Early estimate near £2.3bn, toward £9.8bn spent	Dismantled in 2011
Emergency Services Network	2015 onward	£6.2bn rising to £9.3bn by 2019	Years late
C-NOMIS offender management	2004-2007	£234m approved, est. £690m	Rescoped

Latest or final cost as a multiple of the initial estimate (Public Accounts Committee 2013; National Audit Office 2021, 2009). The NHS starting figure is an early estimate, so treat its multiple as indicative.

The Public Accounts Committee called the NHS program one of the worst and most expensive contracting failures in the history of the public sector, with measured benefits of about £3.7bn against the spend (Public Accounts Committee, 2013). The National Audit Office documented the Emergency Services Network and C-NOMIS overruns in the same pattern (National Audit Office, 2021; 2009). These were not only execution failures. In each case the governing body could not, or would not, move the money once it was committed.

A word on the headline failure statistics. The widely quoted low success rates from the Standish CHAOS reports should be handled with care, because Eveleens and Verhoef showed the underlying definitions are one-sided (Eveleens and Verhoef, 2010). The more defensible number comes from Flyvbjerg and Budzier, who studied 1,471 IT projects and found an average cost overrun of 27 percent alongside a fat tail, where one project in six ran more than 200 percent over budget (Flyvbjerg and Budzier, 2011). The fix they propose, reference-class forecasting, prices the bet honestly before the money is committed (Flyvbjerg, 2006). It is the opposite of the annual envelope.

07 Appendix

A. Where the thesis is firm and where it is inference

The strongest claims rest on peer-reviewed work and primary documents. The capital-allocation stickiness, the option-value argument, the decision-science roots and the public-sector failures are all on solid ground. One claim is a synthesis rather than a single measured statistic. No one study cleanly quantifies budgets are fixed before projects are selected as a rate. The pattern is well supported by Bower, the garbage-can model and the McKinsey finding that allocations barely move, but it is stated as a theoretically grounded and case-supported pattern, not a measured law.

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