STRATEGY & INNOVATION
Breakthrough Insight and Ideas for Driving Growth
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One Hundred Days To Disruption

How businesses in any industry can move quickly from disruptive idea to disruptive plan

BY SCOTT D. ANTHONY & BRAD GAMBILL

The concepts of disruptive innovation are powerful tools with which to spot high-potential opportunities. Whenever we run an idea generation session, we are struck by how intuitive and powerful people find the core disruptive concepts. They allow managers in even the most moribund of industries to quickly envision entirely new, fertile fields of growth.

However, we've noticed a disturbing pattern. If we check back with a company 60 days after a one-time ideation workshop, we frequently find that nothing has happened. Why? Managers returned to their desks, stepped back into the daily grind, and the optimistic feelings generated in the session slowly disappeared or were consumed by near-term priorities.

The gap between the germ of a disruptive idea and successful commercialization can be wide. Sometimes, managers can feel like they have not developed detailed enough plans to move forward. After a successful ideation session they might say, "How do we know we generated the right idea?" or "There's no way we could, in a day, really develop a robust-enough plan to actually spend money on."

And sometimes, managers will go to the other extreme. They will develop an extremely detailed business plan that requires massive investment of dollars and human resources. These plans typically never see the

see '100 Days' on page 13

Gives, Gets, and the Good Enough

A methodical, consumer-driven approach to cutting features, benefits—and costs

BY JOSEPH V. SINFIELD

Innovation is often top of mind for organizational leaders who are striving to spur the growth of their enterprise. The circumstances that spark this focus typically include a lofty growth target, a high level of shareholder expectations, and recognition that the current product pipeline is not big enough to close the gap between existing forecasts and the goal.

But there is another characteristic shared among organizations that concentrate on innovation—these businesses are typically financially healthy. As obvious as

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INSIDE

Voices of Disruption

KAREN MORRIS

Each issue, we feature a person who is "in the trenches" of disruption. This issue we feature Karen Morris, chief innovation officer at AIU (American International Group's property and casualty businesses worldwide). Prior to joining AIG in 2004, Morris spent over 25 years in legal and commercial roles in the international insurance industry and in the fast-moving consumer goods industry. She began her career as an English barrister.

Many large, successful global organizations, to generalize shamelessly, got to where they are today by being very good at what they did yesterday. It is rational to want to sustain and replicate yesterday's success today.

Disappointingly perhaps for alarmists with a dramatic flair, "change or die" just does not resonate well in an environment of prolonged growth and sustained industry leadership. Focusing on the core can actually work quite well for quite a long time. Success breeds success until the gap between what you do and what you *want* to do becomes a chasm.

Fortunately, our senior management's vision was different: We felt that 21st-century success would require a different organizational dynamic than the cost- and quality-control paradigm that we had mastered so well. Enter the AIU Innovation Practice, stage right. Our mission was to stimulate the firm's thinking, strategies, and tactics, so that the gap between yesterday's, today's, and tomorrow's success never became a chasm.

Insurers live and breathe change. The unexpected is what we expect. If it can impact our insureds or their businesses, it is our business. I believe insurance is the most exciting business (but then I don't have much of a social life).

Unless you have a lot of time on your hands, it is not a good idea to Google "innovation." The literature is vast. So many important theories and insights have been developed that it would be futile for me to mimic or précis.

Rather, I want to share some minor insights drawn from my experience of creating an Innovation Practice in a large, decentralized, and extremely successful organization. Fortunately, AIG already had a proven track record of product and service development and transactional innovation. So there was no need to "fix what's broke."

I call these insights my "T-shirt Tips" because if it cannot fit on a T-shirt I cannot remember it.

'Mirror Mirror on the Wall'

We started by evoking Disney's extraordinary innovation—*Snow White and the Seven Dwarfs*, the first full-length animated feature film—in which the Queen consulted her magic mirror every day. Constant, candid evaluation of strengths and weaknesses is critical in ensuring that the organization anticipates where change needs to be made and adopts a stance of change readiness. Although the

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unlocking new market growth

Innosight is a boutique consulting and training firm that helps companies improve their ability to create innovation-driven growth. Its unique methodologies and proprietary tools facilitate the discovery of new, high-growth markets and the rapid creation of breakthrough products and services. Its approach builds on the research of its founder, Harvard Business School Professor Clayton Christensen, author of *The Innovator's Dilemma*, *The Innovator's Solution*, and *Seeing What's Next*. For more information, visit our website at www.innosight.com, call us toll free at 1-877-934-7787, or email us at inquiries@innosight.com

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pace of change in our fast, sometimes flat, global economy has changed dramatically, the developments that overturn companies are rarely if ever a "surprise." It is not that the race has not been announced—it is that some are not even on the starting block when the starting pistol is fired.

We instituted an extensive self-appraisal to evaluate to what extent our "eco-system" was supportive of innovation and change. This diagnostic tool furnished valuable data that we were able to use in devising communication plans and training programs. And it pushed us to deeper inquiry into the authenticity of our customer focus and our value proposition, outward-facing and as perceived by our value chain. This honest holding up of a mirror to ourselves allowed us to plot our journey against a baseline.

'My Space or Yours'

An important learning from our analysis of current practices, priorities, and goal setting was that the "day-to-day" can be all-absorbing for many employees and managers. Since the transformation to innovation embraced everyone's contribution, we realized we needed to find ways to increase (and sometimes create) "space"—temporal, physical, and mental—so that we could look differently at problems and opportunities.

The solutions we adopted, and continue to experiment with, were not new—including off-sites, workshops, storyboarding, adoption of techniques from completely different industries. What made a positive difference was the dedication of time and place, and the explicit liberalization of the "how might we look at this differently" approach.

This glancing reference is illustrative only. Leading some people to think and act outside of their comfort zone can be tough. Some might question the credibility of the imperative to think outside of the box. It is senior management's responsibility to ensure that "outside the box" is a safe place.

'Men in Clogs Kissing Frogs'

Any innovation initiative is going to meet resistance. The word *saboteur* derives from the clogs (sabos) worn by pre-Industrial Dutch workers who attacked and destroyed new technologies that would displace them. There will always be well-intentioned (or not) derailers, especially the disingenuous devil's advocates.

Process can help. If the search for innovative solutions and for the creation of new value is an arbitrary, occasional exploration, or if it involves loitering at the suggestions box, any successes may not be systematically repeatable.

We found that objective, transparent metrics appropriate for evaluating ideas and solutions in context create a genuine competitive marketplace for ideas and facilitate positive and rigorous evaluation, as well as cross-fertilization, dissection, and transfer of ideas.

'Prophet or Profit'

Innovation is intellectually interesting, whether it has commercial application or not. Innovation enthusiasts and those of us whose job it is to consider how new value is created can easily become both evangelical and aspirational.

It is critical to ensure there are sustainable wins with commercial deliverables, sooner rather than later. P&L's are not and should not be patient, and "prophets" can find themselves in the wilderness with a plate being prepared for their heads. This is true even if the prophet is right. Our learning was to ensure that the portfolio includes both short-term and long term deliverables with financial impact.

'Love, Actually'

Anecdotes and case studies often describe passionate and creative innovators/leaders whose compelling vision transforms products, services, brands, customer experiences, and so forth. We've observed that most people get passionate about change they can contribute to and shape. Common corporate practices ought to be put to "the love test": Does this process/system/incentive structure inspire people to love the challenge and the opportunity to engage fully, or is it a passion killer?

Creating a learning organization that constantly questions and that has an open, outward-in orientation requires leadership, strategy, management, motivation, process, metrics, and a number of other puzzle pieces, all in place.

My view is that there is a further indispensable element: trust. When senior executives build an environment where the natural and predictable "fear, uncertainty, and doubt" of change are met with insight, support, and compassion for the challenge that innovation entails, then the power and passion of the people will truly be engaged in creating new value. ◆

Reprint # 050603

Innovators' Update: Reinventing Titans, Round Two

Has Cisco or Wal-Mart taken the lead in the reinvention race?

Each issue, we'll take a look back at a past Innovators' Insight to see how our analysis has held up. In this issue, we look at Insight #71, "The Battle of the Reinventing Titans." We suggested that Cisco Systems had a better chance of reinventing itself than Wal-Mart. What has happened since?

Call it the crisis of success. Highly successful companies get that way through extended periods of double-digit growth, and then markets and analysts come to expect that growth. When companies hit a certain size, though, the "law of large numbers" makes it difficult to continue to create growth at that pace.

Cisco and Wal-Mart are both faced with this crisis of success. Both leading lights of the1990s economy, Cisco dipped as the Internet bubble burst in 2000, and Wal-Mart's fortunes have sagged over the past 24 months as growth leveled off.

Last year, both companies announced bold reinvention initiatives. Cisco announced plans to step up its efforts in the consumer electronics space; Wal-Mart disclosed plans to customize stores to account for local tastes.

Our take was that Cisco had a greater chance of success, because it is far easier to drive reinvention by creating new businesses than it is to actually change your core offering.

In a recent survey, Innosight asked 300 executives, "What organization do you think has done the best job in recent years of transforming itself?" Four of the most frequently mentioned companies were Apple, IBM, Procter & Gamble, and General Electric.

Why do people mention these companies? Is it because Apple completely changed its computing operations, IBM transformed its mainframe business, P&G started selling Tide and Crest in different ways, and General Electric re-invented the light bulb?

No. In all cases, new product lines, business units, or acquisitions drove the transformation. Apple's most obvious success comes from the iPod line. P&G has introduced new brands like Swiffer and stepped up investment in health and beauty products. IBM has moved aggressively into services. General Electric has bought and sold dozens of businesses over the past few years.

Cisco must be doing something right: Its stock has surged more than 20 percent since we wrote that Insight.

Cisco's cause has been helped by the exploding consumption of video delivered over the Internet, which has increased demand for Cisco's core routers and switches.

Cisco also has garnered significant buzz for its TelePresence video conferencing system, a $300,000 system that *Fortune* says "is to traditional video-conferencing what the latest big-screen surround-sound plasma extravaganza would be to Grandma's black-and-white set with rabbit ears." Cisco hopes to bring a $1,000 version of TelePresence to consumers in two or three years.

However, Cisco can't claim success just yet. The TelePresence business is tiny, and Cisco hasn't yet proven that its recent high-ticket acquisitions of cable set-top box provider Scientific Atlanta and Internet conferencing pioneer WebEx will pay off. But it has created the building blocks to successfully transform its business by driving growth in new markets.

On the other hand, Wal-Mart appears to be treading water. Its stock price is essentially flat since we wrote our Insight. Same-store sales growth is sagging. Wal-Mart did report higher than expected earnings in the third quarter of this year—accomplished not by reinvention but by a focus on its core budget-conscious consumers.

While executing a solid strategy is of course a good thing, Wal-Mart is simply too big to execute its way to sustainable growth. The company has grown by expanding into new categories such as grocery and moving to higher-margin products such as clothing, but now appears stuck.

Wal-Mart has planted seeds that—properly maintained—could drive transformation. Former Intel CEO Andy Grove praised Wal-Mart's investment in in-store medical clinics, saying it could "effect profound change by offering direct-to-consumer services and driving down prices for commodity services." Wal-Mart has similar experiments under way in the financial services industry.

Wal-Mart has work to do to catch Cisco in the reinvention race. If it manages its emerging offerings correctly, it could leap past Cisco. If it ends up retrenching and focusing on driving transformation from within, its odds of long-term success are slim.

— Scott D. Anthony

Reprint # 050604A

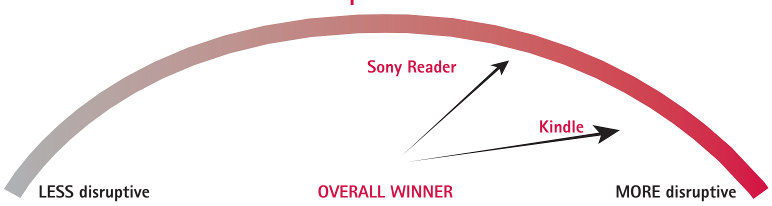
Disrupt-O-Meter

Tale of the Disruptive Tape: Amazon Kindle vs. Sony Reader

"Is company X disruptive?" Whenever we're asked this question—and we're asked it often—we run through a simple mental checklist that looks at the target customer, the solution, the business model, and the competitive landscape. In this issue, we use our "Disrupt-O-Meter" to analyze Amazon's new e-book offering, Kindle.

In November, Amazon launched Kindle into an e-book reader market that already had a front-runner, the Sony Reader Digital Book. Both devices use the same E Ink technology, but their business models differ radically. Kindle offers the ability to buy not only books but also subscribe to digital versions of magazines, newspapers, and blogs that are delivered wirelessly at high speed. Sony Reader users must buy e-books via their computers. How likely is Kindle to disrupt the digital book market?

Disrupt-O-Meter



Sony Reader		Kindle	
Those who like familiarity of downloading e-books onto laptops and then to Reader	CUSTOMER	Current Amazon customers who do not want to download e-books on laptops	WINNER
$299 device got good reviews; content purchased from web, uploaded via PC	SOLUTION	$400 device got mixed reviews; users buy and subscribe to content via wireless	TIE
Makes money from device sales, digital content sales deals	BUSINESS MODEL	Makes money from device sales, digital content distribution, and subscription fees	WINNER
Lack of obvious differentiation might make it hard to fend off competition	COMPETITIVE LANDSCAPE	Business model might make it susceptible to competition from Apple	TIE

More Disruptive: Kindle. The device itself is nothing new, but the Kindle publishing platform, harnessing Amazon's distribution power, has the potential to disrupt the way digital content is distributed and produced. Always-on high-speed wireless, subsidized by subscription fees, allows ease-of use for customers buying books or subscribing to magazines, newspapers, or blogs. Also, Kindle's easy-to-use publishing platform is open to any content provider who wants to offer something for sale. If the publishing platform takes off, it could be as big as Flickr is for images or YouTube for video. The Sony Reader, meanwhile, is limited to selling content from established publishers. And while the device is considered more elegant than the Kindle, its purchase interface has been widely panned. ◆

Reprint # 050605A

EMERGING TECHNOLOGY WATCH

Talking labels customers control

Hawaii startup **Labels That Talk** has developed software that allows consumers to print high-density bar codes that store recorded voice messages. Codes can be read by a handheld scanner, or the scanner can be incorporated into gadgets such as cell phones. RFID technology could do the same thing, albeit more expensively—HP is currently developing Memory Spot, a self-contained storage device with a radio and processor. The device is stuck onto photos or documents and will serve a video or audio recording to a nearby computer or cell phone. **Labels That Talk** is selling their software to consumers and printer makers, and lining up partners to make scanners. Early target markets include scrapbook enthusiasts and pharmacies and hospitals for prescription labels.

New technologies for hearing loss

Denver-based **Able Planet** has developed Linx Audio, a technology that makes high-frequency speech components clearer, but not louder. Linx Audio works by enhancing the harmonics of high-frequency sounds. The technology is built into a line of headsets, telephones, and assistive-listening devices aimed at those with partial hearing loss, as well as those who want to be able to hear voices over other noise, such as video gamers who want to hear each other over virtual battles. Other hearing loss solutions aimed at the aging baby boomer market include **Sound Pharmaceuticals**' gene therapy treatment, currently under development, for regenerating cochlear hair cells.

Language learning via social network

Bellevue, Wash.-based **Live Mocha** has launched a social networking site that brings together immersive language lessons with native speakers. The site features the same kind of language lessons and interactive tools one might find on an instructional CD-ROM, but users are encouraged to use the site's search function to identify and contact native speakers of their target language. Users can chat via text, voice, or webcam. Being able to practice with native speakers allows users to truly become conversational, as well as to learn colloquialisms and gain an understanding of culture much better than they could otherwise.

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'Gives, Gets' (continued from page 1)

it sounds, this financial fitness is what enables an organization to devote resources to new growth rather than dedicating all hands to reviving the core business.

So what happens when an aggressive competitor decides to gain market share by lowering prices? Under this kind of threat to the core business, the mind of the organizational leader must shift to reassess the company's strategy.

At first, questions are raised about how to boost volume, then how to improve productivity. Before too long, however, those two frightening words are spoken—CUT COSTS—words that send shivers through the ranks from the supervisory staff to the warehouse floor. The last thing any leader *wants* to do is to let employees go. So, considerable effort is often dedicated to improving operational efficiency and removing unnecessary costs.

However, in many situations, these measures are not enough. Ultimately, companies are often faced with the realization that their good or service simply includes benefits that are too costly to provide at a price that the market will tolerate. So teams are assembled to strip away costs.

In a manufacturing setting, this may mean reducing the quality of materials, re-evaluating the design of key systems, or simply stripping away features and functionality. In a services environment this could mean cutting back on the benefits offered, when they are available, or how convenient they are.

Identifying these cost-saving opportunities is difficult, especially if you do not take a process approach,

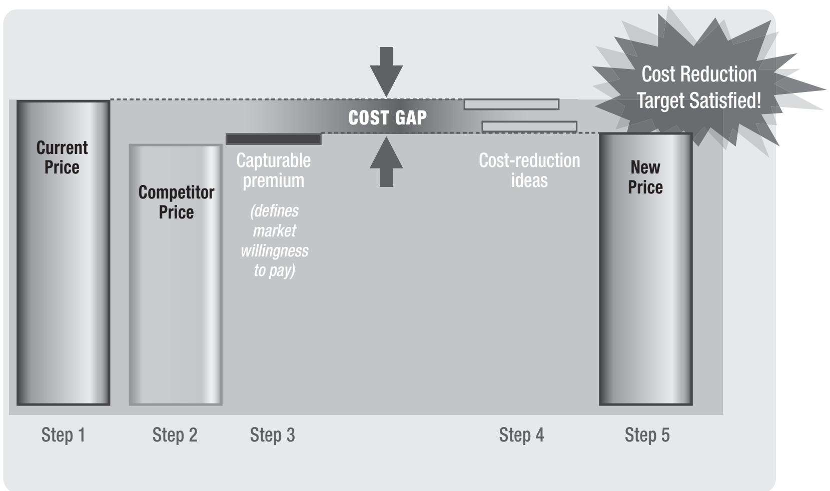

Figure 1: Traditional Cost-Reduction Process

such as we are advocating.

Without a process you risk taking away too much and losing customers, or not taking away enough and losing profits. Neither scenario is appealing. All too often, the tradeoffs customers are willing to make are not well understood. As a result, the very steps an organization may take to improve its bottom line may undermine its reputation and demand in the market.

To address this problem, we can look back to our innovation toolkit. A core concept, the customer's jobs-to-be-done, is critical in understanding which benefits are important and which are not. Remembering that quality is relative and that we must balance what a customer gives up and what a customer gets are routine steps we would typically apply to capture a new-growth opportunity.

When we are forced to re-evaluate what an existing product or service provides to the market, we must not forget these concepts. They can guide our success in removing costly features and benefits without harming demand.

The traditional approach to cost reduction

Companies faced with the need to reduce costs are often caught off-guard. Unfortunately, many organizations really don't know which features (and associated benefits) can be removed without impacting the customer's perception of their offering, especially since the commonly adopted sustaining trajectory of innovation leads to the addition of features year after year.

Efforts to strip costs can be less than well-informed and the results far from effective. Companies will tend to look at the gap between their current price and that of their competitor's offering, adjust for any premium that they feel they can command (which could be why their price might be higher in the first place), and define a cost-reduction target that will allow them to lower their price and retain profitability (**see Figure 1 above**).

The product or service manager and team are then typically

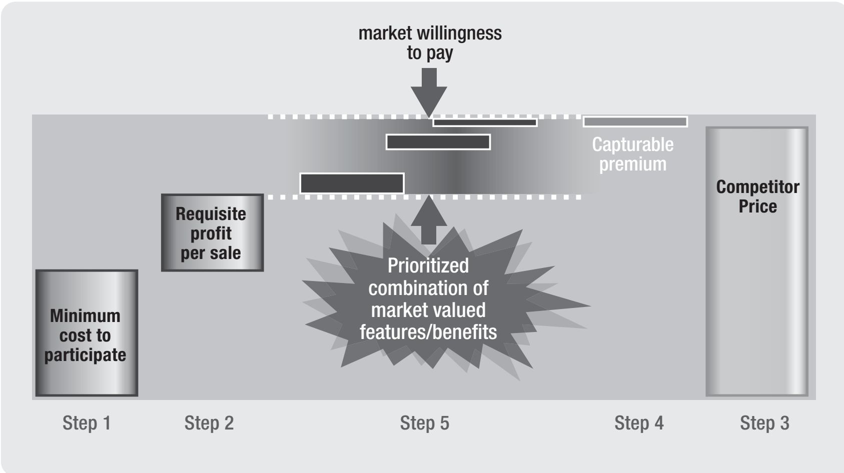

Figure 2: Intelligent Feature Selection Using Innovation Tools

charged with identifying ways to remove the prescribed amount of cost from the offering. The team starts brainstorming, suggesting areas where material quality can be reduced, which features can be removed (ironically often those just introduced last year), or in what ways functionality can be limited.

Then, almost without fail, the ideas are sorted and prioritized, guided by misconceptions of what drives value. After some debate, the low-hanging fruit is selected, picking ideas that miraculously add up to almost exactly the cost-reduction target. When the target is reached, the effort is stopped, congratulatory comments are exchanged, and everyone breathes a sigh of relief.

This approach is quite literally backwards, and simply postpones the inevitable wave of cost reductions that will come when the competitor releases their next product variant. What is needed is a different approach—an approach that leverages the core tools and concepts of successful innovation.

Using innovation tools to intelligently defeature

Rather than trying to reduce the quality or features of the original offering in a piecemeal fashion to achieve a defined cost-reduction target, companies faced with a cost-reduction challenge should undertake this defeaturing effort while still adhering to the core innovation concepts—jobs-to-be-done, gives and gets, good enough, and quality is relative.

The resulting process comprises these five steps:

1. Establish the minimum cost to participate in the category
2. Define the required profit per sale
3. Understand the competitive offering
4. Prioritize features and benefits according to the core innovation concepts
5. Shape an offering that can be delivered to market at an attractive price

To get a better understanding of this methodology, let's examine each step in the process by looking at the case of a global manufacturer of work utility vehicles that was forced to fend off the aggressive pricing moves of a low-cost competitor in one of its core markets.

The incumbent manufacturer offered a utility vehicle to the higher-end consumer at a price point around $25,600, and faced a competitor producing a comparable product (in features that mattered) priced at $21,500.

Step 1: Establish the minimum cost to participate in the category

Any given product or service offering must address the "qualifying jobs" of the customer ("If it can't do x, y, and z, I won't even consider it"). Insight into these qualifying jobs can be gained by examining whatever limited set of benefits is provided by the lowest-priced, successful competitor.

This good-enough version of the product helps to define the "cost to participate," even if only at the lower end of the market. Note that the lowest-priced successful competitor may not in fact be offering the least amount of benefit possible; however, their offering will demonstrate the lowest set of benefits for which demand is validated.

In the case of the work utility vehicle manufacturer example, at a high level a machine wouldn't qualify as a competitive "utility vehicle" unless it had an engine of at least 45 horsepower, a chassis with a 7-year design life, a manual transmission, and the ability to mount or tow a variety of useful accessories.

Delivery of each of these features or benefits has both a variable and a fixed-cost component. The variable cost is usually relatively straightforward and of course can be affected by things like pricing agreements with suppliers. The fixed cost comprises the amount of overhead that must be allocated to each sale. Tallying up these costs provides you with the starting price, or the price below which you would *lose* money. For the utility vehicle maker, let's assume that this was about $16,200 per unit.

Step 2: Define your requisite profit per sale

On top of the minimum price, we must also add the requisite profit per sale to achieve the company's financial goals. While we would all like to make large profits, there are acceptable norms in any industry.

A good starting point would be a number that makes your investors happy and is also likely to be tolerated by the market. The sum of the cost of the minimum offering and the requisite profit per sale establishes the floor on price. The utility vehicle manufacturer wanted to hold to a profit of about $5,000 per unit, so their price floor was $21,200 per unit.

Step 3: Understand the competitive offering(s)

The next step is to understand the price-value position of the lowest-priced, successful competitor. These are all the ways in which the product satisfies the customer's jobs-to-be-done, and may include straightforward functional benefits, as well as social (e.g., brand image, association with status) and emotional benefits (e.g., value proposition that encourages the perception of a "good deal").

Going back to the utility-vehicle example, the prime competitor operating disruptively in the lower end of the market offered 45 horsepower (the lowest in its class), a manual transmission, a simple yet versatile accessory mount, and a chassis with a 5-year design life. This product also offered intangible benefits, such as the perception that its design was so simple users could maintain it themselves, inferring long-term cost savings.

Insight into qualifying jobs can be gained by examining the limited set of benefits that is provided by the lowest-priced, successful competitor.

Beyond these primary attributes, the competitor's vehicle also offered very simple lights for night use, a nondescript body and cowl design, stiff, relatively uncomfortable seats, and was generally comprised of parts made in the simplest and least expensive way possible.

In contrast, the incumbent utility vehicle incorporated a host of technological advances and creature comforts: An electronically controlled 45 horsepower engine to maximize pulling torque, an automatic transmission, dashboard control of the attachment mount, and soft adjustable seats, as well as other design elements such as heavy duty all-weather wiring throughout the vehicle, molded multi-element body panels for a curved design, and extra-stiff welded steps to help an operator climb in and out of the vehicle. All of these features were viewed by the incumbent as key differentiating benefits.

Step 4: Prioritize features and benefits using core innovation concepts

There were significant differences of opinion among the incumbent's engineering personnel, brand manager, and sales team as to which features should stay and which should go. Some felt that they should look for the quickest and easiest ways to remove cost, so that they could get a competitive offering into the market as quickly as possible. One such feature candidate was the vehicle's welded step, which could be replaced easily with a lower-cost component.

Others felt that the company could not compromise on their view of quality and that stripping out cost by removing such features as the all-weather wiring would destroy the company's reputation, as vehicle failures cropped up over time.

Still others attested to the critical competitive merits of other attributes of the vehicle such as the electronic engine controls, all the while simultaneously declaring that the price must come down.

Typically, this kind of debate results in the retention of features that matter more to the company than the users, and removal of features that are easy to take away, yet differentiating in the eyes of the consumers.

Working through this dilemma using the framework provided by the core innovation concepts of jobs-to-be-done, gives and gets, good enough, and quality is relative allows opportunities for cost reduction to be uncovered and for prioritization of those "nice to have" benefits that allow a provider to satisfy differentiating jobs as well as to capture a premium for their offering.

For the utility vehicle maker, a series of quick focus group activities and very targeted surveys revealed that the company's "prized" electronic engine control system, while indeed unique, really only made a difference when the vehicle was pushed to its limits—an event that was rare and, in the eyes of the customer, really not worth extra cost. As it turned out, "provide extra torque under extreme circumstances" was a fairly unimportant job, and a traditional engine without electronic controls was "good enough." So, here was an opportunity to remove cost on an overshot dimension.

Customer feedback also indicated that the automatic transmission was definitely worth paying for. Other input indicated that while it would indeed be easy to change out the operator step on the vehicle, the bulky, strong appearance of the step was frequently perceived to be a sign of quality (even though it was technically no stronger than a bent metal design). Shifting to a lower-cost, bent-steel component would have immediate adverse consequences in the eyes of the buyer. Here an emotional job won out over the functional job in the consumer's mind.

In contrast, much of the wiring system of the vehicle was well out of the elements during routine vehicle operation, and most consumers did not even know that the system made use of robust all-weather wire connections. Clearly, this attribute did not drive any differentiable benefit.

In the end, the goal is to prioritize solutions to the most important and unsatisfied jobs that can be offered at price points the buyer is willing to pay.

Exploring customer-derived insights feature-by-feature forced respondents to make clear their tradeoffs and provided deep insights. Questions to ask here would be: What are the "must-have" benefits and quality standards? Which are tangential to the job the customer is trying to get done?

Step 5: Shape an offering that can be delivered to market at an attractive price

Viewed through the lens of the customer's jobs-to-be-done, perception of quality, and willingness to make tradeoffs, customer preferences can be used to create a prioritized list of features or benefits whose inclusion will bring the base offering up to a well-balanced, differentiated solution to an important, unsatisfied job-to-be-done.

Each benefit should be examined individually to determine exactly how much it will cost to deliver and how much profit can be commanded. Once the fully loaded cost of providing each benefit is defined, additional market insight should be gained to determine the customer's willingness to pay the cost plus markup required to deliver each feature profitably.

In the end, the goal is to prioritize solutions for the most important and unsatisfied jobs that can be offered at price points the buyer is willing to pay. Effectively, you should build on the minimum cost to play and then add-in the highest priority features until you can no longer add benefits without making the price uncompetitive.

Rather than view this kind of scenario as an infringement on the design principles of the company, it should be viewed as an opportunity to drive innovation. After all, ideally a company would pursue this approach in the original design stage for a new offering. However, if this were the case, they probably would not be struggling with a need to reduce costs related to overshot or misaligned products.

The foundation of disruptive innovation rests on just such shifts from better to different, from complex to simple, or from the next-generation to the good-enough. Successfully executing these shifts requires knowledge of where customers are willing to make tradeoffs, and where superior performance must be maintained.

Thus, the ideal approach outlined above can and must often be implemented as a prioritization exercise for intelligently de-featuring an existing product or service. ◆

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The Art of Acquiring Growth

Acquisitions can help a company grow—except when they don't. Here's how to formulate the building blocks of a growth-by-acquisition strategy.

BY SCOTT D. ANTHONY & DHEERAJ BATRA

Organic growth is not the only lever available to growth-seeking companies. Many companies use acquisitions as tools to strengthen their position in existing markets or to enter new ones. Some companies are legendary for their acquisitive bent. General Electric acquires dozens of companies a year. Cisco Systems has made more than 100 acquisitions in its 20-year history.

Using acquisitions as a growth tactic is tempting. Creating new growth organically is far from a sure bet, and new businesses can take years to mature. Acquisitions can be a way to quickly goose sales and make sure the market has already identified the emerging company that is most likely to succeed.

Yet, significant research reveals a stark conclusion: Acquisitions, particularly large ones, tend to disappoint. One study found that managers reported more than 70 percent of all acquisitions fail to create value and up to half actually *destroy* value. High-profile struggles by the likes of auto giants DaimlerBenz and Chrysler or America Online's $180 billion acquisition of TimeWarner provide stark examples of mergers and acquisitions gone bad.

However, when done right, acquisitions can be valuable disruptive tools. We believe that disruptive-minded companies ought to consider acquisitions in the following four circumstances:

Circumstance 1: To consolidate an overshot market

Consolidation is a practical response strategy for incumbents in overshot circumstances. In these cases, investments in improvements along historically important performance dimensions promise diminishing returns. In these circumstances, consolidating an industry and squeezing out costs can be a way to growth profits.

While consolidation plays aren't necessarily the most glamorous of strategies, they can create substantial value. Consider Exxon's merger with Mobil in 1999. Back in the late 1990s, the price of oil was plunging. Analysts suggested that the era of growth for big oil companies was over. The combination of the two largest U.S. oil companies created the world's third largest company. The combined entity saved close to $5 billion in the two years after the merger; between 1999 and 2004, ExxonMobil earned $75 billion in net profit and generated more than $100 billion in free cash flow.

This success created a wave of mergers: British Petroleum merged with Amoco and Atlantic Richfield, Chevron merged with Texaco, and Phillips Petroleum merged with Tosco and then with Conoco. As the combined giants consolidated operations to take advantage of scale economics, they produced huge savings, and increased their market shares profitability.

Similar stories could be told in the banking industry (with Citibank snatching up Travelers, and Bank of America purchasing Fleet) and the telecommunications industry (with SBC purchasing AT&T and Verizon purchasing MCI). These companies realized that pushing for incremental advancements in saturated markets wouldn't be sufficient for growth. Joining forces to gain scale economies was the only way to continue to push profits ever higher.

One challenge with this approach is that, while it provides a temporary boost to the merged entity's fortunes, it doesn't fundamentally change industry dynamics. Once the glow of the merger wears off, the combined company faces continuing challenges to create even more growth. And the strategy is not sustainable: Acquisition targets that are meaningful enough to materially impact financial results become progressively harder to find and more expensive.

Circumstance 2: To buy time

Acquisition activity can also make sense when the acquisition allows an incumbent to "buy time" for its organic efforts to bear fruit.

The Innovator's Solution argues that companies need to start creating new growth businesses before they *need* to create new growth businesses. Why? Once it is clear that companies need to grow, they become very impatient. This impatience forces them to try to make new businesses get very big very fast, an approach that actually lessens their chances of success. Growth-ravenous companies naturally set their sights on large, lucrative markets populated by powerful incumbents, but these markets tend to be inhospitable for truly disruptive growth strategies.

Impatient companies can become trapped in a "growth-gap death spiral" when actions to quickly fill a growth gap result in an even wider growth gap. Because of the perverse dynamics of the death spiral from inadequate growth, achieving growth requires an almost Zen-like ability to pursue growth when it is not necessary.

But what about companies that recognize that, although the time to be a Zen master was years earlier, they need to change *now*? Should they simply pack up their bags and go home? For these companies, moderate-to-large acquisitions can provide "air cover" for the corporation's organic innovation efforts.

For example, IBM acquired Lotus for $3.3 billion in early 1995. Lotus's growth had stagnated as it fought against emerging email providers. Buoyed by IBM's top-flight sales force, deep relationships with key enterprise customers, and willingness to spend big bucks on marketing campaigns, Lotus experienced significant growth after the acquisition. Lotus sold roughly 3 million units of its flagship Lotus Notes application prior to the acquisition; by 1998 the division had sold close to 30 million units.

That growth couldn't have come at a better time for IBM. Lotus's growth provided cover for IBM's emerging move into services. In fact, Lotus helped to facilitate that move—by 1998 IBM estimated that it received $5 in service, support, consulting, and hardware revenues for every $1 of Lotus Notes sold. It is possible that IBM would not have been able to make the seemingly seamless move into services if Lotus had not grown so robustly during the 1990s.

Pharmaceutical companies are increasingly eyeing acquisition as a tactic to fill emerging gaps in their product pipelines. Many large pharmaceutical companies are organized to create "blockbuster" drugs that produce billions of dollars in revenues. They invest heavily in research and development, and take advantage of patent protection to recoup their investment.

However, the unpredictable nature of the discovery process can leave companies in an awkward situation. Just as a company's key drugs are coming off patent—enabling competition from providers of low-cost generics—its near-term pipeline can be barren. In these circumstances, acquisitions can be a viable "stall tactic."

Circumstance 3: To acquire disruptive seeds

Acquiring big companies tends to produce poor returns because the market can appropriately recognize the value in a large company. In these situations, the only way a company can create value is by spotting value that the market doesn't see. This is an incredibly tough challenge, especially for multi-billion dollar companies in established markets that are covered by scores of analysts.

However, while the average return for a small acquisition is similarly meager, the range of results is much wider. The odds of betting wrong are high, but the odds of getting a smashing success are much higher as well. Our belief is that an understanding of the patterns of disruptive innovation—looking with "disruptive lenses"—can help companies more reliably spot the potential winners. Companies can in essence get predictably higher returns on small acquisitions by using disruptive lenses.

There are a number of classic stories of companies acquiring small disruptive companies at relatively modest price points. A great example of a company prospering with a small acquisition is electronics retailer Best Buy. In 2002, the company purchased a 50-person company in its backyard of Minneapolis called Geek Squad. The company provided IT services for individuals, sending technicians to help consumers repair computers, set up networks, and install and manage high-end equipment.

Geek Squad's strategy followed a classic disruptive approach, making it simple and affordable for individual consumers to tap into IT expertise. Best Buy paid roughly $3 million to purchase the company. Analysts estimated that in 2006, Geek Squad had more than 10,000 employees, produced close to $1 billion in revenues, and generated $280 million in operating profits.

Buoyed by its success with Geek Squad, Best Buy expanded its services-focused efforts. By 2007, it offered home entertainment installation and design services through

Magnolia and home remodeling services through Pacific Sales. Both are offered through a store-within-a-store concept, similar to how Best Buy grew Geek Squad.

In 2005, Best Buy acquired two more companies—AV Audiovisions (for about $7 million) and Howell & Associates (for about $1 million)—to augment its Magnolia offering. In early 2007, Best Buy extended its services strategy to small business customers with its $97 million acquisition of Speakeasy, a DSL and VoIP provider. These small acquisitions have allowed Best Buy to create disruptive offerings that allow individuals and small businesses to affordably obtain world-class service.

In the early days of a disruptive innovator's journey, the market is likely to undervalue its potential. Innosight Director Richard Foster describes how the traditional "S-curve" that most innovations follow leads to substantial forecasting error. Before the innovation begins to march up the S-curve, analysts that base their valuation on extrapolation of past trends can dramatically underestimate the innovation's potential, because analysts' techniques are generally less effective in measuring non-existent markets.

Companies that spot disruptive developments early can meet the challenge of acquiring legitimately disruptive, high-growth companies at reasonable prices, before the market recognizes its disruptive potential. If the market does catch on, the price tag goes up substantially, such as when eBay had to pay more than $2.5 billion for Skype in 2005.

Circumstance 4: To acquire enabling technologies

Finally, companies can seek to acquire a key enabling technology that promises to power a disruptive movement. The acquiring company can use the technology to power its own disruptive offerings and sell it to other would-be disruptors.

For example, by 2006 it was clear that newspaper companies seeking to respond to the disruptive forces in their industry had to move beyond providing "news.com" Web sites to create better ways to organize and present local information. While Google and Yahoo unquestionably owned the national search space, consumers looking for local information had to rely on word of mouth or the Yellow Pages.

Newspaper companies seeking to move into these markets had to develop Web offerings that had rich, easily searched information databases. A company called Planet Discover emerged as a key enabler of these applications. In May 2006, newspaper publisher Gannett acquired Planet Discover for an undisclosed sum.

The president of Gannett's digital arm said at the time, "Gannett truly understands the importance of local information, which is why Planet Discover is such a perfect fit for us. With this new relationship, we will move more emphatically into deep, robust local search for our Web sites. This fits well with our mission: To be the go-to provider of must-have local news and information across all media."

Cisco also followed this approach when it purchased set-top box manufacturer Scientific Atlanta for close to $7 billion in late 2005. Cisco recognized that the computing and television worlds were converging and that it would have to couple its competency in the data networking world with competency in the video world. Scientific Atlanta, a leading provider of video equipment, could help Cisco move into the video space (for more on Cisco's growth-by-acquisition strategy, see also "Innovator's Update: Reinventing Titans, Round Two" on page 4).

Companies that are attuned to disruptive developments can spot these key enablers early, before the rest of the market sees their value. They can then pay reasonable prices to improve their own disruptive ability, while profiting by selling the capability to other would-be disruptors.

Acquisition as strategic tool

Statistics suggest betting against companies that seek to use acquisitions to boost returns. However, in the right circumstances—when markets are ripe for consolidation, when the acquisition provides air cover for organic efforts, when a company spots a disruptor before the market, or when the acquisition enables disruptive growth—acquisitions can be a valuable strategic tool.

While following the approaches described here is unlikely to result in a front-page story in *The Wall Street Journal*, they *are* likely to deliver what really matters: results. ◆

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'100 Days' (continued from page 1)

light of day, because senior managers intuitively (and correctly) get squeamish about placing big bets on highly risky plans.

There is another way. Through work with some of our clients—many of them in Asia—we have developed a simple, five-step process that can help companies go from a desire to disrupt to a funded disruptive business plan in less than 100 days.

Step 1: Identify opportunity areas (5 to10 days)

Before developing specific plans, companies should step back to identify broad opportunity areas (sometimes called "domains" or "growth themes") that can form the basis of the investigation.

While companies sometimes think the key to innovation is to encourage unbridled creativity, our belief is that focus is an important enabler of success. As one senior executive told us, "What are our odds of success if we trawl the ocean looking for a whale?"

Finding new, high-potential opportunity spaces isn't always obvious. One trick is to imagine adjacent markets that you touch, but in which you don't actively participate. Look for a market that is close to the core so that your capabilities, assets, or knowledge could form the foundation of a new growth offering, but far enough away that traditional competitors might scratch their heads when they hear about the opportunity space.

The disruptive concept of nonconsumption can be a helpful tool as well. Consider markets in which factors such as product cost, complexity, or inconvenience constrain consumption. For example, there are more than 46 million people in the United States without health insurance. This market has obvious potential for disruptive growth.

Ideally, companies seeking to look beyond the "normal" opportunities that characterize their market should combine the wisdom and judgment of senior management with a healthy dose of experienced judgment that has been gained through achieving not only success, but equally importantly, *painful* failures. It is the pain from these failures that prevents decision-makers from taking easy or obvious paths when their gut instincts tell them something more is required.

Selecting domains requires striking a delicate balance. Howard Stevenson from the Harvard Business School defines entrepreneurship as "the pursuit of opportunity without regards to resources controlled." However, companies do have to have (or be able to create) some kind of right to win in a marketplace.

Spotting opportunity spaces requires managing this balance, remembering that tomorrow's capabilities might look very different from today's capabilities.

Selected opportunity areas should be broad, such as "real estate" or "low-cost tires," and strategically important to the company.

Step 2: Generate idea list (14 to 35 days)

In the next stage, a small team should develop a long list of innovative ideas. The team's goal isn't to develop detailed business plans around each idea. Rather, the team should form nuggets of ideas that can be shaped and polished in the next steps of the process.

The concept of jobs-to-be-done aids this investigation. Remember, this concept holds that great growth opportunities are found in helping people address pressing problems that aren't adequately solved today. The jobs lens provides a blueprint for innovation by zeroing in on key customer pain points.

THE 5-STEP, 100-DAY PROCESS

Step 1: Identify opportunity areas (5 to 10 days)

Activities: Quick scan of adjacent markets; analysis of nonconsumption

Output: Selection of opportunity areas

Step 2: Generate top ideas (14 to 35 days)

Activities: Jobs-to-be-done research; capability analysis; trend analysis; synthesis

Output: Creation of 15 to 20 ideas (target customer, jobs, potential soutions)

Step 3: Disruptive business-building workshop (2 days)

Activities: Opportunity-shaping and whittling

Output: Selection of 3 to 4 lead ideas

Step 4: Build business plans (14 to 56 days)

Activities: Qualitative assessment; back-of-the-envelope financial analysis; completion of 12-page disruptive business plan

Output: Detailed proposal for low-cost pilots (<$200K)

Step 5: Senior management decision-making workshop (1 day)

Activities: Assessment of pilot proposals

Output: Approval to move forward with pilots

Concurrent with the jobs-to-be-done investigation, the team should develop a detailed balance sheet of the corporation's capabilities and disabilities. What assets does the company really have to bring to the identified opportunity spaces? What liabilities will they need to overcome? The goal is to see if there are internal capabilities that could open up new opportunity spaces (such as when Philips started selling its design capability to outside companies), and to begin to think about what capabilities the company will need to create or acquire to master growth.

The final analysis should quickly map out the trends taking place in the given industry space.

Over the last week of this stage, the team should synthesize its work by creating a list of 15 to 20 potential opportunities, each described in two to three sentences that identify the target customer, the job they are trying to get done, and preliminary thoughts about potential solutions. The emphasis during this stage should be on making quick progress. This should not be a boil-the-ocean analytical effort, nor is it intended to be totally exhaustive. Rather, it is a quick way to develop a long list of interesting ideas to get things rolling.

TEMPLATES, FRAMEWORKS ENABLE SUCCESS

The use of simple templates and frameworks can be an incredibly powerful enabler of ideation activities. For example, in March 2007, Innosight Asia and the Confederation of Indian Industries put on a day-long Innovation Summit for 190 Indian managers. The managers came from a wide range of industries and included a rich mix of mid-level managers and CEOs. Most people at the pre-assigned 10-person tables had never met before.

After Clayton Christensen presented the core concepts of disruptive innovation, Innosight Asia presented four opportunity areas: power, automotive, energy, and shipping and transportation. For each, Innosight Asia described some jobs associated with particular customer groups.

For example, a customer who cannot afford regular power service in their home might have the job of, "I want to host a party/dinner at home, for which I need moderate power access for a fixed period of time." Or a grid customer who needs moderate amounts of power at specific times might have the job, "I want to sell my excess power to my neighbor when I do not need it."

Each table spent five minutes selecting the opportunity area that interested them the most, and 10 minutes quickly selecting a pre-worked job-to-be-done. Then they spent an hour coming up with a disruptive solution to that job.

Armed with new concepts and simple tools, the teams came up with a fascinating set of opportunities. For example, one team developed an idea for a "dentist office on wheels" to provide simple, low-cost dentistry services.

A similar idea in a very different space was a portable electronic retail store—essentially a truck trailer that is pre-configured like a store that could be set up in rural areas that lack access to electronic items.

Step 3: Hold a disruptive business-shaping workshop (2 days)

Now the team, key stakeholders, and any other good, innovative minds in the company come together for an immersive two-day workshop. The purpose is to select the highest-potential ideas and begin to flesh out possible solutions.

The first day begins with an overview of the key principles of disruptive innovation, to stir people's thinking about how to spot and seize opportunities.

The rest of the session involves a series of facilitated breakout group discussions. During the breakout group discussions, the group divides into small teams to work on specific opportunity areas. Each team's job is to prioritize the list of raw ideas in their selected area, and then develop one idea into a skeleton business plan.

Teams do this by going through a three-step process. The first step is to define (or refine from the pre-work) a high-potential job-to-be-done—an important innovation problem that isn't being adequately addressed. The second step is to develop a solution that gets the job done better than current alternatives. Finally, the third step is to craft a compelling business model and develop a rough plan to take the idea forward.

At the end of this activity, the large group comes together to prioritize ideas that it thinks have the most growth potential.

One good way to do this is to emulate venture capitalists and allocate play money to the ideas that have been developed.

Useful criteria for selecting an idea include:

1. Is the idea truly disruptive? Consider:
   - Is the job BIG, as well as unsatisfied?
   - Can we find a compelling foothold customer and solution to make progress?
   - Can we start small and earn early profits?
   - Can we avoid competition from large incumbents?
2. Can we find a way to implement with low fixed costs (to allow for iteration) and to pilot the concepts cheaply?
3. Are there long-term sources of competitive advantage available (especially learning curve advantages)?
4. Is there a path to profitability in 24 months or less?

Then, the groups switch up, pick up another set of ideas, develop skeleton business plans, and select the two with the most potential.

Finally, the entire group steps back to evaluate the four to six ideas that it identified as having the highest potential, selecting the leading candidates that will be evaluated in the next stage of the process.

While the two days can be intense, we find this facilitated process—winnowing down the list, building skeleton plans, and focusing on the ones with highest growth potential—is an effective way to make quick progress on a number of ideas, draw in widespread expertise, and begin building organizational buy-in around the ideas.

The results of this workshop aren't immutable decisions about which business plans to write. We find that about half of the output of the process's next stage emerges from discovery and bears little in common with what was discussed in the workshop.

Step 4: Build business plans (42 to 56 days)

Over the next six to eight weeks, the team should further flesh out the selected skeleton business plans, specifically driving toward creating a detailed plan for a low-cost pilot to test the selected idea.

Guiding this effort is a disruptive template that facilitates addressing a series of questions about the opportunity, such as:

- What "job" are we trying to attack?
- What is the size and nature of the benefit from getting it right? Financial? Emotional?
- How many, and which, customers currently have these jobs?
- What three to four key features define our solution? What combination of "gives and gets" will meet the job more effectively?
- On which dimensions will we be only good enough?
- Who are the major competitors?
- If we get this right, how much money is in it? When?
- Can we run an operational pilot with limited funds (e.g., less than US$200,000)?

The team can answer these questions and build their plans via intense working sessions augmented with some focused research efforts. The primary goal is speed, so tools such as focus groups, rough mock-ups, and subject-matter-expert interviews are appropriate.

While companies might feel pressure to create several-tab-level-deep financial forecasts, we caution against that. Instead, we are big proponents of using qualitative assessment tools that can help further unearth risks and unknowns.

On the financial front, companies should start with their targets. What kind of revenues must an opportunity generate on an ongoing basis to be attractive? How soon must it produce positive cash flows? Then calculate backward from those figures to determine what has to come true to reach those projections.

This process is highly emergent and intuitive. Often, the best idea comes midway through the process, as investigation shows that an idea discarded in the workshop actually has growth potential, or unearths an idea that had never been discussed. The team has to remember that it isn't following a pure paint-by-numbers exercise and to be careful to watch for these emergent signals.

Step 5: Decision-making workshop (1 day)

Finally, the team and selected senior managers coalesce to make decisions about which pilots to fund. The first time through this kind of process, it is useful to start with a review of key disruptive principles. Then move to the specific ideas.

Try to make sure the presentations don't drone on, but are used as opportunities to engage management in the ideas and begin active problem solving.

This session is itself an opportunity to change interactions between senior management and project teams. In disruptive circumstances, senior leaders must shed their devil's-advocacy hats and take more of a problem-solving role.

This session can be a great way to begin to engage in collective problem solving about how to address the unknowns. However, at the end of the day, senior management must put its money where its mouth is and sign up to move forward with at least one of the pilots.

Keys to 100-day success

There are three keys to succeeding with this approach. The first is for senior management to provide clarity about its goals and boundaries for the innovation exercise. Senior managers should make very clear the areas in which they are interested, the ones that they would consider in the right circumstances, and the ones that are off the table. We encourage keeping the "off the table" list short, with periodic check-in points to ensure the effort doesn't wander into areas that make senior management *too* uncomfortable.

The second key is allocating resources toward the efforts. It is critically important that senior management agree at the beginning of the process that it will allocate at least some financial and human resources to the winning plans. If senior management *doesn't* make that commitment, the process could likely stall after the final workshop.

Finally, key senior managers should participate actively in the process. Simply showing up at the final meeting isn't enough. Unlocking the power of disruptive innovation requires senior leaders to shift mindsets and act differently. Joining the team for at least part of the journey can help create shared understanding that translates into a real capability.

The approach described in this article is straightforward; however, it is not purely rules-based. Nor does it work in every circumstance. For example, this process would not work for capital-intensive industries that have multi-year development processes (such as pharmaceuticals).

As noted previously, seasoned judgment and intuition must inform many of the strategic decisions made during the process. Companies also must recognize that going through this kind of approach won't produce perfect answers. Instead, the idea is to quickly make progress on an idea and learn from real-world experience.

Following these steps can help teams quickly develop actual, fundable business plans that allow their companies to realize returns from their desire to do things differently.

The U.S. newspaper industry has been struggling over the last few years to cope with seeming hordes of disruptive attackers. After going through a version of this process, Ron Welby, of Enterprise NewsMedia remarked, "It was a lot of work. We had to make time for these meetings, but I think it brought us all much closer together. It really built the strength of the team. We feel like we can take on the world."

One hundred days from a glimmer of hope to an ability to take on the world. Not too shabby. ◆

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