Audio-Tech Business Book Summaries

24/7 Innovation

A Blueprint for Surviving and Thriving in an Age of Change

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A summary of the original text.

In this issue:

- ***Transform...*** your business into one that continuously innovates — every hour, every day, in every department, by everyone.
- ***Implement...*** a proven process for targeting, generating, and selecting great ideas throughout your organization.
- ***Design...*** an innovative strategy based on adding more value for customers, listening to customers, serving customers, or hiring customers.
- ***Deploy...*** the right technology to enable collaboration among your people, to support decisions with real data, and to capture good ideas in idea banks.
- ***Learn...*** how you can use measures to drive innovation by focusing on outcomes, shooting for stretch performance, and measuring the right things.

A culture of innovation can be a company's primary source of competitive advantage, and it can pay off handsomely over the years. But if you want to create this kind of culture, you can't hold a few meetings with a handful of key people once or twice a year.

Instead, you must continuously inject innovation throughout the execution of each process, *every day, by everyone.* In this way, innovation will become as natural as breathing, and the company and its people will easily come up with new ideas to satisfy the constantly changing whims of customers.

But how can you do this? By focusing on developing the right capabilities for innovation.

This is what gives leading companies their strength, their staying power, and their value. Continuously innovative companies command a premium in the stock market because analysts prize their ability to renew, reshape, and refocus their energies to meet new competitive challenges. Analysts say this premium can amount to as much as 20 percent of the underlying value of a company's shares.

To reach this level of innovation, you can't focus only on improving processes. Instead, you must take a holistic view of the business and integrate all of the critical components of a capability. By *capability,* we mean a combination of people, processes, and technology that enables a company to perform activities. Capabilities derive from a business strategy, and they deliver measurable results.

Companies have many capabilities. Some are focused on production, distribution, or sales. Others revolve around support functions, such as finance, information technology, or human resources.

All capabilities are composed of five components:

1. Process.
2. People.
3. Strategy and Customers.

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4. Technology.

5. Measures and Performance.

Innovation is every company's most crucial capability. Therefore, all five components of the innovation capability must be fully developed for a company to be innovative.

- First, you must use a ***process*** to support innovation, so that it is not random, but rather based on a standard model for targeting, generating, and selecting innovative ideas.

- Second, the ***people*** who are responsible for innovation should not be limited to a few creative professionals. Instead, innovation skills must be valued above all others by everyone in the company.

- Third, you need a ***strategy*** to decide when, where, and how innovation will be used to satisfy ***customers.***

- Fourth, the right ***technology*** must be in place to enable collaboration among people, to support decisions with real data, and to capture ideas in idea banks.

- Fifth, you must link innovation ***measures and performance.*** The measures should be focused on business outcomes and results, and they should drive compensation for everyone in the company.

These five elements provide a blueprint that any company can use to create perpetual innovation. By contrast, in most companies, innovation only occurs when someone decides it is time to innovate. Often, the call for innovation happens in crisis mode, when it's already too late: when a competitor is stealing market share, when a once-popular product is no longer selling, or when customers have discovered a better, faster, or cheaper alternative.

When companies see innovation as a capability, however, people do not only innovate to solve the problems that are presented to them. They innovate in everything they do. They continuously improve their products, processes, and organization.

But what kind of innovation should it be? Should it be *incremental innovation* that leads to modest increases in efficiency, or *radical innovation* that completely reshapes the business model, its cost structure, and its markets?

The ideal answer is to use *both* types of innovation. When combined, radical and incremental innovation will allow you to change your operating model while also sustaining a competitive advantage over time. Often, this requires nothing less than continually reinventing the company.

As Gary Hamel, visiting professor of strategy at the London Business School, proved in 1997, the only path to sustainable success is to use innovation to change the rules of the game in your industry.

Hamel found that between 1986 and 1996, only 17 companies out of the *Fortune* 1000 grew their shareholder return at an average annual rate of 30 percent or more. And he revealed in a Fortune magazine article called "Killer Strategies That Make Shareholders Rich," 16 of the winning firms either created new markets or transformed existing markets. The seventeenth reengineered its way to spectacular shareholder value.

Hamel predicts that "the ability to reinvent the basis of competition within existing industries and to invent entirely new industries . . . will be the next fundamental competitive advantage for companies around the world." This requires radical and incremental innovation every day.

In this summary, we will discuss each of the five main components of the innovation capability in greater detail. Next, we will explore the technique of targeting to push the envelope of innovation. The final section describes the stages of change that a company must go through to achieve the ultimate goal of pervasive, 24/7 innovation.

PROCESS

Let's take a closer look at the first element of a capability: ***process.***

Sparking innovation in a company should not be a random activity, like lightning. Instead, innovation should be encouraged by managing the interaction of processes.

Let's be clear about what we mean by process. It is a way of organizing a company's activities and resources that establishes cross-functional coordination throughout the firm.

This kind of coordination makes the pieces of the business work smoothly together to achieve the company's

goals, while also unleashing innovation throughout the organization.

Process innovation is about generating, evaluating, and implementing creative solutions. But such innovation does not just happen. It emerges when people ask the right questions about the work they are performing, and about the ways that work could be improved.

To help you get started, here is a helpful framework for dividing the questions you must ask. The questions can be divided into seven categories called the "Seven Rs."

1. Rethink.
2. Reconfigure.
3. Resequence.
4. Relocate.
5. Reduce.
6. Reassign.
7. Retool.

Each category refers to a different dimension of process and business change.

The first R, *Rethink,* is concerned with the reasons and assumptions behind the company's processes. These are the "Why" questions, as in "Why are things done the way that they are?"

For example, an airline was suffering from the high cost of carrying an excessive inventory of spare parts. The obvious solution was to improve its inventory management. But on closer examination, it was discovered that the problem lay elsewhere. The company used its own planes to move spare parts. But whenever there was revenue freight to be loaded, the parts were left on the ramp. That caused delays, and the airline began stockpiling parts. Those kind of hidden assumptions can be uncovered by rethinking.

The second R, *Reconfigure,* is about the activities involved in the processes. Here the aim is to find new answers to questions that begin with "What," as in "What activities can be eliminated?" Reconfiguring can also involve asking what you can do to redesign a step to make it cheaper, faster, or better. If the process is performing poorly, you may need to start from scratch. Ask, "What would be the perfect solution if we were starting to do this with an entirely new company?"

The third R, *Resequence,* deals with the timing and order in which activities are done. Here the innovation comes from asking "When?" Consider questions such as, "When do particular tasks need to be done?" "Do the tasks have to be done in this sequence, or can we get better results by changing the order in which they are done?"

Sometimes it even makes sense to postpone an activity, because doing so gives you more flexibility. For example, Benetton sells its clothing through 6,000 small boutiques in 120 countries. To get around the problem of rapidly changing fashions, Benetton makes many of its garments in a neutral color, rather than from predyed yarn. When it becomes clear which colors will be popular during a season, the company dyes items just before they are shipped to the shops.

The fourth R is *Relocate.* This R deals with minimizing distance and maximizing communication. It asks questions that begin with "Where." For example, "Where could the activity take place so that we could minimize the shipping time between the company and its suppliers or customers?" For example, Volkswagen arranges for its major suppliers to assemble their components inside its plant in Brazil. This way of working leads to high-quality, accurate just-in-time delivery.

At the other extreme, innovative companies like General Electric are storing goods that they supply to their customers. Small appliance stores can't stock everything GE makes, so GE offers a "virtual inventory" system. Products are kept in GE's warehouses rather than the stores, and GE ships the orders directly to the customer.

The fifth R is *Reduce.* Questions in this category are concerned with the frequency of activities. It asks, "How much of the activity needs to take place, and how often?"

Sometimes innovation means doing something more often; sometimes the innovative answer is to do it less frequently.

For example, gathering more information through data warehousing and data mining allows companies to target highly effective marketing promotions.

On the other hand, less information and fewer controls can improve efficiency. One copier company eliminated its policy of relying on customers to read the meter and send a reading back to generate a bill. Too often, this approach

lead to errors and delays. Instead, the company now bills its customers at a flat monthly rate. Once a year, when the service technician goes out to service the machine, he reads the meter and the company sends a reconciled bill.

The sixth R, *Reassign,* concerns the people who perform the work. It includes coming up with new answers to questions that start with "Who." For example, "Who carries out the activity?" "Could someone else possibly do it more effectively?"

In nearly every industry today, companies are turning to suppliers, customers, strategic partners, outsourcing firms, and temporary employees to do work that was previously handled in-house. This is the most powerful of the Rs, because it offers the potential to change a company's operating model dramatically. You must decide who could get the work done most efficiently. The answer may be to outsource the process, or to set up a new business unit. Or the innovative solution may be to allow the customer to perform the activity, just as FedEx has customers schedule their own pick-ups and track their deliveries on-line.

Finally, the seventh R stands for *Retool,* and it involves how technology and competencies function together to get the job done. It seeks new answers to questions that begin with "How," such as "How can technology transform this process?"

For example, hand-held computers transformed the rental car industry, allowing employees to check in returned cars in the parking lot. And in every industry, companies use the Internet to allow customers to place orders, make payments, and communicate with the staff electronically.

To achieve 24/7 innovation, everyone in the company should use the Seven Rs to continuously ask the seven types of questions: "Why?" "What?" "When?" "Where?" "How often?" "Who?" and "How?" The answers to these questions will allow you to challenge old ideas and create new ones.

You can also use a powerful innovation technique by combining the categories. To use this technique, called *morphological analysis,* select some or all of the Seven Rs and come up with various answers to each, then randomly mix and match various combinations.

For example, if you wanted to redesign the checkout process at a supermarket, you might look at Reassign, Relocate, and Resequence. This is the typical combination for checkout that is done by the cashier, at the cash register, after all the purchases are made.

Let's try a different combination. What if the customers did the scanning, at their shopping carts, as they selected each item from the shelf? This is exactly the process innovation that Safeway is testing in London supermarkets.

Even when you generate combinations that seem like losers, the exercise can help you uncover underlying assumptions. For example, why can't butchers scan groceries at the meat counter when all of the checkout lanes are crowded? It might not work, but considering new possibilities leads to real innovation.

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Creating a Culture of Innovation

By attending to the seven Rs of process innovation, a company begins to make its first move toward 24/7 innovation. To do that requires a high-performance culture, one in which everyone is empowered to innovate all the time.

The most effective way to install a culture of innovation is lead the change from the top. A program for change can cover dozens of elements, ranging from dress code and office design to technology and working hours. Culture also embraces symbols, from whether senior managers park in reserved spaces to whether they can be addressed by their first names. If you change these symbols, you change the culture.

Truly effective leaders must be able to do several things to create a culture of innovation:

1. They have to be able to create a sense of urgency about change. Often the best way to create this urgency is to reveal a crisis, such as sharply falling profits, that pushes people out of their comfort zones.

2. Leaders also must identify the best resources for the job and pull together the right people, processes, and technology.

3. Leaders have to create and communicate the vision of the new culture of innovation.

4. Leaders must have the

ability to overcome resistance. They have to act quickly to defuse any doubts from employees that the new culture is better than the old one.

5. Leaders must have enough clout to make the moves they envision, including reassigning the company's best people to jobs that will support 24/7 innovation.

In addition to effective leadership, a culture of leadership also depends upon a process for innovation. Without a process, innovation will be random and people will wait for good ideas to come to them.

Let's make an important distinction about processes. We've already discussed how you can make innovations in *business processes.* What we're exploring now is the *process of innovation* itself, and how it can be a tool to shift the company's culture. This process should be a systematic approach to identifying opportunities and to generating ideas and refining them into high-value solutions.

There are many different innovation processes you can implement at your firm. However, whichever one you choose, it must separate the tasks of divergence and convergence. *Divergence* means generating many ideas. At this step, you must defer judgment, focus on quantity, and look for new possibilities that will stretch your thinking.

Convergence means evaluating those ideas to see if they will work. It is only at this stage that you should look at the ideas critically, and then choose the most valuable and relevant solutions.

Here is a simple four-step innovation process:

1. Envision.
2. Enable.
3. Explode.
4. EmpowerTool.

In Step 1, *Envision,* practice divergent thinking. Everyone should try to think of as many ideas as possible, without attempting to narrow them down. Create new perspectives on everyday facts and figures, and explore relationships between them that might open the door to truly revolutionary insights.

In Step 2, *Enable,* the aim is to filter the view of the vision that has come from the first step. The filter might be "How would a company in a completely different industry handle this situation?" During this step, the goal is to figure out what is possible, not what would be the "right" solution.

To illustrate this point, imagine that you have been asked to design a two-day tour of Paris and have been given a list of attractions. Most people immediately eliminate certain attractions and create a list of priorities; in other words, they use *convergent thinking.* But they do not allow themselves enough time to *diverge* by considering many different facets of Paris.

To innovate, go back to Step 1 and envision a tour of Paris. One new idea might be to focus on a tour of the city that uses all of the senses. Now, in Step 2, you can apply a filter such as "How do you think Mozart would design a tour of Paris?" This filter suggests more filters, such as "What if the tour were organized around the sounds of the city?" Or "How might you organize a tour that had the flow and feel of an opera?" Each one of these filters provides a route to a unique, memorable tour of Paris.

Remember, though, that none of the details are worked out during the Enable step. You still do not know where you are going. For that, you have to wait for the next step.

In Step 3, *Explode,* you can use traditional brainstorming techniques. By this point, you have a vision and you've looked at it through different filters. Now you can explode with ideas. The key is to focus on relationships instead of activities.

In Step 4, *EmpowerTool,* you begin to make the ideas happen by defining the capabilities that are needed to make them actually work in practice. Instead of rushing to implement the new idea within your old comfort zone, using the same structures and people, you need to decide which new combinations of technologies, processes, and people will help the idea to succeed.

When you have both effective leadership and an innovation process in place, you are well on your way to create a culture of innovation. However, you must still give people a motivation to innovate. Later in this summary, we'll discuss how measures and performance help people to see the value of innovation.

At least four more elements of the culture are needed to ensure that people will innovate:

- First, *get everyone to practice macro thinking.* Macro thinking requires cutting across organizational and philosophical boundaries to work as a team. Show everyone how to focus on outcomes and results, not on the specific activities they are performing.

- Second, *develop an entrepreneurial mind set among all of your people.* To be innovative, employees must be able to take risks. As soon as people go from just doing their jobs to asking, "Why do we do this the way we do it?" you know that you have reached that level.

- Third, *remove the fear of failure.* If you want people to try new concepts, you cannot punish people when those ideas fail.

- Fourth, *help employees to feel like owners.* They need to go beyond what is expected of them in order to suggest new ideas for generating profits for the business.

A culture of innovation is vital to a company, and it is almost impossible for a competitor to imitate. With an impassioned leader, a process for innovation, and empowered people with the right skills, you can build a culture that continuously finds new solutions to large and small problems.

Customer Strategies

Developing a culture of innovation requires looking inward. But true innovation only begins there. Next, the company has to begin looking outward, toward the customer. More than ever before, managers need to know how a customer thinks. To get closer to your customers, you can use four customer strategies:

- First, add more value for your customer.

- Second, listen to your customer.

- Third, serve your customer.

- Fourth, hire your customer.

To use the first strategy, ***discover new ways to add more value to the goods and services that customers are willing to buy.*** For example, food manufacturers have found that people will pay extraordinary premiums to have their fruit peeled and their lettuce washed.

There are three main ways that you can add value:

1. Offer convenience.

2. Make customers feel good about your products.

3. Decommoditize your products.

Offering convenience, as the food manufacturers are doing, is a great way to add value. The makers of Peak antifreeze provide another example. They are now selling a "pre-diluted" product that is 50 percent water. To save the minute that it would take to mix anti-freeze with water, motorists are willing to pay full price to buy a half-gallon of engine coolant.

Another way to add value is by *making consumers feel good about their purchases.* This tactic was pioneered by The Body Shop, the cosmetics retailer that trades on an image of caring about the environment. Other companies make sure that their customers know that a portion of their profits are donated to charities or invested in the local community.

You can also use *decommoditization* to add value for customers. Customers place a higher value on products and services that have been customized to suit their unique needs. For example, Dell computers are configured on-line by the customer. Levi Strauss developed Personal Pair jeans with 5,000 different sizes for different-shaped bodies. For $15 more than the typical cost of off-the-shelf jeans, customers can get a perfect fit.

The second strategy for getting closer to customers is to ***listen to them.*** The only way to understand what customers value is to listen carefully, and often, to what they say and to watch carefully what they do. If a customer likes something and is willing to pay for it, then it has value.

To listen to customers, you must collaborate with them. For example, a computer hard drive company was in danger of losing its biggest account, a large computer manufacturer, because it could not keep up with the demand. At the same time, a competing hard drive company was offering to supply drives at a lower price.

By collaborating with the customer, the first hard drive firm learned that the reason for the increased demand was a new program that allowed end users to return old equipment for upgrades and refurbishments. The program was a tremendous success, and the computer company's

need for hard drives increased dramatically.

As a result of what it learned, the hard drive company created a manufacturing line to refurbish returned hard drives. The company discovered that this change allowed it to meet the increased demands of the computer manufacturer. It also reduced the costs of the drives to match the prices of the rival firm.

The supplier and the customer also entered into an agreement to link their supply chains and share warehouse space. Through all of these collaborative moves, the company not only retained its most valuable customer but increased its profit on hard drive sales by more than 18 percent.

The third way to get close to the customer is to ***serve your customers.*** Customers can either be product-oriented or service-oriented. Product-oriented customers hunt for bargains. They are not willing to pay a premium for higher quality products or better service, so it is difficult to add value for them.

In contrast, service-oriented customers demand convenience and are less concerned with price. They are often looking for more than a particular product. They want to satisfy broad personal goals, such as "a healthy old age," "a secure future for the children," or "a desire to see the world." The opportunities to add value for these customers, and to capture value from them, are enormous.

By bundling goods and services, either from your own company or other firms, you can create solutions that fulfill the customer's goals. The Internet offers many Web sites that provide solutions for serving customers.

For example, Microsoft's HomeAdvisor allows a consumer to do practically anything related to a house move, including finding a house, getting financing and insurance, making the move, turning on utilities, and obtaining guides to various locations.

Finally, the most powerful customer strategy is to ***hire your customers.*** If you think about it, the person who can create the best outcome for the customer is the customer himself.

Customers now are asked into the company to participate in everything from business redesign to order acquisition and service. Through the Internet, *collaborative product commerce tools* allow customers, partners, suppliers, and others to collaborate with product development.

Through such tools, customers can now serve themselves, educate themselves, share information, rank products, and become partners in your business enterprise.

For example, it's now become routine for customers to go to Web sites, such as Disney's retail site, and do all of the work that a Disney "cast member" does in Disney Stores. Customers compare items, pick out the right size, and then place their own orders and enter their own credit card payments.

Through the four strategies of adding more value, listening, serving, and hiring your customer, your company can stand out in today's customer-driven marketplace. To make these strategies possible, you need to use information technology. That is the next component of the innovation capability that we will discuss.

Technology and Innovation

Once you are looking out from a culture of innovation toward the customer, it is time to begin using technology to enable and foster innovation. To do that, you have to start thinking of technology not as automation, but as a transformational element. Fortunately, today's technology of interconnectedness provides the perfect platform.

There are five basic ways in which technology can foster innovation:

1. It can be used to create a virtual enterprise.
2. It can change the rules of the game.
3. It can allow you to collaborate across the value chain.
4. It can increase the knowledge of your employees.
5. It can help you launch new businesses.

Technology is helping all kinds of companies, not just start-ups, to create ***virtual enterprises.*** The Internet, combined with outsourcing, gave rise to a remarkable spin-off of Allianz in the Netherlands. Universal Leven is an insurance company that opened only two years ago, has opened 15,000 policies, and is adding 200 new policies a week. The company has only two employees, who handle corporate strategy, network

expansion, and product development. Everything else, including product branding, product design, marketing, and all back-office functions, has been outsourced to strategic partners.

Technology can also give you the tools to ***change the rules of the game.*** Instead of merely automating existing ways of doing business, you can create entirely new businesses.

For example, Fiat designed a car specifically to be sold on the Web directly to the customer. The customer can arrange for financing, pay cash, trade in a used car, configure the new car, and arrange for a test drive, all through the Internet.

The third way that technology can facilitate innovation is through ***collaboration across the value chain.*** That requires the sharing of information as its key driver. The more seamless and transparent information becomes, the less it matters where work is done, who does it, or even when it is done.

Such services as ClickCommerce can be used as clearing houses for information in any industry, providing everything from account status to product information, targeted promotional information, and order placement. Proposals can be written, revised, and reviewed in real time with instant feedback. Using such systems in redesigning its engine production process, Caterpillar experienced a 67 percent reduction in outsourcing costs and a saving of $1 million a year.

The fourth approach to using technology to drive innovation is ***increasing the knowledge of your employees.*** If business is more and more about knowledge, then you want to make sure your workers have the knowledge they need.

Sales reps, for example, typically spend only 20 to 40 percent of their time on selling. The rest is spent on administrative tasks that add nothing to the bottom line. Outsourcing the transactional work is the answer. Then they can work on increasing their productivity. Again, technology can facilitate this through distance learning. At BellSouth, a training program is forecast to save some $52 million over five years.

Finally, technology allows you to ***launch new businesses*** as a means toward innovation. One such company is Qpass, which is a service for content providers to make charges to customers that are too small to put on credit cards. Selling nearly 2 million digital products from companies such as *The New York Times* and *The Wall Street Journal,* Qpass provides quick and easy purchasing for customers while cutting the costs of digital commerce for publishers.

Technology can certainly foster innovation if used correctly. But consider the following factors when deciding when and how to use it:

- Make sure that it will be an improvement. Don't use technology for the sake of technology.
- Make sure the vision drives the use of technology. Don't let the technology take over.
- Design the process and the technology together. Don't spend a lot of time developing a process for which there is no technology.
- Put operational specialists, not IT specialists, in charge. Include both process and technology design teams.
- Don't focus on one technology to the exclusion of others. Keep a broad perspective.
- Ask the following questions to prevent technology from becoming a barrier to change:
    - Is this just clever technology or is it viable?
    - How much training will be required?
    - How much lead time will be required?
    - Do we have the IT skills to create it?
    - Is the system flexible enough?

Technology can do as much harm as good. But if used correctly, it can drive innovation that will help transform a company. Those who can master its use as a tool for innovation will thrive in the uncertain times ahead.

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INNOVATION THROUGH MEASUREMENT

Whenever a process is changed, whether through technology or other means, *measurement* becomes even more essential than it ordinarily is. But finding the *right things* to *measure* in the *right ways* is tricky. Accenture and the Center for

Business Performance have determined that there are seven ways to use measures effectively:

1. To *communicate* a range of performance targets.

2. To *compete* successfully by making strategic decisions on the basis of hard data.

3. To *compare* the company's performance with that of others.

4. To *compel* corrective actions by identifying variances that go beyond acceptable limits.

5. To *comply* with regulatory standards.

6. To *complete* projects within planned horizons.

7. To *commit* employees to the company's priorities through recognition and reward mechanisms.

In addition, there are three ways that measures drive innovation:

1. Focusing on outcomes.

2. Shooting for stretch performance.

3. Measuring the right things.

Consider the case of Electrabel, a Belgian energy provider, which concluded that the only way to survive increased competition was to be among the best in the utilities industry.

Electrabel's managers focused on the outcomes they wanted to achieve, defined key performance measures, and set stretch goals. They looked at how other utilities operated, but they also looked at companies that excelled in other kinds of distribution. And they used those standards as inputs to the designs of their own processes.

For example, the new distribution network was designed to meet customers' rising expectations. In package delivery, the standard is overnight delivery; in utilities, customers often wait an entire week to have their gas turned on. Electrabel nearly shortened its connection time from five days to less than 48 hours.

There is no one right measure for every company. To find the best ones for your business, ask the following questions:

1. Who are the key stakeholders, and what do they want and need?

2. What strategies are required to ensure that these wants and needs are satisfied?

3. What processes must be put in place to ensure that those strategies are delivered?

4. What are the required capabilities to do that?

5. What stakeholder contributions are required if a company is to maintain and develop those capabilities?

The heavy emphasis on stakeholders is deliberate, for it's now recognized that you can't make stockholders happy if you are ignoring your customers, suppliers, employees, and other stakeholders. Boeing, for example, is the Dell of the airframe manufacturers. It makes virtually none of the components of its 777s. As a result, it is tremendously dependent on those who do.

To manage the interrelationship between stakeholders and organizations, both need to be measured independently. First make a list of all the stakeholders. Order them according to their relative importance. Then list each group's wants and needs. Customers may want "fast, right, cheap, and easy," while regulators may want "legal, fair, safe, and true."

Next, measure strategies and processes. Processes can be measured by the quality of the goods or services they produce and whether they satisfy the customers. You can also measure quantities such as volume, cycle time, cost, and so on.

The next step is to measure capabilities. These include skills, business practices, leading technologies, and physical infrastructure.

Finally, examine what the company wants and needs from the stakeholder. With a thorough understanding of this and the other elements, a company will be in a position to communicate its strategy clearly to all stakeholders, and to measure the implementation of the strategy and keep it on track.

Even the best measures are worthless unless the results are communicated. One utility company was tens of millions of dollars below its target revenue for the quarter, but the managers had no idea of the shortfall.

Once you have the right mix of measures, the company's incentive system must be linked to the outcomes. Be

sure to reward what the employee actually controls, so that he or she can adjust behaviors to meet outcomes. One way of doing that is to reward on the basis of team performance. This motivates employees to motivate each other.

While measurement may seem a mundane activity, it is a place where a great deal of creativity and innovation can apply. Knowing what to measure, when, and how is as much a part of the creative process as coming up with a new product. And without good measures, all the other efforts of innovation can fall short.

Targeting Innovation

As with knowing what to measure, determining which capabilities are most important is a creative act. There is no single path to the right answer.

For example, these four insurance companies rely on four very different mixes of capabilities:

- Unum Insurance differentiates in risk assessment.
- Progressive Insurance excels in claims processing.
- State Farm depends on its huge network of agents and offices.
- USAA specializes in customer service.

To get at the best mix of capabilities, begin by deciding what the company's core values are. One tool for doing that is the Innovation Targeting Matrix, in which you rank capabilities according to whether they are knowledge or transactional capabilities, and whether they are differentiating or support capabilities.

- *Transactional capabilities* are repetitive tasks that can be offloaded.
- *Knowledge capabilities* require human insight.
- *Support capabilities* are necessary, but do not form part of a company's competitive advantage.
- *Differentiating capabilities* set the company apart.

In addition, core capabilities are critical to the business, but not necessarily differentiating. By placing capabilities on a matrix with core capabilities in the center and the other characteristics on the sides, you can get a picture of where your company's strategy should go.

Among the insurance firms, Progressive excels at claims processing, which would be placed on the knowledge side of the matrix and closer to the differentiating edge than the support edge.

On the other hand, Unum excels at risk assessment, so for that company, claims processing would go more toward the transactional and support sides of the matrix.

As a way of initiating change, you can begin moving capabilities around on the matrix to see what the perfect model for your company is. Try doing the illogical thing and switching capabilities from their seemingly natural position to something counterintuitive.

Once those capabilities are outlined and you have the business model that fits, concentrate on improving the overall operation. This entails more than just looking for places to cut costs or reduce cycle times. Here are four areas to consider:

1. *Targeting*. Target innovation to those capabilities that differentiate your company. Put resources where they do the most good.
2. *Extending*. For those capabilities that are already performing well, constantly improve. Are there ways to make their high performance spread to other areas of the company?
3. *Outsourcing*. If a capability is in the support category, consider outsourcing it. Perhaps someone else can turn it into a differentiating capability in ways that you haven't considered.
4. *Improving*. No capability should be ignored. Every one of them can always be improved or extended. Always consider whether a capability might be taken out into the marketplace.

When you launch any change effort, the bottom line is that it must make sense. One utility began an effort to save $26 million, but told its employees that no changes in technology, organization, or compensation could be made. Predictably, it failed.

In addition, not all change can be revolutionary, yet sticking solely to incremental change results in missed opportunities. With a carefully

managed and balanced program of change aimed at innovation, you can become the leader in your industry.

Getting There

A company that rarely innovates cannot make the transition to 24/7 innovation overnight. You might begin by putting someone in charge of one operation as an experiment in change. As it pays off, people will begin to catch on, and the company will turn into a hybrid of old and new styles. Gradually, functional and traditional powers will diminish.

Processes will evolve into capabilities, which will gradually become linked for performance. The company will gradually go through six stages:

1. Functionally Bound.
2. Process-Sensitive.
3. Process-Driven.
4. Process-Dominated.
5. Capability-Based.
6. Alliance-Based.

Let's take a look at each of the stages.

The *functionally bound organization* is aimed at getting things done rather than creating value. This is a silo type organization of isolated fiefdoms. The activities are typically high cost, and they don't add value.

The second stage is becoming *process-sensitive.* Functions are still dominant, but a champion emerges who puts a new emphasis on process. Several processes are identified for improvement, and a taste for innovation is developed. Cross-functional teams arise. Lines of communication between the silos emerge.

The *process-driven* organization is the next stage. Process design becomes paramount, but functions are still deeply rooted. Deeper skills begin to build within the functions. New performance measurement systems are put in place as employees are retrained for process competence.

When process drives competition, a company has become *process-dominated.* Those who bought into process ownership early have gradually taken charge, as the functions reconstitute themselves as centers of excellence. They're now in a supporting role of the process leaders. Lines of communication are open across all disciplines. Now, alignment of all the different capabilities becomes the challenge.

As this happens, the company moves toward becoming a *capability-based* organization. Well-designed capabilities are the new basis of competition. Technology, organizational structure, culture, and competencies all flow together with process, as the business becomes completely integrated for world-class performance.

The final stage is the *alliance-based* company. Such a firm applies targeting concepts rigorously to create the right mix of owned, allied, and outsourced capabilities, which are arrayed so that they can be measured, managed, aligned, and integrated. This is overseen by a single leader, unified by culture, and linked through a common IT system. Innovation becomes the norm in every part of the company. At that point, customer needs are continuously anticipated and satisfied.

Lever Brothers is a company that went through those stages. The company had a traditional functional approach and a silo structure, and it was bogging down in decisions, rigidity, and waste. A new leader immediately began setting up cross-functional teams to break barriers. By retraining 100 managers in total system effectiveness, the company saved $30 million in supply chain costs alone. It began, in other words, by changing the way people *thought* more than what they *did.*

In 1993, when the company experienced a number of product failures, Charles Strauss became the new CEO. He focused on customers, speed, flexibility, and empowering employees to act. Creating two major new units, he linked them through five core processes that cut across organizational boundaries. By the next year, costs were dropping.

By 1996, Lever Brothers was developing products that the market had said it wanted. Inventory planning, production scheduling, and materials planning were all capabilities affected in redesigning for innovation. This sparked improvement in customer service, optimal inventory levels, and lower supply chain costs.

Meanwhile, new measures were brought to bear with key performance indicators. Extensive training and education programs continued to change the culture as

cross-functional skills developed throughout and a team-based environment took over. In 1996, Lever Brothers had its most profitable year in history.

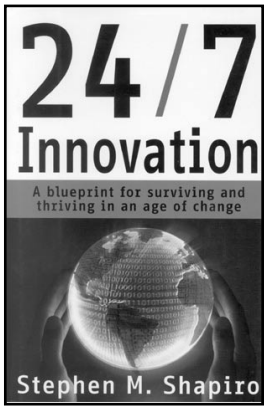
Innovation is not a one-time event. It's a way of life. While it must be systematically applied to different capabilities and processes in the company, it must also become a new way of looking at the world. With a commitment to innovation, a company can survive the daunting competitive environment that has developed.

Through pervasive innovation, and by constantly measuring both inside and outside the company, you can create a model for the future that will sustain your company. Only by changing the way everyone in your company thinks, and by making innovation a natural part of their everyday work, can you move your business to a state of 24/7 innovation — in which it is innovative hour after hour, and profitable year after year.

ABOUT THE AUTHOR

Stephen M. Shapiro is one of the founders of Accenture's Process Excellence practice and has consulted with global leaders from BMW WilliamsF1, ABB, and UPS to Lucent and Xerox.

He has worked with external thought leaders including Michael Hammer and Peter Keen and is recognized as one of today's most influential consultants in the area of process capabilities.



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