

The Thought Column with Robert Shelton, author and consultant



Robert is a co-author of the book, *Making Innovation Work* (2006). This book challenges the prevalent misconceptions about innovation and lays out the tools and processes necessary for an organization to harness and execute innovation. Robert is a Director and leader of the innovation practice at PRTM Management Consultants. He has served as Vice President at Arthur D. Little and as Managing Director at Stanford Research Institute's International's Worldwide Technology and Innovation Management practice.

Robert co-edited a three-volume book, *The Creative Enterprise* (2007) that integrates insights from the fields of management, economics, technology, psychology, and sociology and covers the spectrum across individual and organizational innovation. He has been a speaker on innovation and business strategy to a range of audiences in Asia, the US, and Europe. His work has received media attention from *The Wall Street Journal*, *Financial Times*, *CNN Financial News*, and *Tech Nation* (National Public Radio). Robert can be reached at rshelton@prtm.com.

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I want to focus our discussion on the push to increase the levels of service innovation within companies that have been historically product oriented. IBM and HP are examples of companies that realized significant growth by improving their ability to add services. However, for many companies, learning to innovate in the service space is proving harder than expected.

Innovation doesn't run itself

Through our work, we have been impressed by just how many companies have had significant problems in sustaining innovation. Companies and people in aggregate show a strong proclivity towards being innovative. It comes naturally. So we asked ourselves, why is it that companies are finding it so hard to maintain robust levels of innovation in order to support their business growth. We are not talking about just a few, weak companies; we're talking about a great many of the companies that are leaders in their industry. . . Coca Cola, GM and Sony are wrestling with this very dilemma today. IBM faced a near-death experience years ago. Procter & Gamble and Apple dealt with this innovation problem in the 1990s. These are companies with ferociously smart and capable management. Why do so many of them seem to struggle with sustained innovation? The problem of sustained innovation has many facets, but one essential learning is that sustaining innovation requires strong, effective management of the innovation elements. Innovation doesn't run itself.

Service Innovation is more complex and doesn't come easily

Service innovation is one of the areas of improved innovation management, which has recently been added to a space predominantly occupied by product innovation. In the product space, it became very clear that simply investing repeatedly in new technologies and improved product features, had diminishing returns. For years, companies have been pouring a lot of money into the product technology space, the net result being that every competitor is able to either anticipate the next new innovation or easily counter it if someone else gets there first. Companies that have traditionally been in the business of delivering products - hardware,

software, medical devices, consumer goods - are finding that there is a very important element of innovation which has been overlooked; that of providing services that increase the value for customers and complement the product offering. The problem has been that service innovation is a new area, so there is some important learning about how to innovate in the service space . . . learning what it is that customers and consumers really need and how to meet those needs with a combination of products and services. However, this combined product-service innovation does not come easily to many of these product-oriented companies.

The basics of innovation do not change between product innovation and service innovation. That is not the message. For both product and service innovation there is the technology vector and there is the business model vector. However, services rely more heavily on business model innovation. Historically, companies have not balanced their investment approach to business model innovation and technology innovation. Innovation has focused almost exclusively in the development of technologies -- for the products or for the process of manufacturing them. As a result, this is where their capabilities lie. This is where the innovation tools are in place and where they have the wherewithal and the management focus to make innovation investments.

If you are a product company, it makes sense to say, "We need to also supply services." Then you can launch an Internet support site, as in the case of Intuit, in order to better support its tax preparation products. Alternatively, you can provide consulting and implementation services that complement your products, as IBM has done. It is worthwhile to consider innovating in these areas, but it is not always easy. Service innovation focuses on changing the business model and leveraging technologies. Managing the business model, however, is often handled in a different part of the organization than technology. Therefore, one of the first impediments that product companies bump up against is the bifurcation or split management of innovation between the technology side of the house and their business model side of the house.

Service innovation requires the unification of technology and business model innovation.

Leading companies have begun to realize that you cannot manage innovation in this split manner. It needs to be unified so that there is collaboration and synergy between your technology innovation and your business model innovation investments. Let me point to some examples, and while the list isn't complete, it will give you a good feel for the unification trend. Recently the Volkswagen CEO, Winterkorn, took responsibility not only for the brand positioning and overall business logic of VW, but also for its R&D. This was an unusual move - to see someone in the auto industry step into control of both sides of the house. In the electronics industry, we have Steve Jobs, who sits right on top of both sides. HP has a similar approach. At Sony, in an attempt to resolve some of their recent problems, the CEO, Howard Stringer, has taken over responsibility for both the technology and business models. These companies are realizing that they need to make investments that are coordinated between technology and business model innovation, and that this can't be accomplished via emails sent across the organization or through periodic strategy meetings. The organization itself has to have an innovation center of gravity - a node where both technology and business model innovation can be managed, where the portfolio can be properly balanced, and good decisions about investments can be made.

Service innovation depends on a greater understanding of your company's value proposition.

To innovate in services, you encounter the customer and listen intensely as they talk about their experience. What they are talking about has a lot to do with their perception of the value that they are receiving, and it usually has to do with a range of things that are much broader than the product itself.

When you are shifting your business model from one of being product centric to being product plus service, it forces you as a company to clarify your value proposition with the consumer.

Until now, companies have been unprepared for this shift. In the past, product features and benefits have been explicitly defined and the consumer has extrapolated the value. Now, companies have to come up with a new level of value clarity.

Consider the digital home in which a multitude of companies are playing. There are content providers, content distributors, device companies, service companies, and others. The question is: what value is any given company going to provide? Will they provide just one small piece or are they going to team up with others, as Apple and Microsoft have done with content providers. What value are they going to offer when they start to add services to the products that people are using?

Without services, companies are leaving potential revenues and profits on the table

When customers buy a digital camera, what is the experience that they are looking for? People are not just taking pictures. People take pictures for a host of reasons. Some want to share them . . . some want to memorialize an event with them . . . some want to modify them and use them on a computer screen or to print things. Understanding the values of the user and the experience they want is essential to designing the correct product and service combination.

Flickr™ moved right into picture sharing services because none of the camera makers saw it as a relevant space or business model. The camera companies saw themselves as limited to producing a product, and missed the point that the consumer was after a broader experience than only taking the picture. Therefore, since the product companies didn't offer that part of the experience, a service company moved in. There was no reason, however, that the camera companies could not have provided the service.

The combination of iPod and iTunes has demonstrated that product and a complementary service are a powerful combination. After Apple introduced iTunes services, their sales escalated significantly, and have grown to that 70-plus percent market share which they have since held.

Companies often lack the tools for clarifying value

Companies often lack the tools for effectively listening to customers in a way that will help uncover opportunities beyond the narrow product offering.

The key for doing this is to encounter the customer in a meaningful way. Whether it's a retrospective review of purchase patterns, an ethnographic assessment, or using a virtual world with an avatar - these all allow an intense encounter with the users, and that's what sparks insight and creativity. Recently, I have been seeing a more sophisticated portfolio of these tools in use by product and service companies.

Service innovation requires fresh thinking on partnerships and collaboration

All innovation requires partnership and collaboration. Innovation is a team sport. When it is done successfully, it is done in groups. Partnerships and networking for product innovation have been around for a long time. Companies that make products know how to partner with other companies that make components or that provide a channel into the market. However, service innovation requires new types of partnerships and fresh thinking. Think about Apple. They had to reach into the ecosystem of the music world, all the way back to the content providers and the music labels that own these huge stores of songs, and strike an agreement with them.

If you are a product company, services require that you look freshly and more broadly at potential partners. Earlier, I referenced digital cameras and the fact that there are service opportunities around processing the pictures, sharing them, and presenting them in different ways. The camera company that traditionally creates high optics and picture capture technologies would need to partner with companies that are in a different space and have to do with electronic file transfer, storage and the like. Such partnerships can be difficult, because they

are with companies that have operating styles and business models that are unfamiliar to the product companies. However, companies can overcome those differences by tailoring the partnerships to fit the partners and the situation. Innovators need to develop a set of tools that allow them to develop partnerships that range from the traditional vendor relationship to strategic partnerships built on sharing risks and intellectual property. One size does not fit all -- especially when it comes to combined product and service innovations.

An important lesson for companies to learn is that when companies form partnerships, they need to move quickly. You cannot take five years to negotiate a deal that requires working through large masses of lawyers and contract specialists.

Open innovation helps to keep the focus on the customer and helps to avoid company-centric thinking

There has been much talk about open innovation, which I think is great. Companies need to realize that there are billions of IQ points available for use outside of their organization, both for idea generation and innovation, as well as for bringing products and services to market. Reaching outside the organization and forming partnerships is critical. The more that you become invested in developing something yourself, the more likely you are to be pulled into company-centric thinking. If you define the solution by the capabilities that you have in your organization today or even tomorrow, you end up undershooting the value proposition. I believe that open innovation or partnering, frees you from being trapped in your own way of thinking. There is not a company in existence today that has everything necessary to meet a truly robust consumer value proposition. How do you know when you are successful with your partnerships? When you become recognized as the company with whom everyone wants to work. So, good ideas flow naturally to you.

How you innovate determines what you innovate

There is another very important lesson to learn. In product and service innovation, how you innovate determines what you innovate. Said differently, how you put the pieces of innovation together . . . the partners with whom you're involved . . . the ideation approaches . . . the ways of understanding the customer experience . . . how high you set your goals . . . the leadership involved . . . the people . . . the metrics and motivators that you use for your team. All of these have a profound effect on the level of innovation that you are going to achieve.

If you want breakthrough innovations that help redefine an industry and give longer lasting competitive advantage and growth, then you need to design a system that will give you just that. That is why, in part, companies like Apple develop different answers than do companies like Sony. Apple came at this with a fresher approach to managing innovation. They put together different leadership, resources, partners and innovation processes, and came up with an entirely different answer than did Sony.

Innovation is a path function, not a state function. How you manage the process of innovation determines what types of innovation you will deliver.

INNOVATE is a management consulting firm specializing in new-to-the-company innovation, game-changing growth and breakthrough approaches. INNOVATE publishes *The Innovators* ezine and hosts **Innovate Speaks**, a speaker referral service. For further information visit our website www.innovate1st.com or contact Jaymie Berger, Jaymie@innovate1st.com, or +1.732.564.9145