



CUSTOMER MANUFACTURING GROUP

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YOUR CUSTOMER AND INNOVATION: SOURCE AND TARGET

Recent surveys by IBM Corporation, The Council on Competitiveness, and BusinessWeek-Boston Consulting Group produced important findings on U.S. industry innovation and competitiveness and the drivers which fuel our need to stay ahead of the game. There were also some surprising reflections on the roles we assign our customers.

In our white papers dealing with innovation we usually present some of our philosophy and recommendations based on our many years of both operating management and consulting experience in a wide variety of industries and environments. In these we hope to provide the reader with a perhaps different perspective than that typically found in academically-based texts and how-to publications, many based on seemingly good theory.

In this paper, however, we take a different tack and will present some highlights — and a few comments, of course — of the findings of a highly creditable study and two significant surveys of industry executives that covered their real-world experiences in developing and sustaining innovative companies. From these investigations we've selected those elements that were most closely related to either customer/market-oriented considerations or organizational issues. That is, we have excluded issues such as technology considerations, globalization and economics, private and government research funding, politics, and so forth.

We've tried to make our coverage of this research to be of interest to you in becoming the benchmark of innovation in your industry for your customers. We've provided the full attribution and Website references to facilitate your own more in-depth reading of these studies.¹

Customer and Market Oriented Innovation Issues

From this first study we've selected those items specifically related to customer and market-facing concerns.

IBM Global CEO Study, 2004.
Conducted by IBM's Strategy and Change Practice and the IBM Institute for Business Value, with *The Economist* and Nikkei Research.
Available at: http://www-1.ibm.com/services/us/bcs/html/2004_global_ceo_study_gen.html

1. More than 50% [of the CEOs surveyed] predicted greater customization of products by specific customer segments, with most CEOs focusing *on significantly increasing customer input on the development of new and better products.*

¹ We added italics in order to highlight the most significant findings for our purposes here.

2. To achieve their revenue objectives, 90% of CEOs expect their enterprise to *become more responsive, particularly to customer demand*, within the next five years.

3. More than 60% of the CEOs indicated they need to *do a better job capturing and understanding customer information rapidly* in order to make swift business decisions.

.1 These same CEOs highlighted several potential roadblocks, such as *not being agile enough to identify and chase new market opportunities*.

.2 Almost 60% pointed to the ability to *respond to customer dynamics in time*.

In this survey, the CEO-respondents replied in the context of what their companies needed to do and the challenges they faced, and not necessarily what they themselves would take personal or at least primary responsibility for addressing. Eighty percent of these CEOs stated that their primary attention had become focused on growth and investment opportunities. We suspect that in executing this responsibility in the prevailing environment of mergers and acquisitions and assuaging the relentless demands of Wall Street, many of these captains-at-the-helm have scarce little time to personally consider customer-centric issues. We have addressed this issue in a white paper, "Life After The Merger: Making The Union Work For Your Customers," available at: <http://www.customermfg.com/free/busmgmt.shtml>.

In the following survey, the CEO wasn't allowed the "luxury" of delegation, in that innovation direction and leadership responsibility was placed predominantly in this person's lap. This doesn't mean that the CEO was exclusively assigned the responsibility of being the chief person in charge of customer information, but it does imply that customer knowledge is part of innovation research, development and execution for which the "Big Kahuna" is responsible.

"The Enemies of Innovation," BusinessWeek-BCG Survey in BusinessWeek, April 24, 2006, 68. Available at: http://www.businessweek.com/magazine/content/06_17/b3981401.htm?campaign_id=search

1. When asked to identify "who is the biggest force driving innovation at your company?" the CEO was the top vote getter at 44.5 percent, the head of sales/marketing was a distant fourth at 7.8 percent but at least fared better than the 'VP of Innovation' at 3 percent (third from last).

2. With specific regard to customer and market related issues that have been hindering their companies' innovative progress, the survey respondents identified eight major constraints. "Limited customer insight" ranked fourth (descending) on the list with 25 percent of the respondents

indicating this as the major problem, and "Marketing or Communication Failure" was in the eighth position at 18 percent.

Although 'innovation' was the focus of this survey, this finding comes only somewhat as a surprise and is inexcusable. Quality manufacturers have been talking to their customers forever, and although the pressure to innovate hasn't been as intense as it has now become, it has always been present. Innovation isn't just about new or better products or product-services; it is about everything that has a customer touch point, physically, mentally, visually, that is, in every customer-facing way imaginable.

Some companies — such as 3M, GE, IBM, and P&G who have been around for quite a while, and Southwest Airlines, Starbucks, Apple, Google, and Dell who are newer entries — have always been proponents of talking with their customers. Talking here connotes a two-way exchange of ideas and information, and in the context of innovation, it means finding out what the customer would like to buy, both now and down the road a bit, and not spending a lot of conversation time trying to sell what you already have. In CMG parlance, we call this finding your customer's *What* — what your customer would like to buy from you that is not available from someone else.

It also means asking where your customer is going with their development plans so that you can help them achieve their future goals. We take it a step further; depending on where our clients are in the supply chain, we tell them to find out where their customers' customers are going and what's happening in that industry, two or three degrees of freedom removed.

Our point here is, with regard to this particular survey finding, if you have "limited customer insight," and "marketing or communications failure" at all, what exactly has your marketing department been doing all this time? Blame it on the IT department? Baloney! IT can provide the right tool for the job if Marketing can identify and describe what it needs to know about its customers and their industry(ies). The entire concept of 'CRM' wasn't created to enable a company to collect historic bean harvest sales data faster; it came about from the need to know what the fields were, where they were located, and what to plant, when. This isn't data, it is information and knowledge. If your company doesn't know this stuff, you don't first need new hardware and software; you have some primary organizational and infrastructure issues to resolve.

3. In response to "What percentage of your innovation-related resources are devoted to the following activities," the results were as follows:

- "Improving existing products/services" 31.4%

- "New products/services for existing customers " 28.6%
- "New products/services for new customers" 21.2%
- "Reducing product/service cost" 21.2%

These are some interesting figures and we invite the reader to compare them with the first finding from the "IBM Global CEO Study" cited above, in which the executives' emphasis was on the "development of new and better products." In short, the BusinessWeek-BCG Survey placed emphasis on existing products/services (although "new" wasn't far behind) while the IBM Study did emphasize new ones. Maybe the difference here is a semantics or segmentation issue, but we all know there is a world of difference between the type and degree of resources required for new innovation versus improving the existing product set. In addition, neither survey appeared to make any distinction between 'breakthrough' versus 'distinctive' versus 'incremental' innovation. Again, another huge differential.

Typically, Marketing is great with coming up with the "New and Improved" version of a product, all by themselves, and it will say so right on the packaging. An entirely different and unique solution to a customer's problem, however, starts with the customer; they may not know how to solve it, but they can do a fine job of describing the situation they're dealing with or will be. Just ask them; it may be risky, but to not ask may be fatal.

Internal Environmental and Market Innovation Characteristics

The objective and main focus of this next survey was to identify and highlight the critical need for federal funding for research and development in order for America to remain at the forefront of product innovation in the face of foreign competition. We believe the majority of our readership will be less concerned with the issue of federal funding than they will with how to remain innovatively competitive in general, regardless of the source of funds.

With this premise in mind, we have selected a few of the survey findings that we believe will have the broadest appeal to our readers. However, we do not deny the intent and importance of the National Innovation Survey in total and encourage the reader to peruse the text to review those items of individual significance.

2005 National Innovation Survey. Innovate America: Thriving in a World of Challenge and Change. 2005, 2005 Council on Competitiveness and New Economy Strategies LLC. Available at <http://www.innovateamerica.org>.

Survey Respondents: 199 senior business executives [Chairman, President, CEO, VP] from U.S. companies with \$68 billion in annual sales volume, and an actual average sales volume of \$345 million.

<p>1. Survey respondents were asked to identify the most crucial elements that must be present for the successful development of their companies' innovation programs over the next three years. Twelve such elements were identified, with the top five in descending priority:</p> <ul style="list-style-type: none"> o Scientists and engineers talent pool o Supplier/customer relations o Availability of entrepreneurial managers o Communications infrastructure o Investor base <p>The top two were considered to be of almost equal significance and alone would command 35 percent of the executives' total innovation-related budgets; far and away the largest allocation and greater than the next three elements combined (availability of entrepreneurial managers, communications infrastructure, and investor base).</p> <p>2. <i>Innovation is not the principal driver of today's competitiveness.</i> When asked to rank the factors that are most important in competing for customer sales, <i>executives rank low price and quick delivery as the highest priorities.</i></p> <p>On a scale of 1 to 6, with 6 being most important, of the six competitive drivers given, low price rated the survey's highest average of 4.8, followed by quick</p>	<p>delivery at 4.4, followed by customer service, adapting products to customer needs, then innovation/new technology at 2.9, and finally high quality at 2.6.</p> <p>Let's look at this again: 'Adapting products to customer needs' was ranked fourth (of six keys to competitiveness) and was only of medium importance (a score of 3.0), and 'innovation/new technology' was next-to-last in importance. Apparently reducing the cost (does that mean making a 'cheap' product or making a good product less expensively?) and delivering it faster is substantially more important than producing a "better" product. There must be some market related identified keys to "value" that require more segmentation or drill-down than this particular survey addressed. Still, when you look at the macro summary of the survey participants, this is a very powerful representation of American industry, and the results are more than a little disturbing to us.</p> <p>The survey results seem to be startlingly low rankings for both customer requirements (and all that a company needs to do to acquire this knowledge) and innovation, particularly so-called 'breakthrough' technology. Even more surprising is that these evaluations would surface in a survey essentially designed to influence and convince the</p>	<p>Federal Government of the need for vastly increased federal funding for research and development.</p> <p>Finding out what the customer really wants, might need in a time horizon you can act on, really values, and is willing to pay a commensurate price for are all part of Marketing's responsibility. It's tough work, particularly if your company is pushing the innovative envelope; there's no one else's product to reverse engineer and no one else's mistakes to avoid. So, if you want to stay out of this arena, the automatic default is to become a "me too" company and now the main thing left to even try to be "market competitive" with is price, followed closely by delivery and service.</p> <p>Once you've given up the one thing that will have the most significant and longest lasting competitive impact — <i>innovative value</i> — you're in a dog fight, with everything changing almost daily; price, promotion, place, and all the other alphabet so-called market criteria. Of these, price is a one-way elevator, and you are on your way down. Although it may not have been this way in fact, the National Innovation Survey results seemed to be heavily biased toward product commoditization, that is, making and selling the same thing that everyone one else is that everyone is buying , or at least the average common</p>
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denominator customer. Mass merchandising, or merchandising for the masses, as in ". . . any color you want as long as it is black."

It seems to us there's something out of whack with the survey finding here. Perhaps the key phrase in this finding is "today's competitiveness." We would have liked to see the survey inquire about 'tomorrow's' competitiveness. Perhaps the results for this one would have made us feel more hopeful.

- 3. Survey respondents more frequently *characterize their innovative activities as product modifications or line extensions rather than new product introductions.*

When asked what types of improved and new products, processes or services their companies had developed in the last three years, 82 percent of the executives indicated that their most frequent activity was modifications and extensions to existing products, 65 percent stated entirely new product development was their most frequent activity, 14 percent engaged most frequently in copying competitor's products, and some 7 percent declared some other type of primary activity.

These figures certainly confound the issue of priority significance between incremental versus breakthrough innovation, and also cloud the applied definition of what "innovation" really means. We don't know if the survey provided a definition of "innovation" in order to standardize the responses.

- 4. Business executives cite *internal barriers to innovation as the key challenge, with competing management priorities due to finite resources as the most frequently cited barrier.*

The executives reported that internal factors were at least as important, if not more so, than external ones as barriers or constraints to their companies' abilities to innovate. In addition to the key barrier cited above (61 percent claimed this as the key challenge), short-term emphasis in the marketplace occupied the third-ranked position (at 43%), and lack of time to encourage innovation was tied for fourth (at 32%).

One of the items we found interesting was "inadequate internal knowledge sharing" (listed 7th, descending, out of 17 items at 24%). We don't know if this was with regard to technical, product design and development skills, or the sharing of customer-based

information that could lead to new product development. In our experience, the former is more likely to be the primary case in large, multi-division and product line operations, while the latter is often a prevailing problem in companies of all sizes except for the very smallest of firms.

Not asking what the customer needs, for both now and possibly during the next 2 — 3-year period (or even farther down the road) is a common ailment regardless of the type of industry or the size of the company. And, as quite often happens, even when the question is asked and the answer is given, it is often not shared between the internal parties, i.e., marketing, sales, R&D, engineering, planning, etc. Somehow and for certain reasons (both intentional or due to poor internal system processes), this information is kept secret, if not downright sacred; secrecy that is a death knell to future growth and profits.

Your Customer and Innovation Every good story is comprised of three parts; a beginning, a middle, and an end. In the case of determining what innovative product/service, access, touch-point, process, communication, etc., your company is going to do next, all three parts of your story must have the same principal component; your customers.

"Innovation, almost by nature, has to be decentralized, ad hoc, autonomous, specific, and micro-economic. It had better start small, tentative, flexible. Indeed, the opportunities for innovation are found, on the whole, only way down and close to events." [to which we would add, 'close to the customer']
Peter F. Drucker, *Innovation and Entrepreneurship*, Harper Business, 1993, p. 255.

Your customer is your source, your reason, and your target for all your innovative endeavors. There is an exception to this three-part analogy however; there is no end, no conclusion. The story is on-going and continuous. In today's environment you can't rest on your laurels as they fade and wilt too quickly. With rapid technological advances in practically every industry and accompanying compressed development time, the market landscape changes so quickly that it has become almost virtual; as soon as you launch and insert your next new thing into the marketplace, the background changes. An increasing number of companies can quote statistics such as " 50 percent of next year's revenue will be generated by products that weren't even on the drawing boards [or in the CAD system or the simulator] three years ago," or something like that. Ok, make it two years ago.

But this paper wasn't really about what we think (we just editorialized a bit); it was to provide you with some thoughtful insight provided by much larger research organizations who wanted to frame some aspects of the challenges of innovation that executives are increasingly being forced to face and resolve. In the U.S., innovation is the key to our industrial survival. One can spend a great deal of time debating what "innovation" is, and what types of innovation there are, and what your company must do to be innovative, but one thing is absolutely certain; you will either innovate or fade.

More Information About CMG

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Detailed information on our services and a number of Special Reports and cassette tapes and CDs are also available.

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