OVERVIEW:
THE IMPORTANCE OF INNOVATION AND ENTREPRENEURSHIP

CHAPTER OBJECTIVES

After studying this chapter, readers should be able to:

- describe the core meaning of innovation in organisations, including its elements, benefits and challenges
- describe what entrepreneurship is and what entrepreneurs do
- explain why and how innovation leads to business benefits, advantage and competitiveness in markets
- describe the fundamental differences between new-stream/exploratory activities, and mainstream/exploitative activities in organisations, and the possibility of tensions and synergies between these
- discuss the role of strategy, resources, measures of innovation, rewards/recognition for innovation, and innovative culture and behaviour, as part of a holistic approach
- explain the key role of leadership in stimulating innovation within organisations
- recognise that Australia has a relatively weak national innovation system compared to the world’s best, but that entrepreneurial activities can and do still thrive here
- connect the benefits of systematic innovation capability to overall organisational benefits and performance.
The critical ingredient is getting off your butt and doing something. It’s as simple as that. A lot of people have ideas, but there are few who decide to do something about them now. Not tomorrow. Not next week. But today. The true entrepreneur is a doer, not a dreamer.

—Nolan Bushnell, entrepreneur

INTRODUCTION: INNOVATION IN AN ORGANISATIONAL CONTEXT

Innovation, essentially meaning doing things that are new in order to create value, is an imperative for established organisations because in any competitive market ‘standing still is going backwards’ relative to competitors. Opportunities and threats to all organisations have never been greater, due to the accelerating pace of change that is occurring in every aspect of almost every industry. For entrepreneurial start-ups and smaller organisations, innovation is central to their progress and success. In this book, we will examine and describe the key success factors for making innovation work, which can be adapted to any organisational context, whether large or small, well-established or newly formed, seeking to make sustainable profits or to succeed in the not-for-profit sector.

Entrepreneurship involves creating value in markets, through doing things that are new, particularly in those markets, often while building the organisational resources needed to establish those activities. Start-ups—meaning new organisations grown from a zero base—are a particularly challenging form of entrepreneurial business, attempting to bring innovations to fruition while simultaneously building an organisation, often from scratch. Entrepreneurs often need to operate on many fronts at once, ranging from creating product or service designs, market testing them, finding and arranging financial resources, hiring and managing staff, facilitating production, distribution and services, managing client customer relationships, and a host of other things. Entrepreneurship is challenging and risky, but can be highly rewarding in many ways, as Mark Zuckerberg (founder of Facebook), Larry Page and Sergey Brin (founders of Google), and Richard Branson (founder of Virgin Group) would attest. Entrepreneurial activities that lead to innovations in organisations and society can be the most exciting thing that any of us ever do at work!

Innovation in context

Innovation and entrepreneurial activities are not usually ends in themselves, but are a means to an end, where that end is usually the creation of value and achievement of organisational or personal goals. Those goals are often financial, but especially in the case of social innovation,
might well be related to non-financial goals too. There is a context and purpose as to why people individually and collectively engage in these activities: namely doing new things. For example, imagine if Apple stopped innovating, and was offering the same phone to consumers for five years, while Samsung had gone forward with new features, benefits and more consumer value through lower prices on a continuing basis, or indeed imagine if Apple raced well ahead of Samsung on its features and designs. Market share would quickly change, and it would only take a short while for the laggard to lose their customers, and then their business. This is what happened to Nokia, which went from an industry-leading position to now being completely out of the industry. Or consider the battle for market share between Coles/Woolworths versus IGA versus Aldi, Bunnings versus Masters versus Mitre 10, ANZ versus Westpac versus Commonwealth versus NAB, Shell versus Caltex versus BP, and similar examples in many other sectors. These companies compete fiercely with each other for the customer’s attention and consumption, continuously trying to provide higher levels of value to the customer, through product, process, business model and any form of innovation. Planning and implementing effective innovation has become a key area for competitive advantage.

The battle between companies like Apple and Samsung in terms of innovation is basically for ‘product leadership’ and value (which can be considered in terms of benefits per unit price). This product innovation race, however, is not the case in other industries and sectors. Consider, for example, iron ore, liquefied natural gas (LNG) or gold, which are essentially commodity items, and substantially undifferentiated in terms of their product specification compared with consumer electronics. For commodity items, innovation is still critically important, but it mostly manifests as process innovation, aimed at increasing the effectiveness of the supply function of that commodity item, specifically to lower costs, improve delivery and service, and perhaps flexibility of supply.

Whether it’s producing or selling a highly differentiated product or service, or a commodity, the less innovative company will quickly lose its profitability and its market. Today innovation is a key battleground of competitiveness. Indeed it is not enough to be innovative, a business’s innovation needs to be occurring with at least the same effectiveness as competitors just to remain competitive with them.

This book aims to set out the field of innovation, and the related field of entrepreneurship, in terms of their importance, meaning, constituent elements in an organisational setting, and benefits. Entrepreneurship and innovation each require many elements and capabilities to be planned and implemented well in order to achieve favourable results. They involve managing change and taking risk, both of which are notoriously difficult to do in organisations, which are generally much better at avoiding change and especially risk, and conducting themselves in a ‘same old, same old’ manner.
Defining and describing innovation

The terms innovation and entrepreneurship can mean many things to different people (see also Chapter 8, where entrepreneurship is formally defined and explained). Innovation has been variously defined as:

- The commercial or industrial application of something new, a new product, process, or method of production, a new market or sources of supply, a new form of commercial business or financial organisation. (Schumpeter, 1983)

- Intersection of invention and insight, leading to the creation of social and economic value. (Council of Competitiveness, 2005, in BEA Briefing, 2009, p. 15)

- Innovation covers a wide range of activities to improve firm performance, including the implementation of a new or significantly improved product, service, distribution process, manufacturing process, marketing method, or organisational method. (European Commission, 2004, in BEA Briefing, 2009, p. 15)

- Innovation—the blend of invention, insight and entrepreneurship that launches growth industries, generates new value and creates high value jobs. (Business Council of New York State, 2006, in BEA Briefing, 2009, p. 15)

We will use a generally accepted interpretation of innovation, as follows:

- Innovation can mean new or enhanced products, services, processes, methods, or business models, in order to create value.

We note that this interpretation raises a number of questions about innovation, including how innovation is manifested in various organisations, who is involved in the process, and the benefits that accrue from innovation:

- The ‘what’ of innovation, from the definition immediately above, correctly signifies that virtually nothing that an organisation does is off limits in terms of innovation potential. Every aspect from how it is set up, structured, located and how it is positioned in its markets can be the subject of innovation, as well as the more usual aspects of new or improved products and services, process improvements, new technologies, revenue sources, marketing methods and business models.

- The ‘how’ of innovation is the subject of much of this book, where we will draw on research and case studies to document just what works for those who succeed with innovation, as opposed to those who have tried and failed, and even those who do not try. For the moment, a high-level view of how innovation works is that it must pervade almost every aspect of organisational life and systems if it is to become fully mature, including the important elements of strategic priorities, resources and processes, performance measures, rewards and recognition systems, and ultimately, the ‘people factor’ (that is, behaviour and culture).
When innovation is working well and delivering good business results, all these factors are contributing strongly.

- The ‘how much’ of innovation can be interpreted at two levels: first, how big are innovations to be, and second, how much innovation should an organisation undertake on aggregate. On an innovation’s size or scale, anything is possible, from small tweaks of products and processes, called incremental innovation, to large breakthrough innovations, termed as radical. How much innovation is best for an organisation will depend on the organisation and its strategic positioning as well as on industry dynamics. In a market such as consumer electronics where product life cycles are short and technology moves quickly, a heavy emphasis on innovation is required to keep up and hopefully move ahead of competitors. Apple and Samsung invest enormous amounts of money into innovation, and a substantial part of their workforce is devoted to developing next generation products and services, as well as producing, delivering and marketing the current product range. In other contexts, such as in some industries and government departments, innovation need not be as intensive and pervasive as in consumer electronics, because the forces at play, such as technologies and processes, are not moving as fast. An example is in producing commodity-like food products such as sugar and beef. In the sugar and beef industries, innovation is indeed alive and well, mostly in process innovations (because the products are relatively standard), but is not moving as furiously fast as it is in the mobile phones market.

- Who benefits from innovation? Innovation is the lifeblood of organisations, aimed at satisfying a number of stakeholders. Principal among these and most directly impacted by innovation are the organisation’s customers. When useful new features are incorporated into products and services, consumers benefit. When processes are improved through technical advances or business model innovation, such that costs are reduced, then customers or shareholders (or both) can benefit, depending on the extent to which the organisation banks the cost savings or passes them on as price reductions. When delivery performance (such as speed of responsiveness or reliability) is improved, typically through process innovation, then once again the benefits can be passed on to customers or perhaps price or volumes can be increased. Further, given that innovation is ultimately aimed at increasing the organisation’s value proposition to its consumers, and hence drives its profitability and effectiveness, then the organisation’s owners are key beneficiaries of innovation success. Innovation is a capability to be invested in, and for those who make such investment decisions, a return on investment is expected. No better example exists than Apple Inc., which has in recent times become the world’s most highly valued company by market capitalisation, even beyond resources giants such as Exxon Mobil and BHP Billiton. Apple has one key factor that has driven it to such heights, namely how well it has planned and executed its many innovations, from products (such as the iPod, iPhone, iPad and Macintosh), through to innovative services (iTunes, App Store and Apple retail shops).
A second key aspect of the ‘who’ of innovation is concerned with who does it. Innovation is not only the province of big, established, well-resourced companies. It is true that Procter & Gamble, Toyota, McDonald’s, Samsung, 3M, Apple, GlaxoSmithKline and many other large companies do survive and thrive based on their innovation. But within these giant businesses, innovation is actually done by people, individually and in teams. Further, innovation is not just the province of scientists and engineers, or marketers and executives, or only those people working in research and development departments; rather, in all organisations, innovation can and should be the province of all employees, and even other stakeholders such as suppliers and customers who can provide insightful ideas to help populate the innovation idea bank. Everyone can develop innovative ideas, and in the best of organisations, this happens to a powerful degree.

In any industry, which organisations can be expected to be most innovative? This is an exciting aspect of innovation, because now more than ever innovation is coming from younger, smaller ‘upstart’ people and organisations, often disrupting long-standing and well-resourced businesses. This is not a new phenomenon; for example, it was in the early 1980s that entrepreneurs Steve Jobs and Steven Wozniak started Apple at a time when the giant IBM dominated the computer industry. Now Apple is a key computer industry player, while IBM has exited that industry. However, more than ever there are many instances of start-up organisations going into niches, new industries and even challenging existing large companies through their innovations. These organisations can quickly scale up and reach global markets: just look at Facebook, Airbnb and Uber. Today innovation is the province of small and young companies, just as much as large and older companies. Indeed, start-ups in many ways find it easier to create and deploy an entrepreneurial culture, which is often stultified by the bureaucracy in larger or older rivals. A good example of this is the rivalry between McDonald’s and Subway. Almost being a victim of its stunning six decades of success (1940–2000), McDonald’s kept its offering largely the same for many years, having expanded globally to some 30,000 restaurant outlets and left positioning space for a start-up to enter the field with an innovative make-to-order, fresh baked, healthier offering. McDonald’s has subsequently renewed its offering as well as having embarked on a strong innovation capability renewal initiative, but for a while, many observers would have argued that Subway ‘stole McDonald’s lunch’ in terms of product leadership.

From the observations above, we can conclude that innovation is not a specialised or high-technology activity, but can be the province of all organisations, and everyone within them. It brings significant benefits, and threatens those who under-invest and underperform in innovation. In the twenty-first century, innovation is increasingly becoming a vital organisational capability.
CHAPTER 1: THE IMPORTANCE OF INNOVATION AND ENTREPRENEURSHIP

Invention is not innovation

Usually, in terms of getting innovations to a point where they create value for stakeholders, one starts with ideas, of new or significantly enhanced products or services or processes, business models or a combination of these. However, there is a difference between ideation (having ideas that are hopefully valuable) and full innovation, which is the most difficult and challenging to

Danny Samson and Marianne Gloet with Kathy Wilson

CASE STUDY

RITZ CARLTON: INNOVATION IN TOP-FLIGHT HOTELS

Ritz Carlton has been able to successfully implement a four-step innovation process, which is aimed at fully engaging employees’ creativity to craft service experiences that delight customers. The four steps are:
1. inspire vision
2. foster the right environment
3. stimulate ideas
4. test ideas.

The first two steps in Ritz Carlton’s approach are the responsibility of senior management and other leadership team members. These are aimed at ensuring that employees believe their ideas will be considered and valued (even if they are not all implemented) and that an environment that fosters innovation and ideas is created. Once the environment that fosters creativity has been shaped, managers then take steps to encourage the creation and development of those ideas. This is done by ensuring there is a well-diversified talent pool within the organisation that can be stimulated to study customer behaviour and ask thought-provoking questions. Ideas put forward are tested and evaluated, which can be done through company developed evaluation matrices or other decision tools. According to Timmerman (2009), through the implementation of this four-step process (developed by analysing the current body of knowledge from resources including Harvard Business Review and the American Society for Quality), ‘the Ritz Carlton was able to successfully implement this 4 step process, and can now leverage employee ideas effectively and efficiently, improving its ability to create exceptional experiences for its customers’.

For such new ideas, we have developed and described (see Chapter 4) the key ‘tests’ that can and should be applied to filter and screen the best ideas from the many that will not lead to value creation, and hence should be discarded.

Source: Timmerman, 2009

It’s not about ideas. It’s about making ideas happen.

—Scott Belsky, co-founder of Behance
get right. To challenge this thinking we begin with the controversial assertion that ‘Ideas are cheap’. Smart people are plentiful and smart people have lots of clever, potentially value-adding ideas. For example, people in universities, research institutes and think-tanks, as well as private inventors, come up with all sorts of weird and wonderful ideas. Does this on its own create value? Our answer is that only the potential for significant value is created in an idea, no matter how good it is. Ideas can strictly have commercial value and they can be bought and sold, or licensed for use, but their value as an idea is usually only a small fraction of what can be created when the idea is scaled up and brought to life at high volume. When Sony invented the Walkman portable cassette player, relatively little value was created through that pure first act of invention, however, when Sony was able to produce and sell 22 million Walkman units at high margins, then millions more later in the life cycle, some billions of dollars of value to Sony was created. If Sony had not been capable of scaling up the production and successfully marketing and selling this product at high volumes, would real value have been created just through the act of invention?

Following the success of Sony’s Walkman, consider the compact disc that was invented by James Russell in 1965. Russell claimed intellectual property ownership of the compact disc through patenting it. The compact disc was first co-developed, then commercialised and launched into retail markets by Philips in 1980, and then along came Sony, with its background and reputation in Walkman portable sound reproduction players, manufacturing and quality systems, and its global brand, marketing and distribution expertise. Which of these entities—the inventor, the commercial pioneer or the ultimate mass-market commercialiser—received most of the value created through this radical new way of recording and playing back music and data? All three parties benefited from this successful invention, but while it was still just an invention, the benefits were small, and even when Philips further developed and launched it, the benefits were growing but not near full potential. Sony brought to this invention the marketing expertise, the Sony ‘Discman’ brand, the product quality assurance, and the manufacturing and distribution supply chain, which led to billions of dollars in value, and rightly, Sony appropriated much of the value, even though Sony was not the inventor or even the primary product developer.

**Individual innovations versus a portfolio of innovations**

Later in this book we will provide an outline of how to test and decide whether an idea or invention has potential commercial value as an innovation (see Chapter 4). Here we discuss how to manage not just single individual ideas and innovations, but to assemble a valuable portfolio of ideas into a development pipeline. These can include new offerings to the market, cost-reducing process enhancements, and changes to business structure or even a complete new business model. Business model innovation includes changes to the way a business is
set up and operates. Such innovations can be completely novel, as when Dell computers set up a ‘make to order’ system that allowed for customisation and a more efficient ‘pull’ supply chain than entrenched ‘make to forecast’ business models that ‘pushed’ product to markets. Amit and Zott (2012) suggest that business models can be innovated by adding new activities, such as through forward or backward integration, linking activities in new and different ways, or changing who conducts such business activities. They suggest that business model innovation can be stimulated by questions such as:

- How can new business model activities address new customer needs?
- What new activities will best serve these needs?
- How can such activities be linked in new value-adding ways?
- Who should conduct these activities and how should they be governed?
- What revenue models are possible?
- How will all stakeholders achieve a value creation increase?

While these questions are generic and do not give immediate leads or answers, they are a good starting point. Consider how companies such as Airbnb and Uber have created new business models by rethinking consumer needs for accommodation and transport, respectively, then finding innovative ways to provide these services. The original establishment of Federal Express can be similarly considered, when a basic delivery need was reconceptualised and a solution found that was ‘outside the box’.

According to Nagji and Tuff (2012), the innovation portfolio is critical to innovation effectiveness. They use the term ‘total innovation’, which involves having a clear innovation ambition, then balancing the elements of innovation efforts going into core, adjacent and transformational activities. They argue that a mix of 70 per cent core, 20 per cent adjacent and 10 per cent transformational innovation resources is how high performers balance their efforts, but they also note that returns on innovation effort come from the opposite proportions, namely 10 per cent core, 20 per cent adjacent and 70 per cent transformational. Nagji and Tuff point out that these proportions can and should vary between industry, competitive position and stage of development of the company. They also acknowledge that different skills and metrics are required for different categories of innovation. For example, core innovation and even adjacent innovation requires close analytical attention (that is, tightly managing the tests of an innovative idea; outlined in Chapter 4), whereas transformational innovation might require a more qualitative and imaginative approach, including people from multiple disciplines bringing disparate views to the innovation process (for a good example of transformational innovation, see the Diggerworks case study later in this book). Non-traditional innovative metrics might be useful in the transformational aspects of innovation; for example, Nagji and Tuff (2009) point out that for Google, the only performance metric and goal of transformational innovation is that the company learns from it!
A caution has been issued by Gottfredsen and Aspinall (2005). In their article about innovation versus complexity, they point out that we must be careful in our innovation efforts to not overdo the complexity of an organisation’s tasks. For example, the Mars Corporation pet food division, known as Uncle Ben’s and later Mars Petcare, found that its innovation efforts in Australia led to it having an overly complex product range, of several hundred stock keeping units (SKUs), making manufacturing difficult and less than optimally efficient. Federal Express also faced issues with complexity and innovation. Federal Express was successful with its original supply chain design for moving parcels all over the USA because of the simplicity of its model: moving all parcels overnight through Memphis, Tennessee. The company came to grief when it applied this model to Europe because of the complexity that country border customs brought to its operations. This caused Federal Express to withdraw from Europe at great cost. It returned once cross-border European integration had advanced so that fast, clear and efficient overnight delivery now works with simplicity and speed.

Entrepreneurs do innovation, and more ...

Having defined, illustrated and exemplified innovation in principle, let us now turn our attention to entrepreneurs: who are they and what do they do? To begin with, it is clear that entrepreneurs do things that are innovative; they do not just imitate existing products, services, processes and business models. Entrepreneurs find new ways to create value for stakeholders, and hopefully aim to profit from those activities. A key characteristic that differentiates many entrepreneurs from innovators within mature, established companies is that entrepreneurs are often also developing new businesses at the same time as they develop new products and services. This is the case particularly for start-ups, which by definition involves a business being created, from nothing, in order to promulgate and commercialise a new idea into a valuable innovation. The risks for entrepreneurs are often higher than for mature businesses, because mature businesses have a mainstream of operations in which they generate the cash flow for their innovation investments. If the ideas they try to commercialise fail during any period, they still have their mainstream base and they can try to innovate again in the next business cycle.

In contrast, entrepreneurs do not have a mainstream funding source for the new-stream they are trying to build, and they often fail at the first hurdle because they have built a business around one single product or service. Entrepreneurs in start-ups often have little choice but to ‘put all their eggs in one basket’ when they are first starting up. They need courage, determination and single-mindedness, as well as large amounts of business acumen.

We hear about successful entrepreneurs such as Richard Branson and Steve Jobs, but we hear much less about the many entrepreneurs who tried and failed, often more than once, and hence did not become famous. We also hear about large mature businesses, yet many of these began as entrepreneurial ventures, such as those started by Henry Ford, Kiichiro Toyoda, Éleuthère Irénée du Pont, Alfred Bernhard Nobel and a host of others.
Entrepreneurs often attempt radical innovation, trying to disrupt whole markets, but this is highly risky. Kogan (see the Ruslan Kogan case study in this book) is an example of a business that is disrupting retailing in Australia from electronics to grocery markets. Michael Treacy (2004) has pointed out the high risks of radical innovation, compared to the slow and steady path of multiple incremental innovations. Treacy argues that sometimes a radical innovation takes a company too far out front of the market, leading to too much market risk, and possibly also involving significant technical risk. We would argue that ultimately a portfolio approach should be taken, where the best set of innovations from a risk and return perspective are taken into consideration. Of course, working on incremental innovations does not preclude searching for and implementing radical innovations, and vice versa. Entrepreneurial start-ups may not have much choice other than to concentrate on only a small number of innovations, and be over-exposed to a single innovation. This is in contrast to large mature businesses such as the giant Procter & Gamble, which manages a balanced innovation portfolio based on the risk and return of innovations, individually and on aggregate.

If you’re not a risk taker, you should get the hell out of business.

—Ray Kroc, founder of McDonald’s

We should not underestimate the challenges that entrepreneurs, especially first-time start-up entrepreneurs, face when they try to build innovative ideas into businesses. Most fail. They have to create a legal structure and entity, set up systems of everything from accounting to human resources, raise and manage money and create a budget for their expenditure, make choices about technology, research the market and study their potential competitors, decide how they will manage their intellectual property, plan and execute the production and marketing of their offerings, and manage the expectations of a number of stakeholder groups, all while trying to progress their innovation through the development funnel. While most struggle to succeed in all these areas, and ultimately the statistics show that most do not commercially succeed, those who do make it, such as Steve Jobs, Bill Gates, Richard Branson and Mark Zuckerberg, make entrepreneurship a very attractive path to aspire to. In a later chapter of this book, we describe and discuss entrepreneurship in the context of both start-ups and within existing businesses in much more detail (see Chapter 8).

Innovation and competitive markets

There are many ways in which an organisation can compete, such as through superior performance in terms of cost, quality, delivery (speed or precision), flexibility or innovativeness. All these elements are possible means of creating competitive advantage. However, a single competitive advantage can be a fleeting thing, and almost never lasts for more than a few years, with some rare exceptions of companies that have been able to succeed through a single competitive strategy for decades.