Forrester Consulting

MAKING LEADERS SUCCESSFUL EVERY DAY

April 13, 2007

Business Managers Don't View Innovation As Strategic

Companies' innovation efforts are inwardly focused and seek operational efficiencies — not top-line growth

The following is a commissioned study conducted by Forrester Consulting on behalf of Microsoft.

FORRESTER®

Headquarters
Forrester Research, Inc., 400 Technology Square, Cambridge, MA 02139 USA
Tel: +1 617/613-6000 • Fax: +1 617/613-5000 • www.forrester.com

Table Of Contents

Executive Summary

Microsoft commissioned Forrester to conduct a custom study that examines how companies are investing in IT and human capital to improve customer relationships. On behalf of Microsoft, Forrester Consulting undertook a Web-based survey of 630 business process owners and business managers and a phone survey of 205 senior IT decision-makers in November 2006 and February and March 2007. We selected survey respondents that were responsible for managing customer relationships, establishing and/or managing partnerships, managing innovation, improving operational efficiency, contributing to strategic planning, recommending or evaluating technology investments, managing a team of information workers, or specifying the types of training employees receive. Nearly a quarter of the people we surveyed (23%) had responsibility for managing innovation.

Despite all the media hype about innovation, we found in this study that only 41% of business respondents ranked innovation as the first or second area of strategic importance for their organizations, compared with customer relationships (75%) or operational excellence (52%). That doesn’t mean these managers don’t value innovation at all — actually none of the business managers surveyed said they don’t — but rather that they assign higher value only to innovations that positively impact customer experience (75%) and increase operational effectiveness (73%).

The survey data shows that companies are well advanced in the deployment of techniques, tools, and business processes that help drive innovation, with an impressive 60% running formal idea management programs to source innovative ideas from across their enterprises. While companies seem to reward good ideas — sourced either internally or externally — that lead to business success, they don’t tolerate bad ideas that generate failure. Indeed, 55% of interviewees believe that their risk-averse corporate culture doesn’t tolerate failure associated with “innovations gone bad”. Yet, that hasn’t stopped nearly half (49%) of companies in 2006 from ranking innovation capability as their first or second largest area of technology spending in 2006. Among the 130 big spenders who ranked innovation as their top investment, the most popular tool deployed to foster innovation isn’t a sophisticated functional one like portfolio management (32%) or mind-mapping (29%) but plain vanilla collaboration software like employee portals, which are used by more than half of the firms to support innovation.

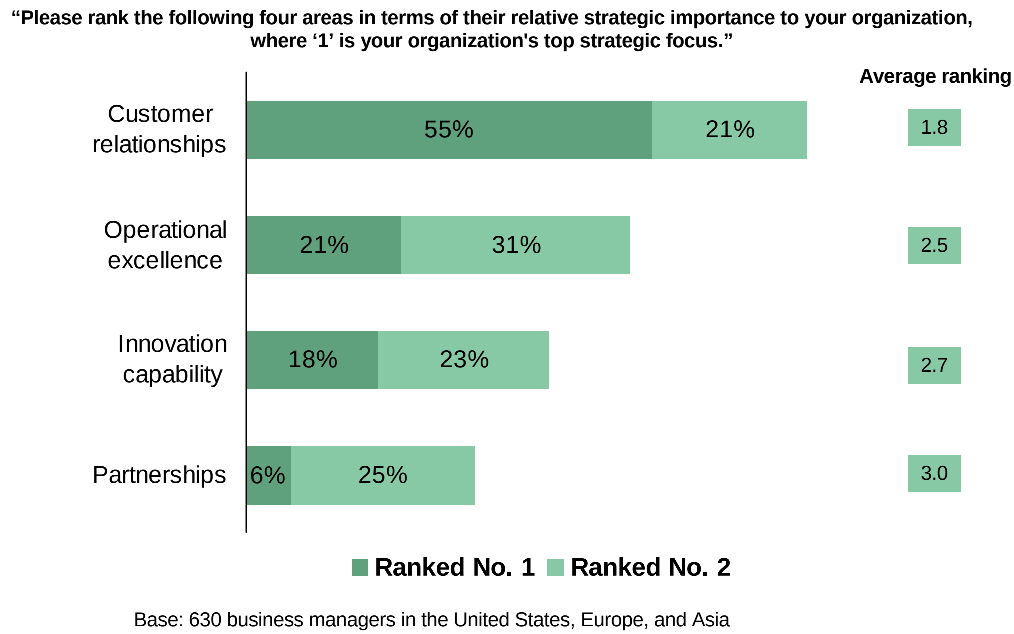
It’s also worth noting that 34% of the managers spending heavily on innovation believe that supply chain management software also enables innovation — re-emphasizing the importance they place on operational innovation. This obsession with operational efficiency becomes even more evident when the respondents were asked to list the key benefits that could result from improved ability to innovate: cost reduction tops their list (50%) — even more than improved customer experience (45%) or top-line growth (41%). In other words, if the managers with whom we spoke could invest more in innovation, they would rather direct that money to invent new processes that streamline cost structure rather than use that funding to create new products or services that delight customers or building new businesses! But companies don’t seem to realize that innovation, unlike operational efficiency, is a human-mediated activity — which explains why only 47% of companies ranked innovation capability as their No. 1 or No. 2 area of human capital investments in 2006.

Most Firms Innovate To Reduce Cost — Not To Drive Top-Line Growth

Judging by the proliferation of cover stories on creativity and innovation in leading business publications, and the numerous conferences and award programs dedicated to the innovation theme, one might come to believe that innovation tops firms' growth agendas as they face growing customer demand for new products and services. Many CEOs have gone on the record stating that their firms' organic growth strategy is squarely centered on driving high-performance innovation. Yet recent research conducted by Forrester Consulting on behalf of Microsoft seems to indicate a disconnect between the C-suite's high-level strategic aspirations around innovation and the operational reality.

Despite all the media hype about innovation, we found in this study that only 41% of business managers ranked innovation as the first or second area of strategic importance for their organizations, compared with customer relationships (76) or operational excellence (52%) (see Figure 1). Clearly, while CEOs talk the talk about innovation, business execs in their organizations don't seem to walk the walk by building up their firms' innovation capacity.

Figure 1 Innovation Capability Lags Behind Customers And Operations As A Strategic Focus



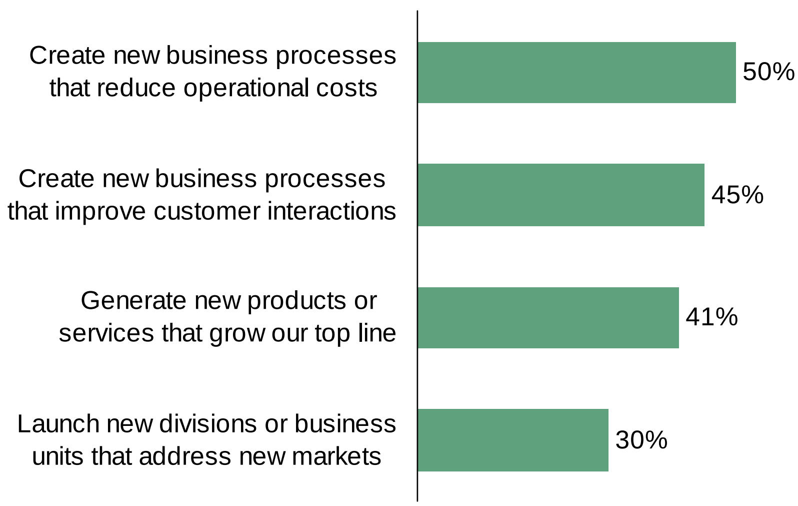
Source: Forrester Consulting online survey commissioned by Microsoft in November 2006, February and March 2007

That doesn't mean these managers don't value innovation at all — actually *none* of the business execs surveyed put themselves in that category — but rather they assign higher value only to innovations that positively impact customer experience (75%) and increase operational effectiveness (73%), two areas considered as strategic for business success. While this attitude is mostly consistent across all regions we surveyed, specifically with regard to the high value placed to customer-experience-enhancing innovations, the mean score for European respondents was only 3.91, with 5 being "strongly agree" and 1 being "strongly disagree," whereas it was higher in both Asia (4.13) and the US (4.29). Firms' obsession with operational efficiency becomes even more evident when respondents were asked to list the key benefits that could result from improved ability to innovate: Cost reduction tops their list (50%) — even more than improved customer experience (45%) or top-line growth (41%) (see Figure 2).

Forrester found that the biggest regional variation among the business managers and business process owners we interviewed was in the amount of innovation outsourcing they undertake. While just 8% of US respondents acknowledged that their organizations outsource some or all of the R&D and/or product development activities, that percentage was nearly twice as high among European respondents (14%) and almost three times higher among Asian interviewees (22%). This would indicate that Asian companies, and to some extent European firms, are more actively forging external innovation partnerships than US firms. This trend may be counterintuitive for the reader, as Asian corporations seem to outsource R&D even if they view innovation as relatively more strategic than their European and US counterparts. The only explanation that can reconcile this paradox is that Asian firms view R&D outsourcing as *a critical element* of their overall innovation strategy. They consider external innovation partnerships as strategic.[1]

Figure 2 Business Managers See Innovation As A Means Of Cost Reduction

"If your company's ability to innovate increased, what would be the result? Please select all that apply."



Base: 630 business managers in the United States, Europe, and Asia

Source: Forrester Consulting online survey commissioned by Microsoft in November 2006, February and March 2007

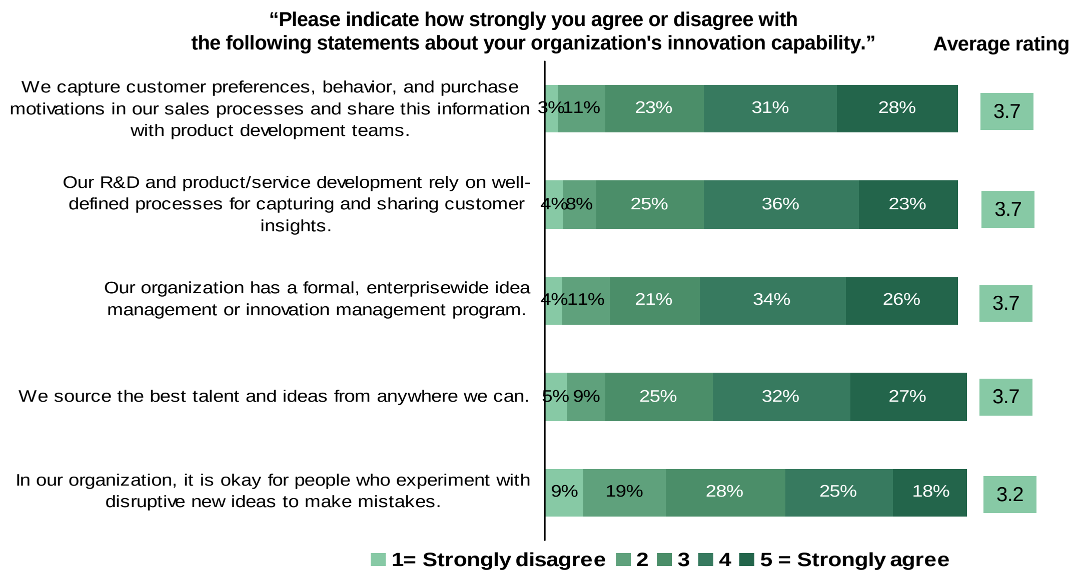
The second biggest regional variation in survey responses centered on key benefits managers expect from improved innovation capacity. If they could invest more in innovation, Asian respondents indicate that unlike US and European managers, they won't direct *all* that money into inventing new processes that streamline cost structure, but use some of that additional funding to create new products or services that delight customers or even build entire new businesses. Indeed, a whopping 50% of Asian respondents state that their company would be able to generate more top-line-growing new products if their company's ability to innovate were to improve, compared to 36% for US and European respondents. And 38% of Asian managers believe that increased innovation capacity would allow them to launch entire new divisions that address new markets – compared to 25% and 28% for US and European respondents.

All other things being equal, this survey data indicates that, compared with US executives and with, to some extent, European executives, Asian managers are taking a broader and more strategic view of innovation. They also boast a higher appreciation for innovation's top-line contribution.

Firms' IT And Human Capital Investments Reflect Their Tactical Innovation Focus

The survey data shows that companies are well advanced in the deployment of techniques, tools, and business processes that help drive innovation — with an impressive 60% running formal idea management programs to source innovative ideas from across their enterprise. They are also collecting ideas from customers, either via well-defined R&D and marketing processes (59%) or by mining sales data (59%) (see Figure 3). On a regional basis, European managers' responses indicate that European companies are slightly behind their US and Asian counterparts in the deployment of formal innovation management techniques and processes. For instance, when asked whether they have well-defined processes to capture and share customer sales and preference data with R&D, the mean score for European respondents was only 3.41, with 5 meaning "strongly agree" and 1 meaning "strongly disagree," whereas it was higher in both Asia (3.88) and the US (3.81).

Figure 3 Business Managers Report Advanced Approaches To Driving Innovation



Base: 630 business managers in the United States, Europe, and Asia

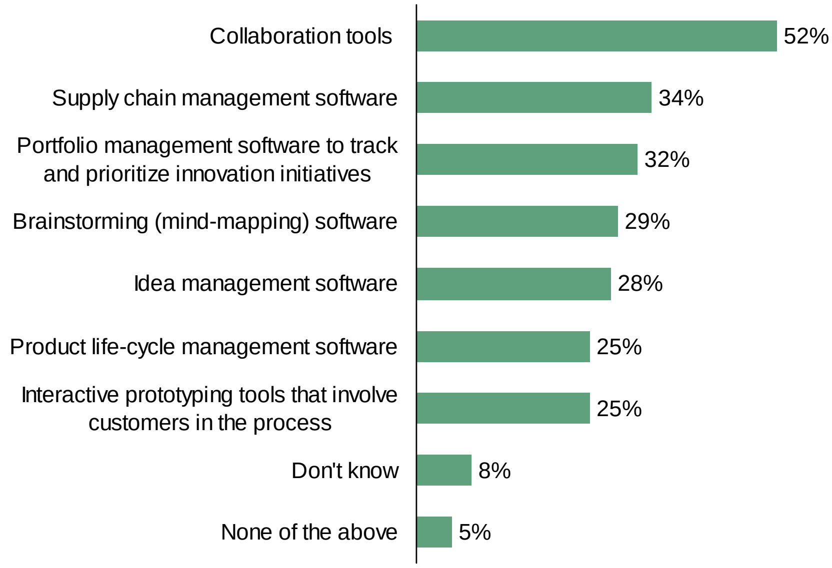
Source: Forrester Consulting online survey commissioned by Microsoft in November 2006, February and March 2007

While companies seem to reward good ideas that lead to business success, they don't tolerate bad ideas that generate failure. Indeed, 56% of interviewees believe that their risk-averse corporate culture doesn't tolerate failure associated with "innovations gone bad".[2] Yet that hasn't stopped nearly half (49%) of companies in 2006 from ranking innovation capability as their first or second largest area of technology spending in 2006.

Among the 130 big spenders who ranked innovation as their top investment, the most popular tool deployed to foster innovation isn't a sophisticated functional one like portfolio management (32%) or brainstorming (29%) but basic collaboration software like employee portals, which are used by more than half of the firms to support innovation (see Figure 4). The latter isn't necessarily a positive thing: The low emphasis placed by business managers on partnership management indicates that these collaboration tools are mainly used to generate innovation *within* the four walls of the corporation and not to engage partners like suppliers or distributors in innovative projects.

Figure 4 Cutting-Edge Innovation Tools Lag Behind Among Big Innovation Investors

"Which of the following technologies is your organization currently using to support innovation? Please select all that apply."



Base: 130 business managers in the United States, Europe, and Asia who rated innovation as their top technology investment
(multiple responses accepted)

Source: Forrester Consulting online survey commissioned by Microsoft in November 2006, February and March 2007

It's also worth noting that 34% of the managers spending heavily on innovation invest in supply chain management software to enable innovation — re-emphasizing the importance they place on operational innovation. But companies don't seem to realize that innovation, unlike operational efficiencies, is a human-mediated activity, which explains why only 47% of respondents ranked innovation capability as their No. 1 or No. 2 area of human capital investments in 2006.

Once again, Asian managers distinguish themselves from the pack by putting their money where their innovation is. The mean ranking for 2006 IT spending in innovation capability by Asian respondents was 2.19, whereas it was 2.66 in US and 2.76 in Europe, where "1" was the area of most spending. Similarly, the mean ranking for 2006 human capital investments in innovation capability by Asian managers was 2.26, whereas it was 2.57 in Europe and 2.66 in the US, where "1" was the area of most spending.

Conclusions

From this study of organizations' perception of innovation, the maturity of their innovation management processes, and their IT and human capital investments in support of innovation capability, Forrester Consulting found that:

- All respondents across regions do value innovation, but only as so far as it improves their operational effectiveness and enhances their existing customer relationships. Consequently, their risk-averse, tactical innovation initiatives focus on explicit customer needs and cost efficiencies — thus possibly sacrificing a growth orientation.

- Companies are well advanced in the deployment of techniques, tools, and business processes that help drive innovation, although European firms lag slightly behind their US and Asian counterparts.

- Firms' IT investments aimed at boosting innovation capability are limited to basic collaboration software and efficiency-seeking tools. More worrisome: Companies didn't make enough human capital investments in 2006 to support innovation, which is essentially a human-mediated activity.

- Compared with US, and to some extent, European executives, Asian managers take a broader and more strategic view of innovation, which they view as a collaborative process that needs to be extended to external partners. Asian respondents also boast a higher appreciation for innovation's top-line contribution. As a result, their innovation management processes are more mature and they make bigger investments in IT and human capital to further strengthen their innovation capacity.

Appendix: Supplemental Material

Related Forrester Research

Innovation Management

June 14, 2006, Trends “Innovation Networks: Global Progress Report 2006”

January 26, 2006, Quick Take “The CEO’s Five New Year’s Resolutions To Drive Innovation-Led Growth In 2006”

November 3, 2005, Best Practices “Make IT Matter For Business Innovation”

March 16, 2005, Forrester Big Idea “Consumer-Focused Innovation”

Forrester Methodology

In November 2006 and February and March 2007, Forrester Consulting conducted a research study on behalf of Microsoft to investigate the strategic importance, technology investments, and human capital investments in four areas: customer relationships, innovation capability, operational excellence, and partnerships. The project consisted of a Web-based survey of 630 business managers and business process owners in the US, Europe, and Asia. The business managers and business process owners we surveyed worked in more than 17 industries. The industries most frequently represented in this survey are public services, government, professional services, high-tech products manufacturing, industrial products manufacturing, and consumer products manufacturing. The majority (80%) of the people we surveyed work for organizations that have more than 1,000 employees, and all respondents worked for companies with more than 500 employees.

Endnotes

[1] Asian companies are among the first to abandon vertically integrated invention-to-innovation cycles in favor of far more productive ecosystems of specialized partners: Inventors, Transformers, Brokers, and Financiers. See the June 17, 2004, Forrester Big Idea “Innovation Networks.”

[2] When asked to rate their level of agreement or disagreement with the following statement: “In our organization, it is okay for people who experiment with disruptive new ideas to make mistakes,” 55% of respondents said 1, 2, or 3 (on a scale of 1 to 5, where 1 is strongly disagree and 5 is strongly agree).