SideBoard

Conversations that matter for non executive directors

Disrupt or be disrupted

Disruptive innovation and change have always been a constant in business. Today's challenge is the pace of change fuelled by technology, data and social connectivity. Dr. Soren Kaplan, a global expert in innovation, culture and disruptive change, recently shared his ideas on how boards can harness disruptive innovation to drive new business growth.

Q. What is disruptive innovation?

The classic definition of disruptive innovation is a technology that's introduced into the market that has lower cost and greater benefits or features. But the concept has become much broader. Now it's about business models, industries and even whole sectors, being disrupted by innovations brought about by rapid technological change.

Q. Why should non executive directors care?

Disruptive innovation should be on the radar of every board because it represents both an opportunity for growth and a threat to shareholder value. The world is moving faster, technology is moving faster and disruption is moving faster. The pace, scale and impact of disruptive innovation is greater than it's ever been. And any company, any business and any industry can potentially be subject to disruption.

Q. What's an example of a company that's suffered due to disruptive innovation?

In the 1990s, Kodak was a global brand and the market leader in film. Despite being aware of digital photography as early as the 1970s, they did not believe it would disrupt their market. When they could no longer ignore the threat, they decided to compete – not in digital cameras, but the low cost printing. However the rise a digital technologies, particularly smartphones, saw the market for film and photo printers plummet. Kodak declared bankruptcy in 2012. Their mistake was to ignore technology, wait too long to respond, and place a single big bet.

Q. What about the upside?

There are many upsides for both companies and industries. One is that innovative disruption can actually increase the size of a market; it can 'grow the pie'. For example, before Uber, the San Francisco taxi market was worth about $140 million per year. It's now worth more than $500 million per year as a result of this disruptive innovation. In New York, there has been a 400% increase in ride growth.

Q. What's the key to developing businesses geared towards disruptive innovation and growth?

Culture is absolutely critical. And in this regard, boards have a key role to play in setting the tone at the top. One of the most important strategies is to communicate that failure is OK. Organisations with a strong innovation culture know that failing, learning and innovation go hand in hand. People need to know that they will not be punished for having a go. There are a number of practical things Boards can do. An imperative is to ask management for an innovation strategy with clear KPIs.

Boards need to:

- *set the tone from the top*
- *find a way to balance risk with the need to experiment and innovate*
- *set KPIs that drive a culture of innovation*
- *ask "what is our innovation strategy?"*
- *promote stories of failure as a learning opportunity*
- *ensure the DNA of the CEO embodies an innovation mindset*

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The CEO is integral to challenging existing business models and leading an organisation through a disruptive innovation strategy. Boards need to ensure their CEO has the DNA required to tackle the challenge and opportunity disruption brings. Today's CEO needs to embody an outside in approach, they need to have an external view, be skilled at creating partnerships and building networks. Their risk tolerance level should be higher than yesterday's CEO, they need to encourage experimentation and communicate that failure is learning. The CEO isn't in this alone, building a diverse executive team that embodies the appetite for change will help the CEO create a culture fit for innovation.

Culture is critical. Failing, learning and innovation go hand in hand.

Q. What are the strategies for disruptive innovation?

There are four.

- **Innovate adjacencies** – look for opportunities in markets that are close to your core business. For example, Fuji, unlike Kodak, embraced digital photography and now has a $20 billion market capitalisation.
- **Disrupt using data** – with the amount of data collected each year growing exponentially, there are increasing opportunities to provide innovative services and products through the smart harnessing of online data.
- **Change the business model** – technology is just technology until it meets a business model.
- **Create a culture of innovation** – promote smart risk taking, experimentation, and re-frame failure as "learning".

Four strategies to innovate:
- *Innovate adjacencies*
- *Disrupt using data*
- *Change the business model*
- *Create a culture of innovation.*

Q. Not all innovations turn out to be winners. How do you manage the risks?

Boards have traditionally been risk averse. But in the current climate the most risky strategy is to do nothing. Organisations are unwilling to cannibalise their core business. But if you don't cannibalise it, someone else will and with it a large growth opportunity is lost. Boards need to find a way to balance risk management with the need to experiment and innovate. The best strategy is to take a portfolio, such as the 70:20:10 model. This means 70% of innovation should be of the incremental kind, such as continuous improvement in existing process and products. 20% should be for sustaining innovation, which means major advances in the core. And 10% should be committed to disruptive innovation, those things that could be complete game changers to the business and market. The 10% is the hardest to achieve but well worth the effort. To succeed the 10% needs to be driven outside of the core business, ensuring existing barriers do not limit innovation potential.

Dr. Soren Kaplan
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Q. What are the key questions boards should be asking themselves and management about disruptive innovation?

- Assess the impact and likelihood of disruption. This means asking 'Who and what could disrupt us from outside the industry?' Industries that are ripe for disruption typically hold dear to long-standing assumptions, apply a business model that hasn't changed in years and have a finite set of players.
- 'Do we have a balanced – that is 70:20:10 – innovation strategy?'
- A key question to ask is about culture: 'Do we have a capability for sustainable innovation?' It can be hard to innovate from within a business, but that doesn't mean you simply don't do it. There are many strategies, such as innovation hubs, partnerships or alliances that companies can adopt to capitalise on the growth opportunities innovative disruption presents.

Explore disruptive innovation by video

Dr. Soren Kaplan discussing Disruptive Innovation and the role of Directors
https://youtu.be/Kj56i1dDUZ0
Candid Camera Elevator – light hearted way to look at conformity
https://vimeo.com/61349466
Dollar Shave Club.com – example of new market entrant disrupting a long held business model
bit.ly/1Pv7EKM
Card trick – shows how when we are solely focused on one area, we are blinded to what's around us
bit.ly/1FgEqzl

For more information on issues relevant to Boards in Australia please contact our Chairman
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