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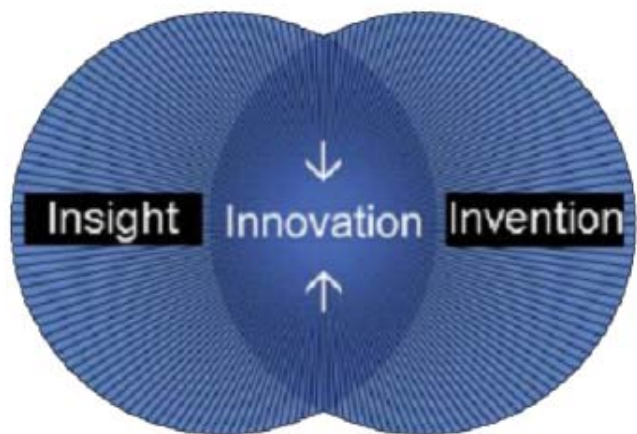
# **Canadian Competitiveness The Innovation Imperative and the Role of the CFO**

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## The Innovation Imperative and the Role of the CFO

FEI National Breakfast Seminar  
February 2008



*Do you really have to print this presentation?*

## Agenda

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- Achieving growth through innovation
- Innovation strategies
- What approach is right for your organization
- Your role as CFO

## On the mind of the CEO: Growth, change and innovation

**Growth and  
change are critical**

Above average growth doubles the odds of higher shareholder value<sup>1</sup>

**Conventional  
growth drivers  
aren't enough**

- Acquisitions often destroy value
- Incremental organic growth rarely creates differentiation
- Creating efficiencies are always necessary, but don't create sustainable advantage

**Innovation  
enables growth**

Best opportunity for sustainable growth

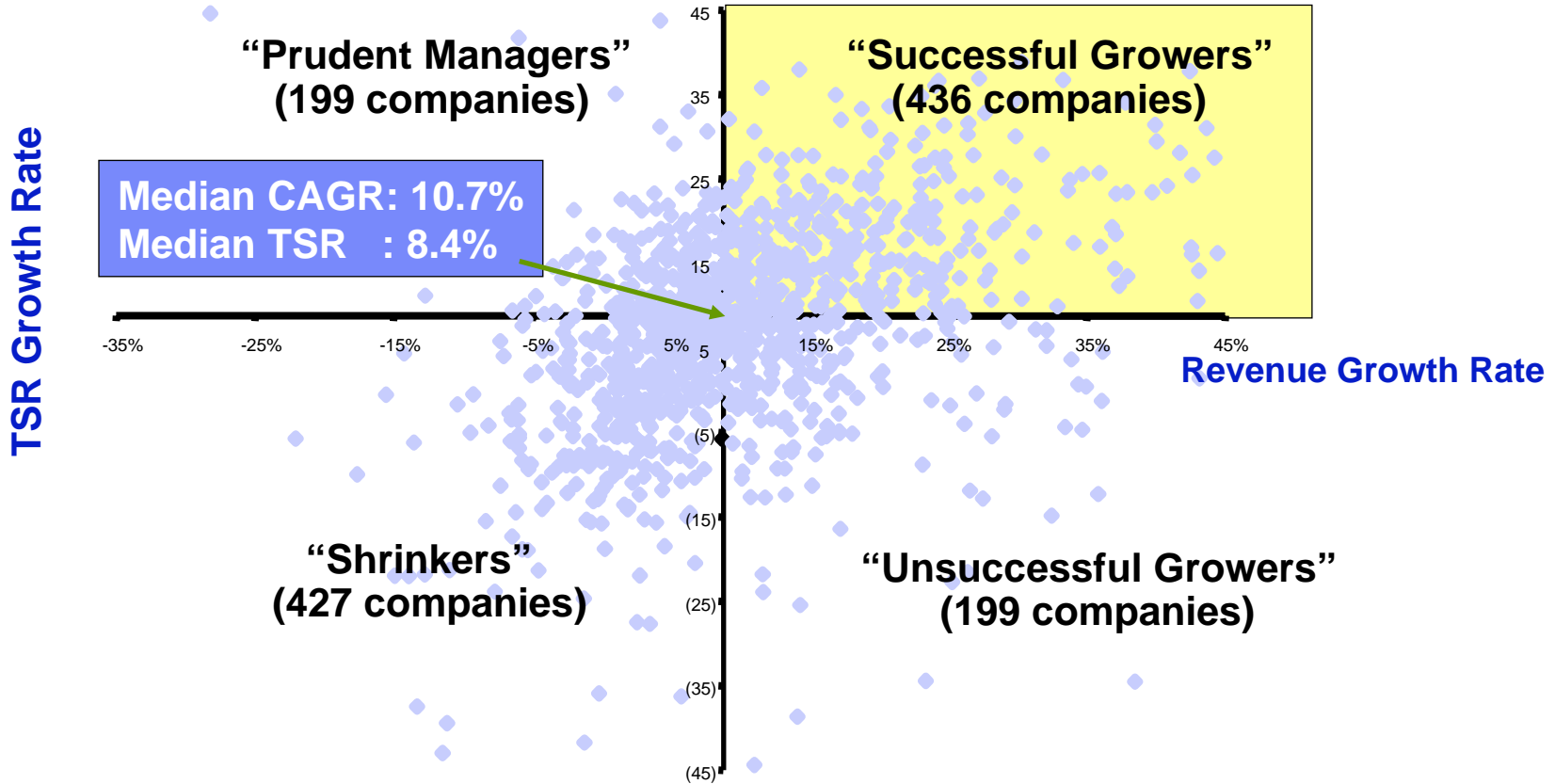
*"In the last ten years, the free movement of information, products and services has made putting up sustainable competitive advantages more difficult. Companies need to be quick and agile by identifying and acting on opportunities quickly."*

*–CFO, A Leading Supplier of Industrial Gases*

<sup>1</sup>Kapur, Vivek, "The Growth Triathlon," IBM Institute for Business Value

# Profitable Growth – Everyone wants it but few have it

**Revenue Growth & TSR For The S&P Global 1200  
(1995–2005)**



## Why not? Why don't we have profitable growth?

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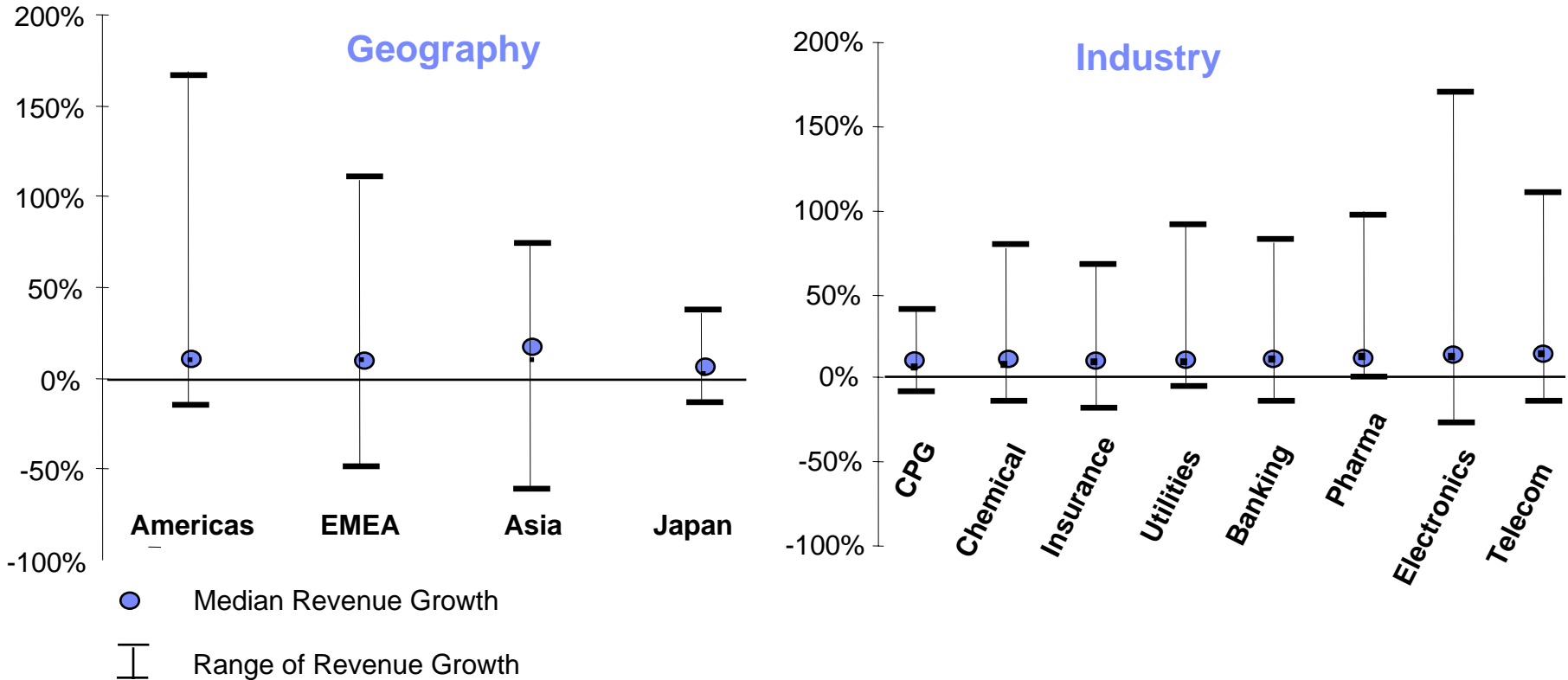
- Our neighborhood constrains us
- We are too large to grow fast
- Its risky
- We don't know how to

The "Beliefs"  
of Growth

The Disciplines  
of Growth and  
Innovation

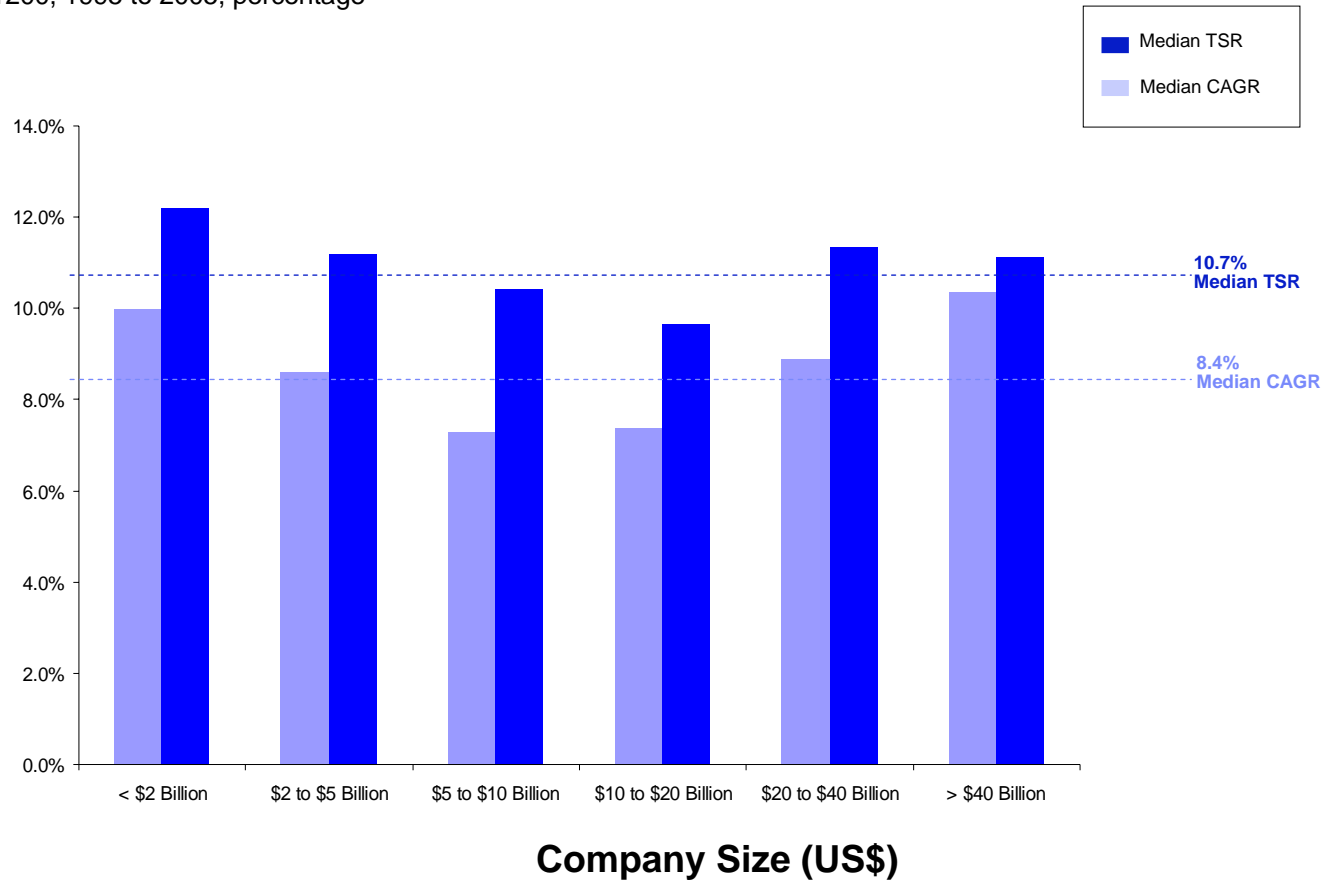
# Neighborhood is not destiny – While industry and geographic growth rates differ... strong performers outgrow their peers by wide margins in any neighborhood

**Revenue Growth : Median & Range**  
*S&P 1200 Companies Revenue Median & CAGR %, 1994–2003*



# Size is not the issue either - large companies can grow as well as small ones, if not faster

**Median Revenue Growth Rate and Annual TSR by Company Size**  
S&P 1200, 1995 to 2005, percentage



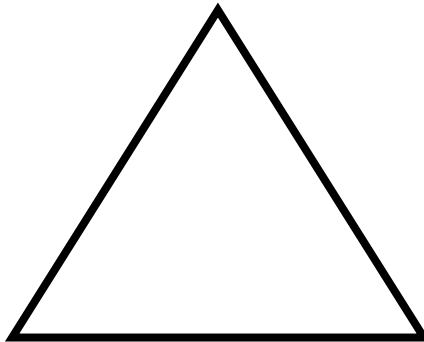
Note: Median CAGR is based on calculation of the median for each group of companies based on net 2004 revenue  
Source: IBM GBS analysis

# Successful Growers are Tri-athletes. They are strong not only on “Course”, but also on “Capability” and “Conviction”

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## Course

- The identification and selection of opportunities. Development of a winning model. Sustaining growth by creating sufficient initiatives and funding for them
- **Key questions: What’s the landscape? Where do I play? How do I win? How do I keep winning?**



## Capability

- The activities that support the operational model and allow the execution of the growth strategy
- **Key question: What do I need in order to win?**

## Conviction

- The creation of organizational belief, momentum and resilience in moving towards growth goals
- **Key question: How do I get going, stay moving, bounce back?**

## Successful Growers are Tri-athletes. They are strong not only on “Course”, but also on “Capability” and “Conviction”

### Course

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## CEOs told us . . .

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***“Competitors are emerging from everywhere”***

***“The market imposes innovation.”***

***“Our Business Model is drastically changing and innovation is very important for this. 40% of our business is over the internet.”***

***“Globalization, commoditization, higher cost structure, increasing specialization needs ... We must stay in front of the commoditization curve.”***

***“We must innovate to keep justifying their existence.”***

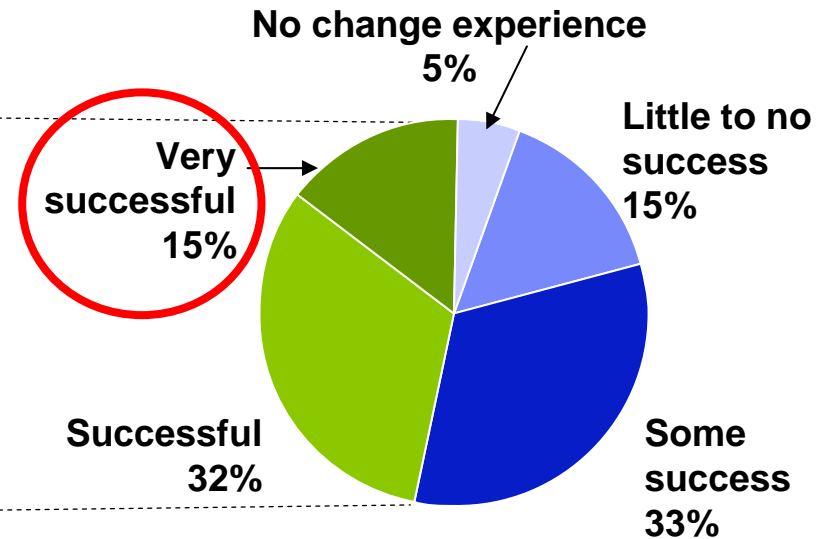
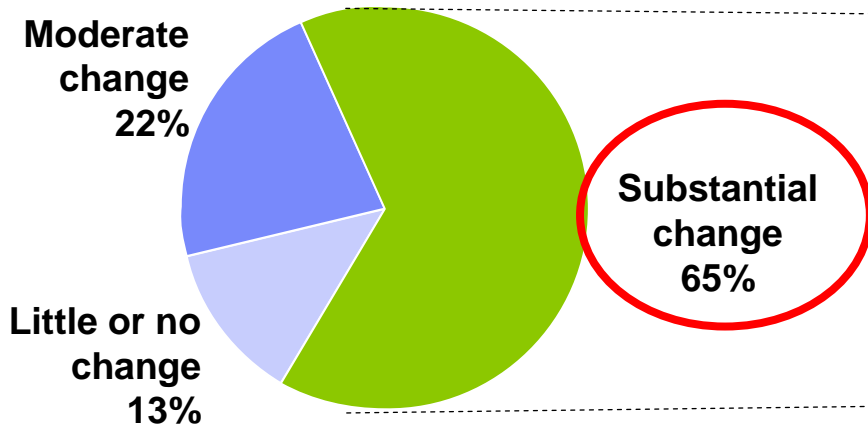
***“There is no growth without changing ourselves and the industry itself.”***

***“Last year’s products are last year’s dollars..”***

# CEOs indicated that fundamental change was required, but they seemed uncertain about their organization's ability to manage it

**Extent of Fundamental Change Needed Over the Next Two Years**

**Past Level of Success at Managing Fundamental Change**



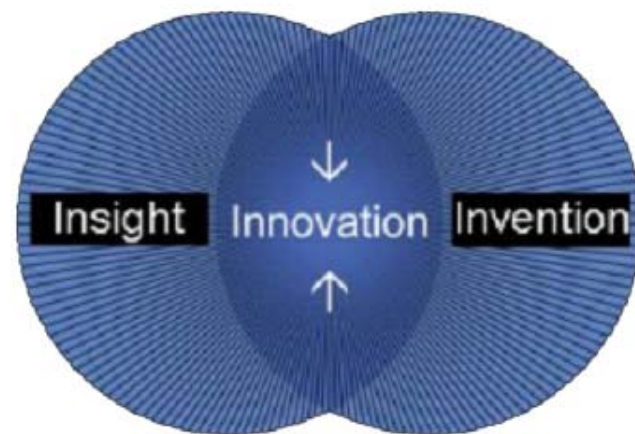
*Innovation was seen as being at the centre of the changes required of businesses*

Source: IBM CEO Study 2006

## Key Definitions

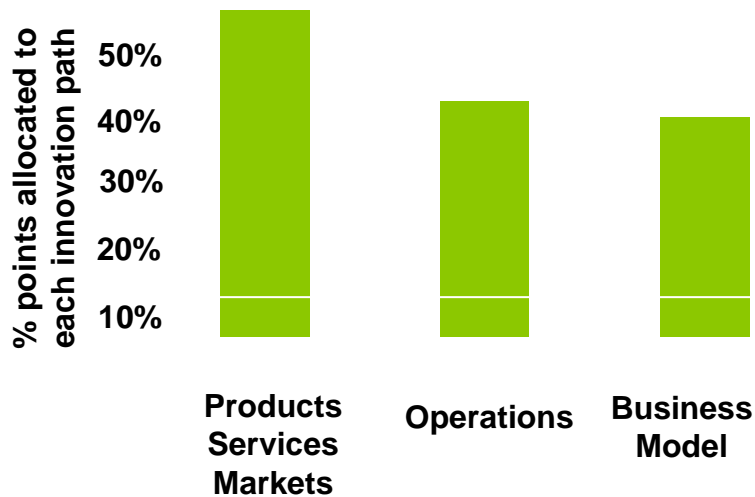
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- Innovation
  - Using new ideas or applying current thinking in fundamentally different ways that result in significant change
- Business Model Innovation
  - Significantly changing the structure and / or financial model of the business
- Operations Innovation
  - Improving the effectiveness and efficiency of core business processes and functions
- Product/Services/Markets Innovation
  - Creating new or significantly differentiated products, services or go-to-market activities

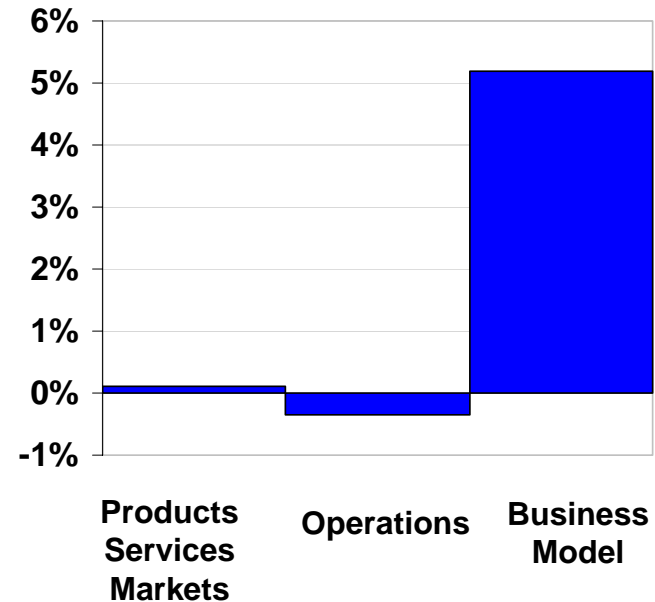


# Business model innovation gains prominence . . . And correlates strongly to an increase in operating margin relative to peers

### CEOs Innovation Focus

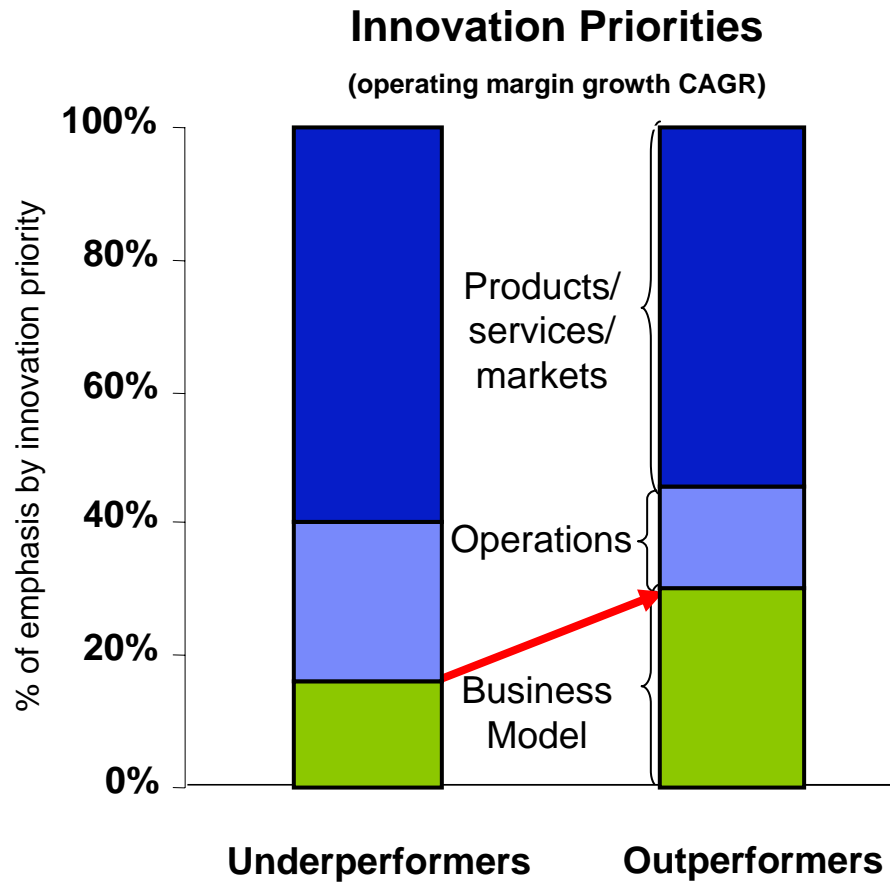


### Operating Margin Growth in Excess of Competitive Peers



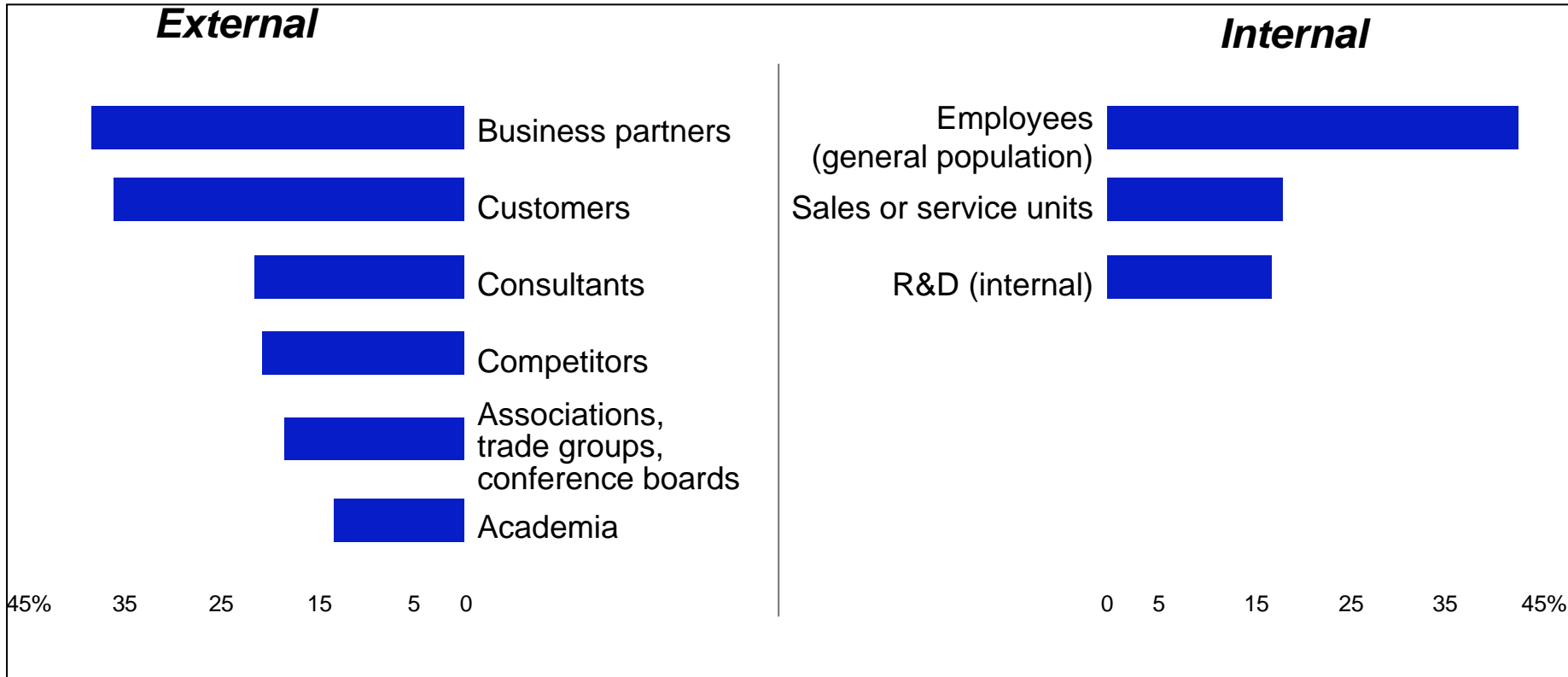
Source: IBM CEO Study 2006

... and outperformers are nearly twice as likely as underperformers to innovate their business model



Source: IBM CEO Study 2006

## Sources of New Ideas and Innovation – Collaboration has taken on new importance

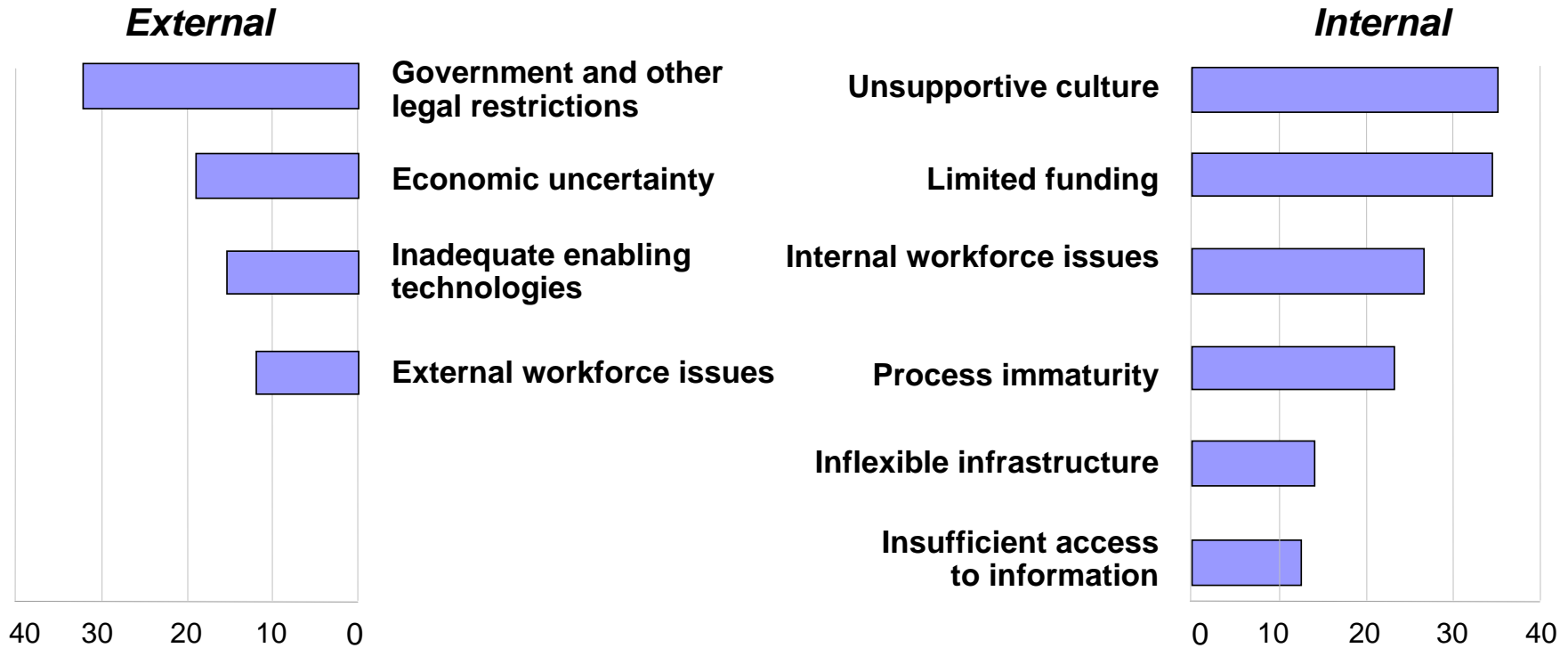


*“today we have a lot more capability and innovation in the competitive marketplace than we could try to create on our own.”*

Source: IBM CEO Study 2006

# CEOs also indicated a number of pervasive internal obstacles to innovation

## Obstacles to Innovation



*“Innovation starts when we break with and deny the status quo.”*

*“Innovation czar equals innovation ghetto.”*

Source: IBM CEO Study 2006

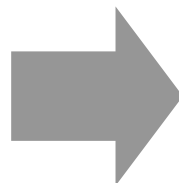
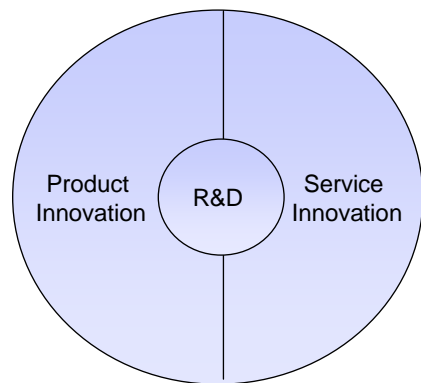
## Agenda

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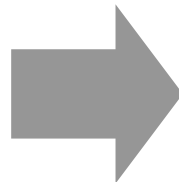
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# The innovation model has changed

## *Innovation – Historical*



## *Innovation – Going Forward*



- Focus on Product and Service Innovation
- Development and technology driven
- Central role of R&D function
- Closed and internal to enterprise
- Technology as a differentiator

- Broad innovation agenda, including business model
- Research and customer driven
- R&D as a process, key role of leadership & individuals
- Open and collaborative
- Technology and business integration as differentiator

## Putting this all together ... 8 new innovation rules to consider

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### Capitalizing on New Markets & Business Models

1. **Grab and monetize the Long Tail of demand**
2. **Get ready - Your customers value digital content**
3. **Jump in - Virtual worlds are real business**

### Getting Closer to Your Markets & Customers

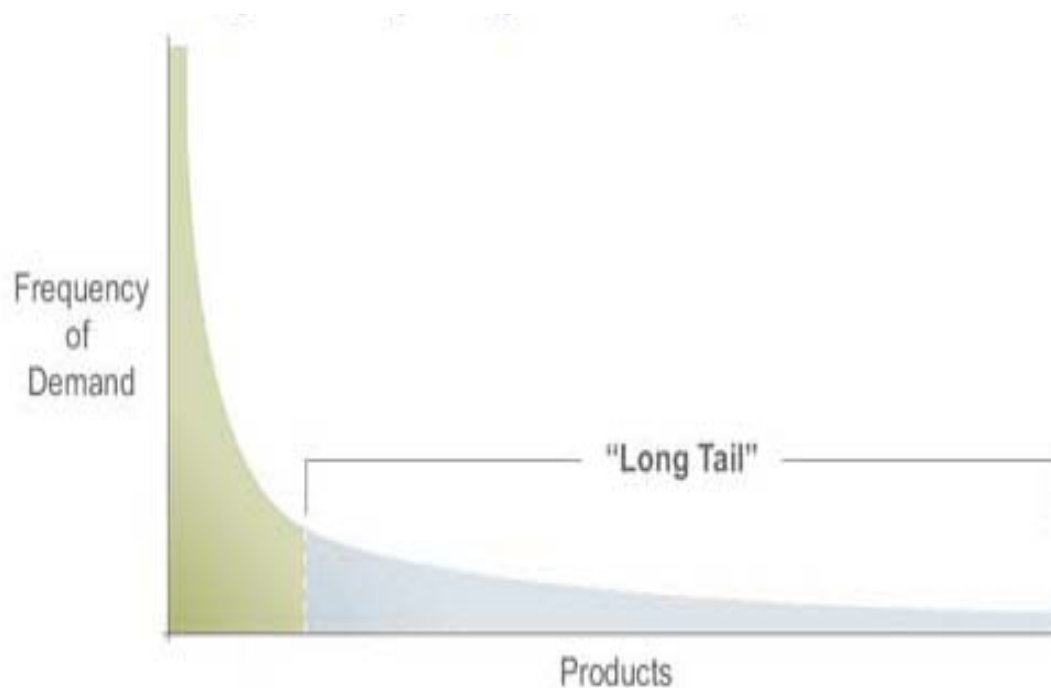
4. **Trust the network – it really does know more than you**
5. **Embrace your customers**
6. **Use social networks to create solutions**

### Creating New Capabilities

7. **Embed flexibility in business models and information systems**
8. **Foster rapid, collaborative innovation in the enterprise**

## RULE #1: Grab and monetize the Long Tail of demand

- Grabbing and monetizing the long tail of demand – beyond the traditional core 20% of demand and sales revenue of a product – is now a viable growth strategy
- Enabling technologies are helping enterprises to:
  - Access customers at a lower cost
  - Offer a broader selection of products & services
  - Better target customer expectations & understand their purchasing behaviors



Source: <http://www.scdigest.com>



# RULE #2: Get Ready – Your customers value digital content

amazon.com®



**You Tube**  
Broadcast Yourself™



- Consumers have shown a clear desire to consume/create and share digital media across platforms and devices
- Emerging technologies are enabling new ways to create, share and consume all forms of digital content
  - Phones, laptops, video, mp3
- Enterprises can take advantage of this opportunity by adjusting their business models and business design
  - Music – Radiohead, Prince, Madonna
  - Consumer Electronics – iPod ecosystem
  - Publishing – What is the future of reading?
  - Your industry – how will it impact you !



## RULE #3: Jump in – 3D Internet/Virtual worlds are real business

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- Creating new markets for virtual products and services – Virtual goods and services paid for in real-world dollars (e.g., avatar clothing, virtual houses, cars).
- Opening a richer direct channel to customers – New opportunities to advertise and deliver virtual and real-world products/services beyond that of a simple web page or B2C/B2B site.
- Enhancing collaboration and communication – In a global, hyper-distributed, matrixed world, could meetings, learning and training be the ‘killer app’ for the 3D Internet/virtual worlds?



## 3D In Action – Royal Bank Virtual Agent...

- **Virtual agents** are digital people – realistic-looking, 3-D characters on screen – to help talk you through complex processes.
- Royal Bank of Canada is using one of the basic virtual agents created by CodeBaby. Her name is May, and she **walks customers through online banking**.
- RBC is focused on attracting new immigrants as customers. The bank has already created a **Cantonese avatar** for its Chinese language site.
- RBC is exploring creating additional virtual agents to appeal to **20-somethings** and others to appeal to the **baby boomers**. ([The Toronto Star](#) 04/Feb/2007)



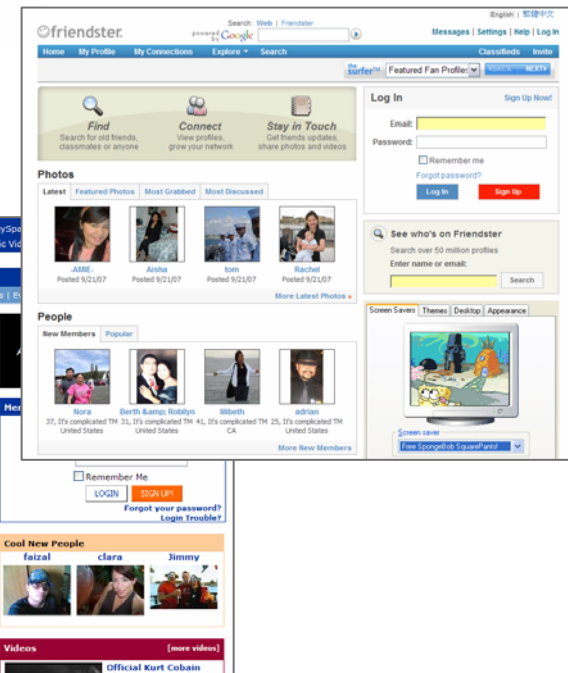
See also:  
[Ms. Dewey](#)  
(interactive search assistant)

## RULE #4: Trust the network – it really does know more than you

- The Internet is a powerful source of information on consumers, their buying habits and preferences
  - New analytical technologies emerging to mine data
- Mining information for business intelligence is only beginning
  - Privacy, legal, & ethical issues
- Enterprises are seeking market intelligence from the social web that will help them learn more about their customers
  - Facebook, Friendster, MySpace - Right to sell users' provided data?



Google Analytics





## RULE #5: Embrace your customers

- Ease of access reduces relationship barrier and creates new opportunities to:
  - change the way enterprises connect
  - build customer relationships
- Build rich communities of participation (crowdsourcing) by opening up the dialogue and encouraging discussion around your own products and services
  - Improves the overall quality
  - Creates better products and services
  - Creates better brand experience
  - Lowered costs to serve new customers



Source: [www.wikipedia.com](http://www.wikipedia.com)



## Rule #6: Use social networks to create solutions

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- Collaboration is the key to innovation
- Innovative technologies are opening up an entirely new dimension to integrating an ecosystem – a long establish solution strategy
- Solutions require better integration across business partners to meet client needs.
- Social networks, enabled by innovative technologies, are critical components for creating these web-based solutions driving value in key areas:
  - Building loyalty, trust and camaraderie in an increasingly mobile and global marketplace
  - Fostering innovative discussion and support among online communities with committed participants, expert users and early adopters
  - Creating advocates for the company in the increasingly transparent world of the social web, where information and misinformation disperses instantaneously.



## Rule #7: Embed flexibility in business models and information systems

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- Rethink overall business design, taking a modular/component view of the enterprise
- Make hard decisions about which activities belong inside or outside the enterprise to achieve competitive advantage
- Adopt a service oriented technology architecture that translates the business component model into IT services that support superior business performance
- 3 types of business model innovation:
  - Industry model innovation (IM) - Innovating the industry value chain by:
    - Moving into new industries
    - Redefining existing ones
    - Creating entirely new value chains
  - Revenue model innovation (RM) - Innovating how revenue is generated through:
    - New value propositions
    - Pricing models
  - Enterprise model innovation (EM) - Innovating value chain roles by:
    - Changing the extended enterprise to be either more integrated or more specialized
    - Transforming networks of employees, suppliers, customers and others



## Some case studies ...

# Business Model Innovation

## Industry model Innovation

## Revenue model Innovation

## Enterprise model Innovation

### INDUSTRY TRANSFORMATION



• Apple transformed the music industry through a new way of connecting hardware with software to download music with iPods/iTunes product & service combination



• Dell redefined the PC value chain and industry model by using a direct to customer sales model

### HORIZONTAL MOVES



• Virgin moved from one value chain to another, leveraging its brand across industries including airline, media and telecoms

### PRICING / REVENUE MODEL



• Gillette innovated the pricing model by giving away razors and making money on the blades



• Netflix shifted the revenue model from product / rental based to a subscription based annuity model

### VALUE PROPOSITION



• Cirque du Soleil reconfigured offering and value elements to transform the circus experience

### INTEGRATION



• Zara's Fast Fashion model is supported by a highly integrated business model along its value chain

### SPECIALIZATION



• Bharti created a highly specialized Telco business model by focusing only on its key differentiators – marketing, sales and distribution – and partnering for everything else

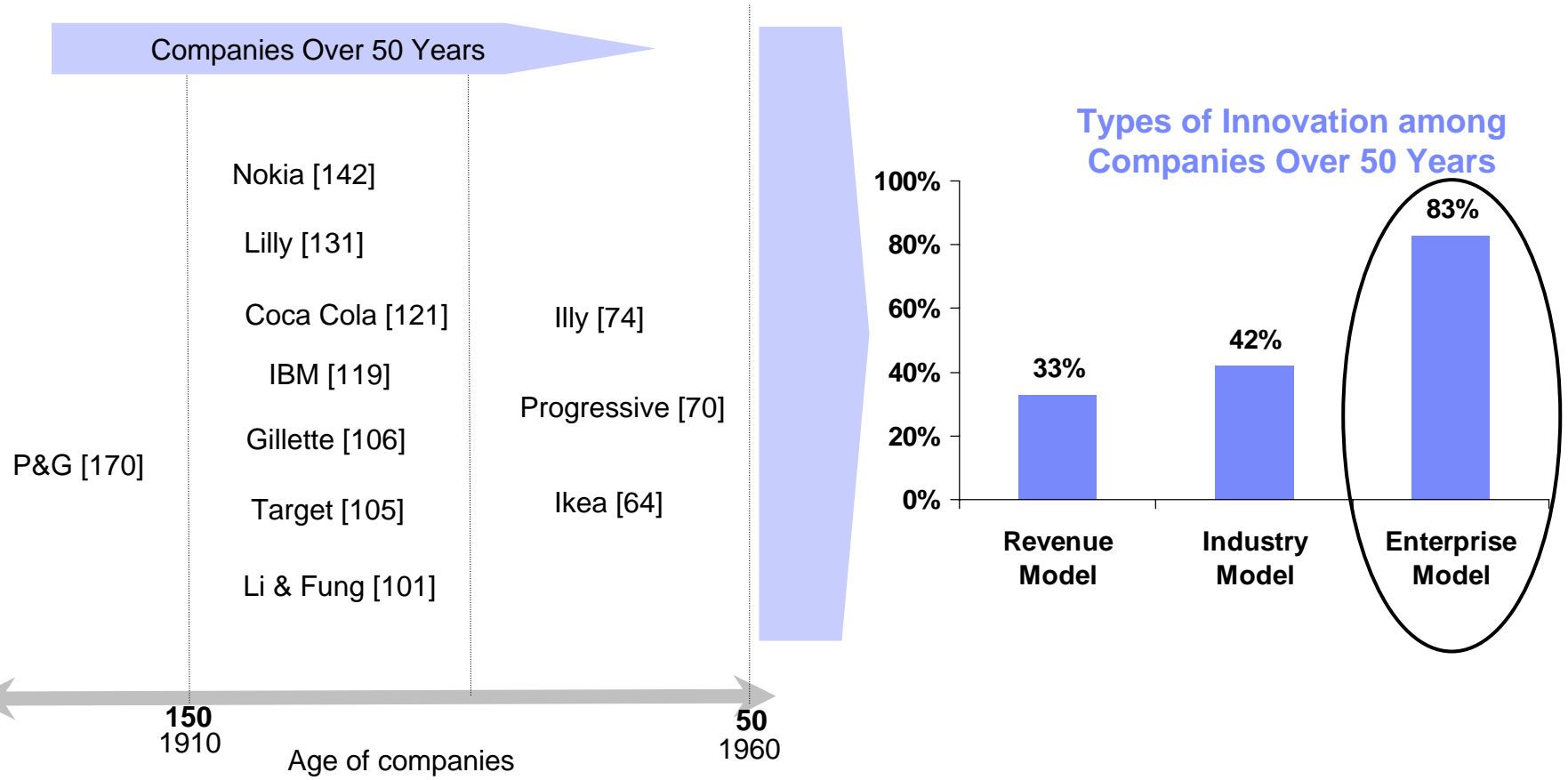
### EXTERNAL COLLABORATION



• P&G uses an innovative R&D collaboration model "connect & develop", sourcing over 50% of ideas externally



# Enterprise model innovation is especially relevant to older companies



Source: IBM Institute for Business value analysis of Thomson ONE Banker financial data and company annual reports, 1997 - 2006

Note: Each company can innovate in more than one dimension – totals will NOT add up to 100%



## Rule #8: Foster rapid, collaborative innovation in the enterprise

- Collaborative tools & social networking provide greater transparency & opportunities to innovate
- Lowered costs
- Decentralized grassroots innovation vs centralized R&D
- “Fail fast, fail cheap”
- New mindsets & metrics to measure innovation ROI





## The IBM InnovationJam \*

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- **What:** Global online brainstorming sessions involving hundreds of thousands of participants -- IBMers, clients, business partners, academia and even family members
- **Why:** To create breakthrough new marketplace opportunities/partnerships for IBM and clients
- **How:**
  - Four fora built around major aspects of our professional and personal lives: [Going Places](#), [Staying Healthy](#), [A Better Planet](#) and [Finance and Commerce](#)
  - Participants discuss potential innovations made possible at the intersection of emerging, new technologies and major business/societal shifts
  - Emphasis on surfacing ideas for new products, services, processes and new business models that will transform industry and society
- **Outcomes:**
  - A set of meaningful marketplace opportunities and partnerships that IBM and its clients announced in November 2006
  - Supported by up to \$100 million in development funding for the best ideas.
- **Two Phases:**
  - Idea Generation – 4 days long
  - Idea Refinement – 4 days long

## Agenda

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## The innovation dilemma

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### CEO Study: Innovation is profitable because it is hard to do

- 76% say collaboration is critical
- Only 52% collaborate “to a large extent”
- 35% see unsupportive climate and culture as top obstacle



Source: *The Global CEO Study 2006: Expanding the Innovation Horizon*

# There's no single path to innovation

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## Innovation Models (or Archetypes)

A unique mix of cultural and operational traits that represent how the company innovates.

- The marketplace of ideas
- The visionary leader
- Innovation through rigor
- Innovation through collaboration



# Inside the Archetypes



*Marketplace of ideals (16%)*



*Visionary Leader (22%)*



*Innovation through Rigor (37%)*



*Innovation through collaboration (25%)*

Leadership  
People  
Process  
Environment

- “Bottoms up” approach
- Content with “leading from behind”

- “One man show”
- Leader determines direction of innovation & selection of ideas

- Involved Leadership
- Sets priorities, raises urgency, and allocates resources

- Leadership sets framework for collaboration
- Ideas generated with partners & customers

- Fully uses employees
- Recruited for creativity and passion

- Adept at the teamwork necessary to execute leaders’ plans

- Small groups dedicated to problem-solving
- Strong team culture

- Collaborators
- Empowered to make deals with outside vendors

- Well-stated innovation goals for individuals
- Effective stage gate process, pilots and trials
- Clear metrics of success and failure

- Fast implementation of select ideas
- Portfolio maps and strategic plans to link executive vision to daily activities

- Fewer ideas, with strong formal vetting process
- Strong focus on cross-functional teams for rapid execution

- Robust stage gating and implementation mechanism
- Frequent pilots and trials, involving partners and customers

- Environments that allow experimentation
- Generates Large number of ideas – mainly internal

- Few inter-dependencies with outside parties
- Select ideas generated and pursued

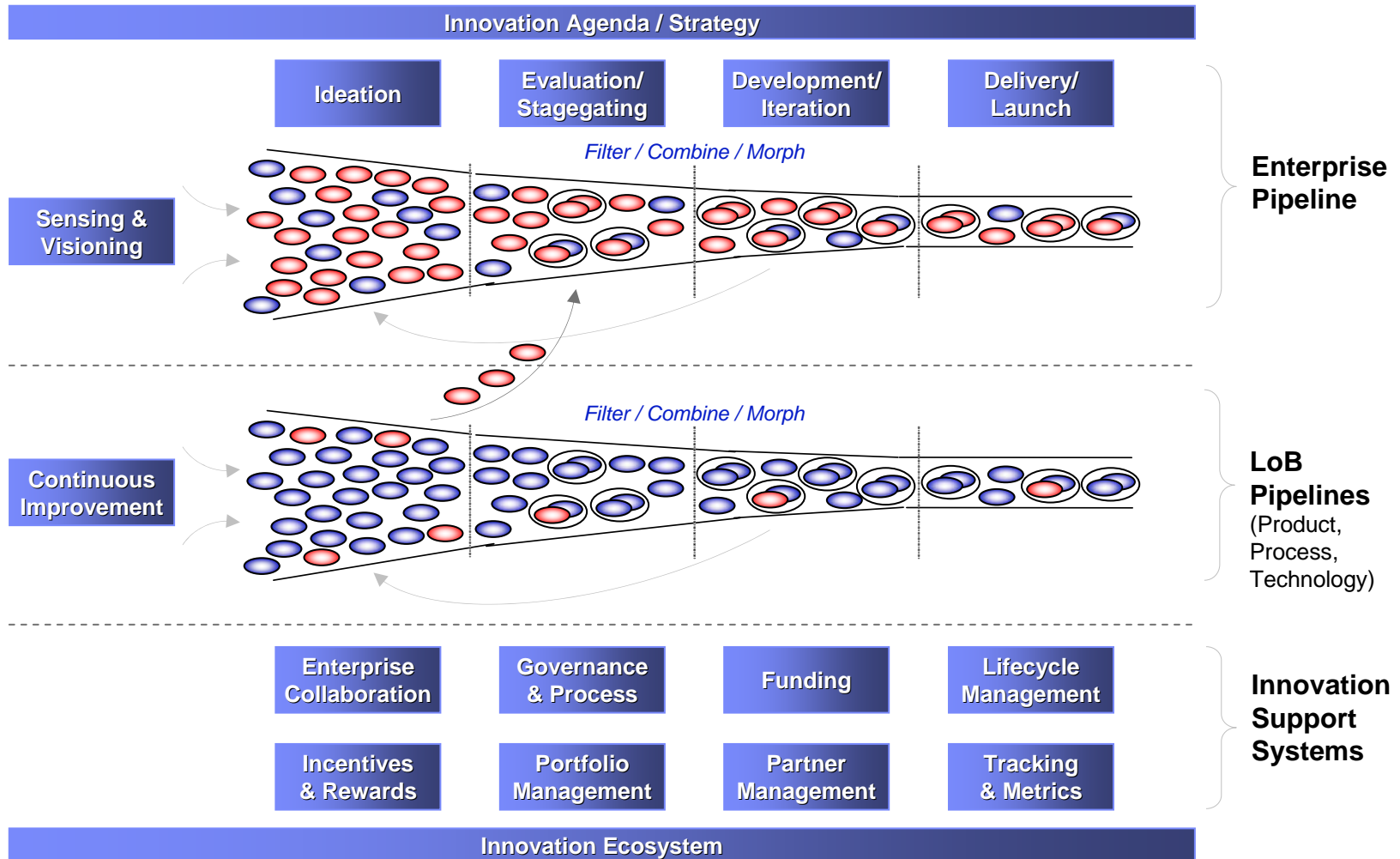
- Diffuse product lines impossible for a small set of visionary individuals to control
- Rigorous scanning

- Understanding of customer needs and partner participation
- White space innovations

# Skills are required in all aspects of IBM's Innovation Capabilities Model

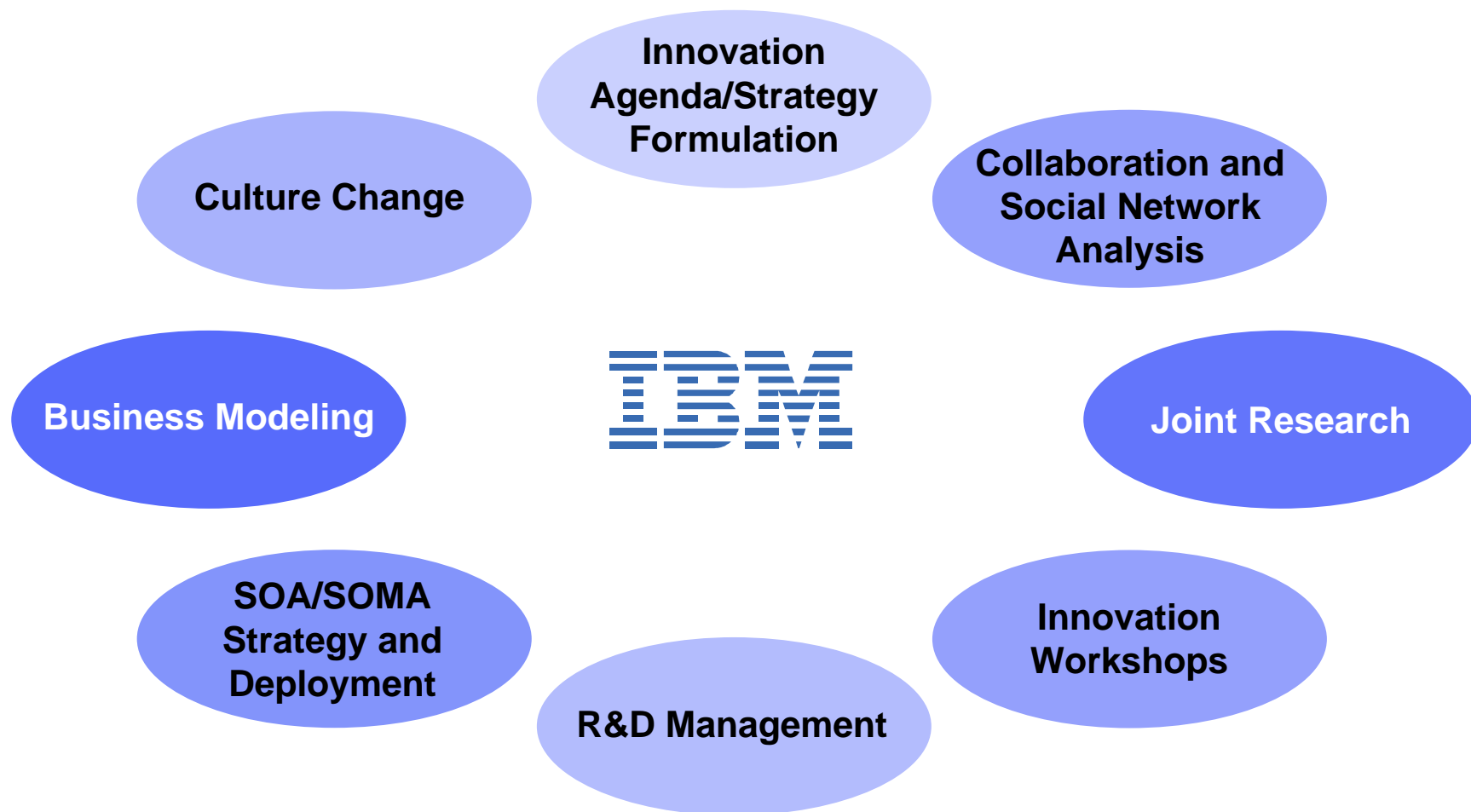
<b>Innovation Agenda</b>	Market/Customer Insights		
	Innovation Portfolio Management		
	Strategic Planning		
<b>Innovation Capabilities</b>	<b>Products / Service / Market</b>	<b>Operations</b>	<b>Business Model</b>
	Product / Service Lifecycle Management	Operations Management	New Business Model Management
	Solution Ideation	Supply Chain Management	Business Model Detailing
	Solution Selection	Customer & Channel Management	New Business Incubation
	Solution Development	Operations Optimization	New Business Launch
	Solution Launch		
<b>Innovation Enablers</b>	Integration of Business & Technology		
	Collaboration & Partnering		
	Idea Generation		
	Climate for Creativity		
	Metrics & Incentives		

# ... and integrated into a framework to manage innovation end-to-end



## How IBM helps companies with the innovation journey...

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## Agenda

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# The new Agile CFO is an Innovation Leader

## CEO Agenda

Business model innovation matters



CEO

## Agile CFO Actions



1. Lead Innovation Through Insight

CEO

## Innovation Building Blocks

- Identify business model innovation opportunities
- A finance function that enables insights and flexibility for business model innovation

Collaboration is indispensable



CEO



2. Eliminate Innovation Inhibitors

CEO

- Reduce structural complexity to facilitate collaboration
- Create global business process sight lines

Innovation must be orchestrated from the top



CEO



3. Create an Innovation Climate

CEO

- Track innovation without stifling it
- Fund the unknown world
- Dialogue differently

# CFOs need to take a different approach to innovation than they would for established practices

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**Shield from budgeting cycle**

Shield innovation project teams from the annual budgeting cycle

**Problem solvers**

Be problem solvers, not bean counters – get involved in the brainstorming and trouble shooting

**Good enough**

Don't push for perfection – good enough can be great

**Don't leap**

Step, don't leap – leap frogging rarely works, thoughtful staged approaches often do

**Learning**

The right kind of failure is success – learning what's wrong with an approach and adapting appropriately is a good thing, not a failure

# Measurement and metrics need to be tailored for innovation and differ depending on the stage of activity

## Early Stages

The focus is on potential magnitude and patterns

## Measuring Innovation

- Avoid early detailed financial estimates when the accuracy is generally low<sup>1</sup>
- Focus on the potential order of magnitude versus precise revenue projections<sup>1</sup>
- Determine how well the innovation fits within the pattern of success<sup>1</sup>

## Later Stages

More traditional measures are typically employed

- Track new product/services success and survival rates
- Assess cumulative new revenues
- Determine the return on investment

## Overall

Establish and include innovation metrics as part of a comprehensive measurement program<sup>2</sup>

- Use a comprehensive set of measures, rather than a single metric to indicate progress<sup>2</sup>
- Track measures specific to innovation at the program or department level to enable timely and effective decision making<sup>2</sup>
- Ensure innovation is not an island by linking innovation

Sources: Anthony, Scott, Matt Eyring, Lib Gibson, "Mapping Your Innovation Strategy," Harvard Business Review, May 2006, Campos, Krystl and Erin Hipple, "Innovation: Putting Ideas into Action", APQC 2005 and IBV analysis

## In Summary - Innovation has evolved to the point that it is based on a new set of realities !

Old Belief	New Reality
Innovation means developing new products and services	<b><i>Business model innovation matters</i></b>
Innovation is too critical and proprietary to involve outsiders	<b><i>External collaboration is indispensable</i></b>
Responsibility for innovation should be delegated	<b><i>Innovation must be orchestrated from the top</i></b>

“We will fight our battles not on the low road to commoditization, but on ***the high road of innovation.***”

— Howard Stringer, Chairman & CEO, Sony

“***Constant reinvention is the central necessity at GE...*** We’re all just a moment away from commodity hell.”

— Jeffrey Immelt, Chairman and CEO, GE

“The ***business model we choose will determine the success or failure*** of our strategy.”

— CEO Study Participant

“***Innovation is viewed as a multi-dimensional concept, which goes beyond technological innovation*** to encompass... new means of distribution, marketing or design. ***Innovation is... an omnipresent driver for growth.***”

— Erkki Liikanen, EU Commissioner for Enterprise

Note: Named quotes derived from published sources; non-named quotes derived from CEO Study 2006 interviews

