The Innovation Culture

A guide to excellence in product innovation

The product executive has a unique view on the software organization. Product Management serves as the thread that binds together the disparate and often competing functions of Sales, Management, I.T., Operations, Finance and Marketing. If there is any one person who feels the pain of the entire organization, it's the Product Manager.

Yet most companies are neither created by nor run by seasoned Product Management professionals. Software companies are often created by I.T. wizards, Finance gurus and professionals from the various vertical markets served by software products. A financial services product is often created by a Financial professional. A medical product by a Physician. A fitness device by an athlete.

It is therefore average that the center of innovation in any company is *not* in Product Management – at least on day one. But as growth occurs, inevitably, a Product Management organization is needed to manage that growth, prioritize ideas, incubate, test, prove and drive a consistent and data-driven path to growth.

The insertion of a Product Management organization comes with as many risks as benefits. How does a company navigate the insertion of a Product Management discipline in order to create an Innovation Culture?

This white paper offers a roadmap. – Laurence Dunne, Author

Developing a Product Strategy

The simplest mistake many companies make is never articulately defining a product strategy that filters down into all decision making. A good way of thinking of a Product Strategy is to use the Roadmap analogy. The most important question to ask is "*What is my destination?"* From this simple question, you develop a strategy. You navigate roads, intersections, bad weather and dangerous turns. You plan food and fuel stops and choose hotel stays. As with any good road trip, changing your final destination, extending the trip, taking side-trips are all acceptable, as long as you incorporate these into your strategy.

A good product strategy treats the company's intended destination as its most important defining point. This may seem obvious, but it often isn't. Is the company striving for profitability within the next year? Is market penetration more critical? Top-line revenue growth? You might say *all of the above*, but that's not necessarily true. Ultimately, the product strategy is defined by investor expectations, as expressed by the C-Suite.

CRITICAL: The product strategy expresses the most effective path to reach a destination defined by Investors.

For example: *A software company wants to exploit new technologies in mobile GPS and payments to deliver a door-to-door fast-food service partnered with local restaurants. They believe there is a market for 30,000,000 customers in the United States. Investors give management $1 Billion to spend creating the company, and set a two year target to reach 10,000,000 of their customers. Their highest priority is becoming the most recognized name in the business. Revenue growth can be achieved once customer acquisition has reached this milestone. Profitability can be achieved through efficiency gains that come with the scale they have then achieved.*

What is the destination? Profit? Revenue growth? No. The destination is clearly expressed by investors:

Investor 2 year horizon destination: Become the most recognized name in door-to-door food delivery business, and serve a minimum of 10,000,000 customers in year 2.

This simple mission statement enables you to focus on developing a product strategy because it tells you where you want to go. Now, it's time to figure out how to get there.

Step 1: What do we need?

Step 1 is defining your needs. It's the product equivalent of saying "I'm going to this destination, I will need a car, money, food, clothes, sun-tan lotion" etc. In this example, it's clear we need all of the following:

- A Mobile App for consumers to order the food
- Local food vendors in target markets to prepare the food
- A payments engine
- Drivers on-call in all locations
- A marketing campaign to raise awareness
- Back office support

As simple as it sounds, this tells you how to organize your product team for the first two years. It's time to figure out how we're going to get to our destination.

Step 2: How do we get what we need?

In step 2, we innovate. We have a seriously aggressive timeline (negative) but lots of capital (positive). We don't have early enough talent (negative) but our investors are deeply interested in the outcome (positive). We use our strengths and weaknesses to make decisions. These decisions introduce us to the four major categories of product strategy:

- **Development Strategy**
- **Partner Strategy**
- **M&A Strategy**
- **Competitive Strategy**

Development Strategy

Development Strategy concerns the strategy of what we must ***Build, Lease or Buy.*** The key question to ask is *How do we best reach our destination with a solid development strategy?*

A good starting point for a development strategy is as follows:

Define and ***Build*** your core competence.

Lease standardized or slightly customized functions that are not core competences

Buy highly customized functions that fit your core competency, but are temporarily out of reach.

In our example, a good start for a development strategy might be as follows:

Build	**Lease**	**Buy**
Restaurant Management	Accounting Software	Consumer Mobile App
Driver Management	Payments Software	Database/Server software

In this example, we have defined the mobile relationship with customers, drivers and restaurants as a core competency, but we have determined that the extra level of usability and complexity for the consumer mobile application will take us several months to acquire so we want to build it faster than we can hire mobile developers. Buy makes sense, because we can add it to our core competencies once it's purchased.

Partner Strategy

The partner strategy concerns how we leverage partnerships to help us get to our destination. Partners can be resellers, channels, providers of ancillary services or simply companies who have things that we need in order to succeed.

In our example, there are two obvious examples of good partners: Large-scale restaurant chains and companies who hire lots of drivers. To incent them, we will have to decide what motivates them. A restaurant chain may not need to be paid because they get to sell their food to our customers. In fact, they may be willing to give our customers a discount, increasing our value. The drivers, however, will need to be paid, and we must incorporate their fee into our pricing model.

Of course, a key component of a partner strategy is also the analysis of partners who could become competitors. But we will deal with competitive strategy later.

M&A Strategy

The M&A strategy concerns how – or whether – we leverage mergers and acquisitions to achieve our goals. M&A isn't always advanced and complex. Early stage M&A could simply be buying a small mobile development shop for its developers and office space. M&A strategy can fall into multiple areas:

- Buying Influence
- Leveraging someone else's scale
- Buying customers
- Buying investment
- Cutting cost

In our example, an obvious acquisition might be a mobile development company, a marketing firm, restaurant chains, taxi services etc.

In almost all cases, the product organization will lack the authority to execute on M&A activity, so for our purposes, we are going to use M&A to simply buy a marketing company to gain consumer recognition as fast as possible.

Competitive Strategy

A competitive strategy concerns how we will outmuscle our competitors. There are several strategies that can be considered to improve market share relative to competitors, including:

- Pricing Competitiveness
- Feature Differentiations
- Value Differentiation
- Speed-to-market Differentiation
- Quality Differentiation

In our example, we will use speed to market as the differentiator. Food at your door in less than 30 minutes or its free.

Step 3: Creating a Strawman for a Product Roadmap

In step 3, we take what we put together a Strawman for a roadmap. Taking all of the strategy statements we reached in Step 2, we create a high-level roadmap that includes internal development, partner development, acquisitions, etc. This is now our playbook. This is our product strategy.

Structuring a product team

There is no right way to structure a product management team, but there are many wrong ways. Consider the following example of a Product Leader who made the classic mistake made by so many leaders in growing small enterprises.

Experience: The 'Failing' Product Team

A software company, built as many are on the innovation of technology wizards, had nine products. The CEO recognized the need to create a Product Management team, and hired a VP to run the team, and gave him 9 open positions to fill. The new VP of Product Management decided to fill the position with nine product managers, each managing a single product. Simple.

Over time, things fell apart. Everyone agreed that Product was failing, but no-one could agree why. I.T. liked working with three of the product managers, but not the other six. Sales valued a different three. Management favored yet a third group.

The CEO fired the VP of Product Management and hired a consulting firm to help him reorganize.

The consulting firm, qualified in Pragmatic Marketing, immediately discovered the problem: Sales reported that only three of the product managers had an instinct for closing deals. They were skilled at PowerPoint, great in person, and had a knack for pricing, positioning and competitive analysis. Management claimed only three were able to think strategically. They excelled at developing Roadmaps, defining budgets and impressing investors. Engineering complained that only three could write good requirements.

After careful reflection, the CEO reorganized the group. The new Product Management group consisted of three separate teams: Sales Engineering, Product Strategy and Product Management. Each team excelled in one function. Each player could now focus on their strengths.

This experience teaches us a 101 lesson about Product Management. There is no one discipline in which every person excels, and Product Management is an area that requires a broad number of differing skillsets. Technical competence, pricing savvy, marketing competence, legal and regulatory knowledge, sales savvy, all are very different propositions and require very different people.

While there is no right answer for all organizations for how to structure a product management organization, a good rule of thumb is to respect ***The Product Management Triad.***

The Product Management Triad

In general, dividing product teams into at least these three functions allows executives to hire and place people based on specific skillsets and give them specific functions.

At the highest level, it is the role of the Product Strategy group to DEFINE the strategy, the role of the Product Management group to EXECUTE the strategy and the role of the Product Marketing group to SELL the strategy.

We have already discussed defining the strategy, so in the next two sections we will cover Management and Marketing.

Product Strategy

Product Strategy is the pinnacle of Product Management. As defined earlier, the Product Strategist defines the direction of the entire organization. Among the key stakeholders of his/her work is:

- The entire C-Suite
- Investors and potential investors
- Large scale partners
- M&A targets

Therefore, this person, or persons, is among the most senior and respected members of the team. Product Strategists spend most of their time selling their ideas and budgets to the CEO, CFO, Chairman of the board and influential leaders within I.T., Legal and Compliance, etc. This is the most key position within any product organization.

Product Management

Product Managers must be able to execute on the company's roadmap. They manage budgets, work with sales and marketing to help develop a message, and work with I.T. to execute on the roadmap. They may manage vendors, clients, sales support efforts and feature enhancements.

Product managers may have backgrounds in I.T., Business, Finance or the chosen area of expertise for a specific company. For example, our food delivery company may hire a product manager from the fast food and/or delivery businesses. Ideally, the leader of the product management group hires a diverse team from different kinds of backgrounds and then facilitates cross-functional team exercises to help cross-pollinate knowledge. Key attributes of a good product manager are:

- Strong personal presence, influencing skills
- Detail Oriented
- Technical Proficiency
- Excellent writing and presentation skills
- Demonstrated problem solving ability
- Experience in related field

Product Marketing

Product Marketers must be able to sell the roadmap to key stakeholders – often both internally and externally. This includes not just the sexiest – and arguably easiest – of functions, marketing the product to clients or consumers, but also the ability to sell it to sales people, partners and internal employees. Training and employee development may fall into their area.

Collateral, advertising content, channel marketing, partner development are all key components of their area. Contrary to popular belief, this is a highly technical function, requiring skill at analyzing data to come up with price points, market segments and channels. This team works closely with finance on pricing models and with advertising agencies on external collateral. A wide range of skillsets is needed, and this team will ultimately drive how the product reaches the consumer.

Engineering Product Innovation

Of course, none of the above creates an innovative environment. So far, we have a strategy and a team, but no innovation has occurred. And that's a key lesson. Product does not innovate any more than any other part of the company. Innovation comes from all corners of the company, and from outside the company.

Here's a few great examples of how innovation is stifled in companies. As we look into these, how can we engineer an organization that doesn't fall into these traps? Let's take a look at our fictional food delivery company a couple of years down the line and see where they are failing.

Example 1:

Peggy from the call center has noticed that three of the calls she got today were requests from customers to reset their mobile passwords. There is no area in the CRM tool for Peggy to note the reason code for a password change (the closest is "website issue"). So Peggy tells her manager, John, that she believes there's a systemic problem with password management. John is already aware of this, but is afraid that if a better user experience leads to fewer calls to the call center, he might lose his job as a supervisor as the call center needs fewer employees. He thanks her for her note and doesn't follow up. He hopes nobody notices the issue.

Example 2:

Simon in marketing accidentally discovers a 68% overlap between people using our product and people shopping for groceries online on a regular basis. He discovers the reason for this is that both services are typically used by people who don't have time to cook, but have money to order in. Simon reasons that offering an overlapping service where people can order both restaurant food and groceries from local stores and have them both delivered to the door can increase efficiency and improve top-line revenue. Simon puts together a PowerPoint presentation explaining his ideas, and presents it at the next monthly product meeting. He is asked to follow up with a detailed revenue projection, but the following month, Simon is promoted into a new position and the idea drops to the floor.

Example 3:

Janet works in the fraud group as an analyst. She notices that only 28 zip codes account for 38% of Fraud while accounting for only 1% of revenue. She analyzes why, and discovers that credit card theft groups are operating out of addresses in these zip codes. She tells Andrea, the product manager, but she reasons that fraud accounts for only 0.1% of cost, and it's a problem not worth fixing. Next month, the amount of fraud from those zip codes increases tenfold, and a lot of money is lost.

Example 4:

Bob is a database analyst, and he's been looking for a promotion into the product team. However, another candidate was chosen ahead of him. He notices that a small subset of customers are ordering the same products over and over again even often the same food product on the same day every week - and thinks a "favorites" function and a "automatic re-order" capability would encourage more of this positive behavior. However, upset that he won't get 'credit' for the idea if he doesn't get his move into the product group, he sits on the idea.

In all of the above examples, what common threads can we see?

1. Ideas come from everywhere, even the most junior employees
2. The person who came up with the idea was not the person responsible for executing on it
3. Failure always came down to not following up
4. Motives are diverse and sometimes self-serving
5. **Nobody believed they would be personally enriched if the company implemented their idea and profited from it**
6. **None of the people involved believed there was a central innovation lab where they could submit their ideas.**

That last two points are the most important. Nobody believed there was somewhere to put their idea, or that they would profit from it. And isn't profit the core motivation for all work?

The Innovation Lab

This brings us to the importance of the innovation lab. *Anyone* can submit an idea for the lab to review. To prevent a large number of bad ideas from reaching decision makers (which will kill the innovation lab), ideas must go through formative stages. Here's a good simple structure for creating an innovation lab:

Every month, one third of all employees, taken from all areas of the company, are assigned for an entire day to innovate. They are randomly assigned to cross functional teams, each team consisting of people from management, product, IT, QA, marketing, call center, risk, billing etc. Each person submits to their team their ideas, and the team votes up the best ones. Later in the day, the teams present their best ideas to the product team. The product team includes the best ideas in the next iteration of the product roadmap, and each employee who submits an idea that gets implemented gets a financial reward. The next month, a different one third of all employees attend the innovation lab.

To make this workable, each innovator must know that they will get a significant financial reward for submitting a successful idea.

Cross Functional team building

The innovation lab is the most structured way to engineer innovation. Cross functional team building is another. A typical company organizes its physical space based on co-locating people with similar job functions. For Product Management, this often means placing product managers near each other, and therefore away from the engineers who build their products, the sales people who sell them and the operations people who support them.

Switch it up. Arrange cross-functional team building exercises.

A good example of a great cross-functional exercise is divide into teams and to have each person on the team express the hardest thing they faced at work in the last 24 hours. When the fraud manager says "*Having to log out and back into the CRM tool eight times,"* the production support person on the team might express surprise that she never raised the issue to him. But if she knows it will take an hour to fix the issue or two minutes to work around it, she will work around it. But everyone else nods their heads – they're all working around the issue. Because of the cross-functional team building exercise, the issue is resolved, the fraud manager gets a bonus for raising the issue, everyone is happy.

Collaborate, collaborate, collaborate

Everybody likes to think they are a participant in the decision making process. Of course, not everyone can set the direction for an enterprise, but everyone can play a part. The creation of annual product roadmaps, defining of requirements for specific projects, setting of direction for marketing campaigns etc, should all be open-invite collaborative sessions.

A good way to facilitate this is with open workspaces. Product Managers especially should be encouraged to work from different workspaces a couple of days a week, meeting developers, QA, project managers, call center supervisors and others who can provide different perspectives on the product. The Product Manager doesn't have to take every suggestion on board, but the collaboration makers everyone a solution creator.

To encourage this hallway collaboration, the product manager should be incented to record the ideas, the source and then allowed give a financial reward to the person who created the innovation.

Align incentives with goals

Of course, it's not always possible to hand out large wads of cash for every idea. Let's go back to our food delivery company and see if there is another way to reward employees for ideas that help the company reach its goals. Lots of companies award stock options or purchase plans, annual bonuses etc., but these are usually tied either to stock price or company performance.

The larger the organization, the less each individual is motivated by these metrics. Instead, it makes sense to create an allocation of stock options to be awarded to employees based on their contributions to the innovation culture.

Now, lets go back to our first four examples and see how different the outcomes are with an innovation culture.

Example 1:

Peggy from the call center has noticed that three of the calls she got today were requests from customers to reset their mobile passwords. There is no area in the CRM tool for Peggy to note the reason code for a password change (the closest is "website issue"). So Peggy meets the product manager who is working out of a call center workspace today, and tells him about the issue. He walks over to a database admin and asks for a query to define how often this happens. The DBA discovers there were 6,807 instances of this in the past 12 months, at a cost of over $3 per call, for a total of $21,506 in cost. The product manager notes Peggy's name, and mentions the issue at his next daily stand up. The develop tells him it will cost 20 hours to fix. With an internal cost of $60 per hour, that means it can be fixed for $1,200. He prioritizes it for the next sprint cycle. It launches a month later, and saves the company $21k/year. On the day it's fixed, Peggy is called to the board room. When she gets there, her manager hands her a check for $2,000, representing 10% of the money saved.

Example 2:

Simon in marketing accidentally discovers a 68% overlap between people using our product and people shopping for groceries online on a regular basis. He discovers the reason for this is that both services are typically used by people who don't have time to cook, but have money to order in. Simon reasons that offering an overlapping service where people can order both restaurant food and groceries from local stores and have them both delivered to the door can increase efficiency and improve top-line revenue. Simon puts together a powerpoint presentation explaining his ideas, and presents it at the next innovation lab. The idea is voted up, and is put onto the roadmap. Simon gets 500 shares in the company as a reward for his suggestion.

Example 3:

Janet works in the fraud group as an analyst. She notices that only 28 zip codes account for 38% of Fraud while accounting for only 1% of revenue. She analyzes why, and discovers that credit card theft groups are operating out of addresses in these zip codes. She tells Andrea, the product manager, but she reasons that fraud accounts for only 0.1% of cost, and it's a problem not worth fixing. Not satisfied with this, Janet attends the next innovation lab. Her idea is voted up, but doesn't make it in time for next months release. Next month, the amount of fraud from those zip codes increases tenfold, and a lot of money is lost. However, Janet is recognized for her idea, awarded 100 shares in the company and promoted to Senior Fraud analyst.

Example 4:

Bob is a database analyst, and he's been looking for a promotion into the product team. However, another candidate was chosen ahead of him. He notices that a small subset of customers are ordering the same products over and over again even often the same food product on the same day every week -

and thinks a "favorites" function and a "automatic re-order" capability would encourage more of this positive behavior. He presents the idea at the Innovation lab, its gets voted up and implemented. Orders increase 10% in the following month. Bob is awarded $5,000 and 1,000 shares in the company as a reward for his contribution.

Fostering a culture of Innovation

The Key word is *fostering*. It takes continuous effort to weave a culture of innovation into your corporate DNA, and to keep the culture strong. As the company grows, the distance between the Product Management team and the rest of the organization grows with it. As a company matures, it becomes less able to award stock, but more able to award cash, promotions and other incentives. The culture of innovation requires constant innovation itself, or it will die. Companies who create, and maintain, a culture of innovation across their entire organization are the ones that grow and succeed.

While Product Managers should be great innovators themselves, the greatest thing a Product Management organization can do is to create and foster a culture where the entire organization continues to innovate.