



Finding new growth: the case for innovation by enhancement

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Most companies aim their innovation efforts at seeking ways to protect and increase turnover of existing products and services within their existing customer base. Top innovators, however, take a different approach, spending time and money on finding ways to broaden their customer base through smart new combinations of existing technologies and markets. This article shows how innovation by enhancement works and demonstrates how to find and assess enhancement opportunities.

Ever since modern innovation management started to take serious shape in the 1960s and 1970s, companies have recognized that innovation can have various forms and dimensions. They distinguish short-, medium- and long-term developments. They try to balance incremental and radical innovation. And they may tune their portfolios towards existing, new-to-the-company and/or new-to-the-world applications.

From our work with clients pursuing effective growth opportunities, we find the following classification most useful when examining forms of innovation (see Table 1):

- Intensification: ways to protect and increase a company's turnover of existing products and services within its existing customer base
- Enhancement: ways to broaden a company's customer base through smart new combinations of existing technologies and markets
- Enlargement: ways to enlarge a company's product and service portfolio or develop new applications.

As the results of our recent survey (Innovation Excellence study 2009/2010, see www.adlittle.com) clearly point out, the average company still focuses its innovation efforts primarily on intensifying the current business. Top innovators, on the other hand, spend more time and effort on enhancing or enlarging their business – and as a result are up to twice as profitable.

In this article we will make the case for the enhancement type of innovation. Many companies are leaving serious money on the table by not identifying or developing accessible growth opportunities in adjacent market areas. They continue grazing their often barren land, yet do not see the green pastures around them.

Table 1	Three types of innovation and growth		
New Markets	III. Enlargement		
New Customers	II. Enhancement		III. Enlargement
Existing Customers	I. Intensification	II. Enhancement	
	Existing Products	Modified Products, Enhanced Functions	New Products

Source: Arthur D. Little (derived from an original concept by Igor Ansoff, 1957)

Top innovators spend more time and effort on enhancing or enlarging their business – and as a result are up to twice as profitable as others.

First we will describe the features and benefits of innovation by enhancement. Then we will indicate in which businesses the opportunities for innovation by enhancement are most prevalent. Finally, we will outline an approach for finding and assessing such opportunities in markets near to yours.

The features and benefits of innovation by enhancement

Each type of innovation has its merits and drawbacks. Business intensification by incremental innovation has a clear appeal to companies aiming for predictable timelines and easy-to-identify market segments. Alas, price premiums for incremental new products tend to be low and many me-too product innovations fail to excite the consumer. Information Resources Inc. has estimated that no more than a quarter of the 30,000 or so yearly occurring new consumer product launches in Germany have any meaningful chance of survival.

On the radical side, there are probably very few companies that have not considered every angle of the enormous success of the innovations that the Apples, GEs and Googles of this world have brought to the market in recent decades. If only one could copy the magic formula underlying their breakthroughs, then fat margins and vast market opportunities would arise. Of course, behind these evident success-

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es there are many hidden tragedies of companies that saw their promising breakthrough fail miserably after investing many millions and losing valuable time.

Between the easy-but-low-margin incremental and the high-reward-but-elusive radical lies a seemingly attractive middle ground where companies identify and develop adjacent markets, applications and product functionalities. For companies that master this trick of enhancing their opportunity space well, this is good territory in which to operate. They can rely on most of their existing core competencies, since they do not need to venture into fully unknown technology or market fields. Risk-reward profiles are such that they can still apply most common innovation management tools and processes, such as business case development, stage-gate processes and project funding. At the same time, successful products and services derived from innovation by enhancement typically enjoy greater margins, longer product lifetimes and more differentiation than do incremental innovations.

For example, when McDonald's decided to fight Starbucks in its adjacent food service business, it took only a modest innovation in its offering: the introduction of good coffee. The McCafé baristas at each of the 14,000 Golden Arches locations in the US now turn out coffee that easily compares with the much pricier lattes and espressos sold at Starbucks. By doing so, McDonald's has gained access to a huge and growing consumer segment that is willing to pay for good-quality products - not only coffee but also its new salad lines.

Another example is non-woven fabrics. These used to be a niche material used mainly to provide stiffness to coats and other garments. Innovative players have found clever ways (e.g. by using different fibers or finishing formulations) to customize non-wovens for various applications including filtration, soil management, medical applications, and many others. Depending on the situation, non-wovens often outcompete other materials on price, ease of application, versatility and in other ways. Today, the global non-woven business permeates virtually all material applications and has a global value of around €15 billion.

Even though such middle-ground innovations rarely make headline news, they have a number of features in their favor, such as their relatively low risk profile, low resource intensity and short time-to-cash nature. Nevertheless, companies often fail to grasp these innovation-by-enhancement opportunities. From our experience, we find that there are seven reasons why companies often leave this money on the table:

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1. Cost reduction and continuous improvement take strategic precedence over identification and development of new ideas and applications.
2. Innovation efforts focus on product performance in existing markets, not in new ones.
3. The understanding of current customers has been perfected but the overview and network in other markets are lacking.
4. The skills and manpower to work on opportunities for innovation by enhancement in a concerted way are lacking.
5. The innovation culture insufficiently stimulates creativity, lateral thinking and risk-taking.
6. It is difficult to accept ideas from the outside.
7. Ideas are often not given the chance they deserve.

Businesses with abundant opportunities for innovation by enhancement

In our experience the opportunities for innovation by enhancement are most present at companies in a maturing business and/or companies that offer intermediate products or services. When you are in a mature business, success rarely continues to derive from your initial technology or product leadership. Most often, you thrive on cost leadership and line extensions, and your innovation pipeline has low value. In such cases, innovating in nearby spaces can be rewarding. For example, when the Dutch company FrieslandFoods (now FrieslandCampina, one of the world's

largest dairy companies) launched a yoghurt in an easy-to-use squeeze pack called Breaker in 2002, it moved out of the over-crowded dairy dessert market into the growing and highly profitable on-the-move business, selling at gas stations and roadside kiosks.

Similar opportunities abound at companies that offer intermediate products or services because components and intermediates allow countless permutations and end-markets. For example, a chemical company in one project identified opportunities representing a net present value of tens of millions of Euros (see insert). When you are a supplier of basic materials, on the other hand, opportunities may be more limited because basic materials are less adaptable. Likewise, when you manufacture end-products, the number of new applications may be restricted.

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Finding new growth in performance polymers

The performance polymer company operates in highly commoditized markets. It manufactures a material mainly for traditional applications in the very competitive packaging and building & construction industries, which together account for more than 95 % of the total market. The business had delivered relatively few successful innovations in recent years and faced limited market development perspectives.

The company therefore defined a new business strategy with the goal of becoming a market-driven organization with new applications in new industries and realizing a step change in the innovation process. It set an ambitious target of creating value-adding growth through new market applications for its products outside the traditional markets. The company's management team was aware that this new business course implied "looking for a needle in a haystack" and could only be realized successfully through a change in mindset towards market-oriented innovation.

Any company will find opportunities for innovation by enhancement as soon as the new targeted application of its product coincides with one or more areas of unmet need. The latter are often associated with today's megatrends, such as renewable energy, water management, climate action, feeding the world and security.

They set up a project team to find the targeted NPV from new product applications. Initially, 15 potential application fields were identified, out of which three focus fields were selected for further scanning. The team scanned these fields intensively for two months, performing more than 100 market interviews, visiting market fairs and carrying out extensive desktop research. Almost 200 ideas were identified and analyzed. Finally, nine opportunities were selected for further commercial assessment and NPV calculation. For the opportunities that proved to be economically viable marketing and implementation plans were developed.

The project team reached its ambitious target: the identified opportunities represented a multimillion NPV significantly boosting both the top- and bottom line. In addition, the "finding new growth" project resulted in a number of added benefits such as the regional transfer of ideas, increased internal networking across business units, "quick hits" for the current business, and opportunities for regional application. Above all, the project initiated a change of mindset towards market-driven innovation, supported by intensive communication and newsletters to the entire organization.

More generally, however, any company will find opportunities for innovation by enhancement as soon as the new targeted application of its product coincides with one or more areas of unmet need. The latter are often associated with today's megatrends, such as renewable energy, water management, climate action, feeding the world and security. For example, packaging producers of PET bottles for soft drinks are gradually entering the wine market, hoping to replace glass as the major packaging material. Essentially an 18th-century technology, glass bottles weigh about eight times as much as PET bottles and are far less robust. At a time when supermarket chains in Europe and the US have started to reduce the carbon footprint of the products on their shelves, PET may just have the advantages needed to convince the conservative wine industry to move beyond glass.

An approach for finding opportunities for innovation by enhancement

An effective approach for finding and assessing growth opportunities in adjacent market areas consists of three steps:

Step 1: Generate ideas in promising growth areas

To find the greenest pastures around your business, you need both product-driven and market-driven pointers. You can generate product- (or solution-) driven pointers by answering the following questions:

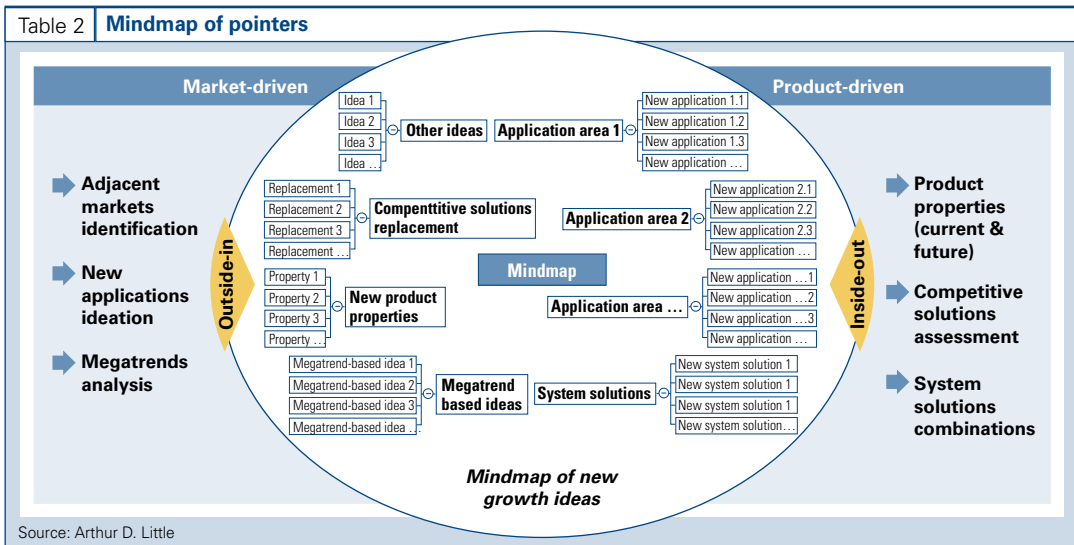
- What are the fundamental (and differentiating) properties of your offering, now and in the planned future? What does it bring, make, do, etc.? For example, if you produce household compressors, are you not, in fact, providing cooling capacity?
- How does this compare to the next-best alternatives? For example, if your product brings impact-resistance, what other technologies do this that yours could compete with?
- Can you combine your product or solution with others made by your company or by partners that together would open up opportunities in markets that are now irrelevant to your solution? For example, if your product is delicious but messy to eat while driving, can you combine it with a new type of packaging that resolves this problem?

Likewise, you can generate market-driven pointers by answering the following questions:

- What are currently your adjacent markets where essentially the same products or services are sold to different types of customers – or perhaps the same customers but at a different time of day? For example, parabolic mirrors (as applied in satellite dishes and headlights) are now successfully being sold by glass producers to concentrated solar power customers.

- What are the interesting megatrends impacting your business and society at large that may conceal relatively easy-to-access opportunities? For example, if you are a handset manufacturer and you see an ageing population around you where more and more people struggle with small buttons and squint at small font sizes, why not make a phone where everything is simply larger and easier to read?

A mindmap is a powerful instrument for structuring and visualizing the pointers from both a product and a market perspective (see Table 2 for a simplified example). In our experience, combining these two dimensions in interviews with experts, (potential) customers, suppliers and partners, as well as in desktop research and visits to relevant fairs and exhibitions, will typically bring you about 200-300 ideas worth exploring. The most promising ideas are then transformed into opportunities, which clearly describe your product’s function and properties in the application, as well as the initial solution concept.



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Step 2: Make a commercial assessment of the attractive opportunities

Each of the identified opportunities needs evaluation in terms of the commercial potential it offers. As the opportunities often represent unknown areas, they are by definition difficult to evaluate. Therefore, strive for the best possible estimation of the business potential, but at the same time accept the relatively high level of uncertainty at this stage. Besides commercial assessment (e.g. based on net present value or expected commercial value), you should also evaluate the opportunities in terms of fit, effort and risk. You can then select the best opportunities for implementation.

Step 3: Plan market entry

In order to realize the expected benefits of the chosen opportunities, you should create a market entry plan soon after their evaluation. You could involve your lead customers to confirm expected product acceptance. You should also draft an implementation plan, thereby preferably including some of the people who were involved in Step 1 (idea generation and opportunity scanning) so that they can continue working on the growth opportunities they identified.

Insights for the Executive

Many companies are leaving serious money on the table by ignoring accessible growth opportunities in adjacent market areas. Such opportunities arise from making smart new combinations of the company's existing technologies and markets. Especially when you are in a maturing business and/or offering intermediate products and services, opportunities for innovation by enhancement are abundant.

Compared to innovation by intensification (existing products within the existing customer base) and innovation by enlargement (totally new applications), the innovation by enhancement model has a relative low risk profile, low resource intensity and short time-to-cash. A process driven by the systematic search for unmet customer needs and an appreciation of your products' functional properties can lead to a plethora of commercially viable new offerings, contributing millions in net present value to your innovation pipeline.

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