

Opportunities for Action in Consumer Markets

A Disciplined Approach to Breakthrough Innovation

THE BOSTON CONSULTING GROUP



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Most major consumer-goods companies spend heavily on innovation—as much as 5 percent of sales. Truly innovative products create value for consumers, extend the category, generate higher margins, and strengthen the brand. Moreover, in an age of increasingly powerful retailers, innovative products boost companies' bargaining power for shelf space and retail displays.

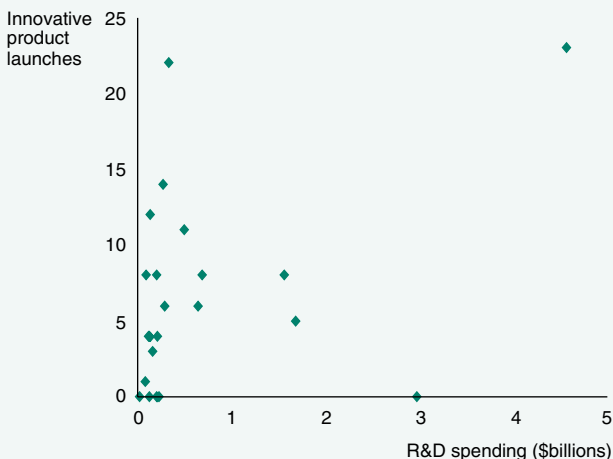
Yet for all the resources that companies pour into the innovation funnel, surprisingly few truly breakthrough products emerge at the other end. Over and over, we see pipelines clogged with inconsequential projects while potentially valuable ones expire for lack of resources. As a result, most product launches represent only minor variations on existing SKUs.

The remedy for ineffective innovation, however, isn't necessarily more spending. Indeed, when we analyzed more than 20 of the top packaged-goods manufacturers, we found that the total dollars they spent rarely correlated with the number of innovative products they launched (see Exhibit 1).

We define innovative products as those that offer consumers significant new benefits through advances in technology, formulations, or applications, or through more convenient packaging. Some companies may discover that they do need to increase their overall investment in innovation in order to achieve breakthroughs. But the first step for ensuring a consistent flow of innovative products is to understand why the current process is failing.

Exhibit 1. More Spending Won't Guarantee More Innovations

Performance at top packaged-goods companies from 1997 to 1999



SOURCES: Marketing Intelligence Service; company reports.

The Black Hole of Innovation Spending

In working with global companies to diagnose their innovation problems and rebuild their systems, we repeatedly encounter the same obstacles: weak portfolio management, clogged pipelines, “ghost” projects (flawed projects that won’t die), and fragmented resources. Refocusing a company’s efforts on solving these problems can yield far greater results than simply increasing spending.

Weak Portfolio Management. One fundamental cause of innovation breakdown is a lack of disciplined portfolio management. Although most companies distinguish core from noncore categories and brands, their innovation portfolios rarely reflect those priorities. At

one company, noncore brands accounted for roughly half of the past three years' product development projects. At another company, nearly one-third of all projects were authorized by brand managers three to four levels below the CEO. Because the brand managers didn't have a comprehensive view of consumers' needs or the company's priorities, the resulting portfolio failed to align with corporate strategy.

Such mismatches of resources and strategy nearly always point to a project initiation process that is not widely observed. In theory, most of the companies we have worked with had tracking systems that required estimates of investment and sales growth for each project. In practice, more than half the projects at these companies were initiated without such basic business justification. Disciplined portfolio management, which is how many pharmaceutical companies succeed with innovation, enforces crucial decisions and eliminates wasted effort.

Clogged Pipelines. Breakthrough innovations that deliver valuable benefits to consumers bring in tens or even hundreds of millions of dollars in *incremental* sales. But such growth requires more than minor SKU modifications or product-line extensions. Unfortunately, most product pipelines are clogged with "project sludge"—a backlog of low-return projects that are designed merely to tweak an existing product.

How does project sludge get into the pipeline in the first place? In most companies, incentive systems and short-term rotational programs reward a brand manager for initiating *any* project—regardless of its size or return on investment—during the manager's brief time in his or her position. As a result, managers feel enormous pressure to load the funnel with as many projects as possible. Several senior management teams

told us that they approved a list of 50 to 100 projects only to find one year later that there were three times as many projects in the pipeline.

At most companies, breakthroughs are expected to drive at least 60 percent of the organization's growth. We have found, however, that only 20 to 30 percent of the innovation investment in most companies is devoted to truly innovative projects. That gap represents a serious misallocation of resources.

Ghost Projects. Ailing projects siphon off valuable resources, but no one wants to be the executioner. That's why at most companies fewer than 10 percent of the projects active at the beginning of the year are killed by the end of the year, despite the fact that 30 to 40 percent fail to clear hurdles. Frequently, the champions of these lost causes take their pet projects underground or into the skunkworks to escape the hatchet. One R&D director described his company's innovation pipeline as being "haunted by ghosts—completely hopeless projects that refuse to die but continue to suck the lifeblood from healthy ones." To create organizational awareness of the use—and misuse—of resources, a pharmaceutical company we worked with instituted "liberation parties," at which employees celebrate the resources freed up by aborting a project.

Fragmented Resources. Companies with a glut of insignificant or ailing projects force their scientists and technicians to spread themselves thin, fragmenting their valuable time. At several consumer companies, we found that the average project received less than half of any scientist's time. That may be sufficient for a minor change in packaging or a new flavor or fragrance, but it will not drive significant innovation at the pace required today. Without dedicated resources to provide focus and continuity throughout

an innovation project, the time to market stretches out well beyond the best practice of 12 months.

Getting More from Each Dollar

Innovation is the future. It excites consumers and provides an outlet for creativity and insight. Companies that are dedicated to successful innovation and growth adhere to the following five principles.

Employ an investment portfolio approach. An objective portfolio-review process is essential for managing a successful pipeline. The goal is to have the right mix of line extensions, category improvements, and breakthrough ideas that will deliver consistent returns over several years.

Some companies create a senior-level, cross-functional portfolio review committee to ensure a good balance of projects. In most instances, this group's meetings can be tucked into other scheduled events to avoid bureaucratic delays. Such committees should include senior executives, who have the clout to make the inevitable tradeoffs among strategic priorities, resources, launch timing, and consumer and financial hurdles. Once the committee has approved a portfolio of projects, it can meet quarterly to review the competitive environment and other factors that may have changed since the last meeting. Many committees develop templates that help them make timely and informed decisions.

Revamp the innovation process. Great ideas are often hard to sell early on, and premature demands for numbers and analyses can kill creativity. Nevertheless, consistent breakthrough innovation is impossible without an explicit process of business justification, especially as an idea approaches the development

stages. The best process requires some justification at each stage of the project. Requirements at various stages might include

- consumer research to verify the market for an innovation
- consistent development and commercialization steps with well-defined timelines
- financial, operational, and consumer hurdles that are monitored consistently and unemotionally
- project postmortems to provide timely feedback

Such a process—if followed in a disciplined manner—will speed the development of the best ideas. And it will mercifully eliminate the doomed ones.

Marshal experience and cumulative knowledge. Most consumer companies have launched hundreds of products in recent organizational memory, yet the record of that experience is little more than anecdotal. An organization must record, track, and analyze its knowledge to reap the most value from it. Projects should not be allowed to move through the pipeline without thorough documentation that includes reports on consumer-testing methodology and results, investment and time allocations, and predicted versus actual sales. We recommend a database of project reviews to create a multiyear history.

Dedicate resources to breakthrough projects. Look behind the most valuable innovations and you are likely to find sufficient resources. Good innovators make sure their budgets are commensurate with the opportunity. They also dedicate full-time R&D and marketing staff to ensure that the focus remains on the breakthrough idea. Often these companies form

cross-functional “assault teams” that work on the project throughout the development and commercialization stages (see Exhibit 2). Such teams, whose members may change as the project progresses, are usually led by an R&D or marketing person.

Leverage external partnerships. Increasingly, external partnerships are essential for speed, economy, and success. R&D departments need to develop relationships with vendors that rise to the level of collaboration. With such arrangements, new technical capabilities can incubate over time without substantial resources.

Getting Results

Companies that revamp and refocus their investment in innovation have demonstrated surprisingly dra-

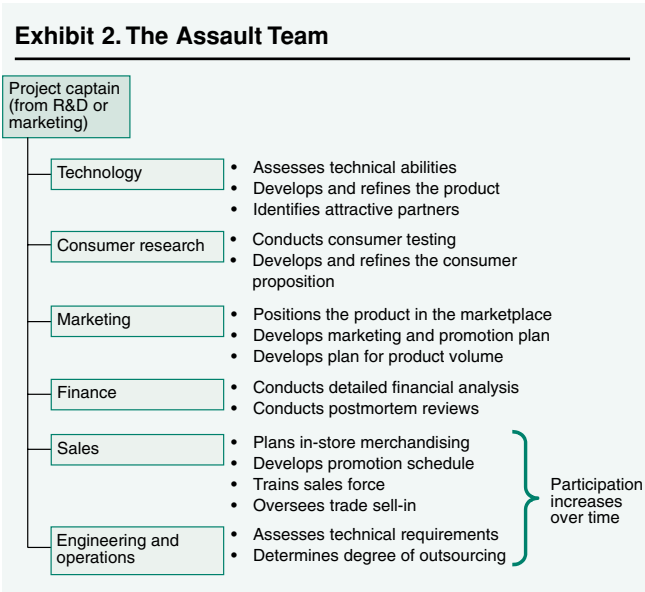


Exhibit 3. The Results of Refocusing Innovation

Improvements at major packaged-goods companies within 18 to 36 months

Metric	Before		After
Number of active projects	200–350	➡	125–175
Percentage of innovation budget devoted to breakthrough projects	20–30%	➡	35–50%
Development time for new products	18–26 months	➡	12–16 months
Number of breakthrough product launches per year	0.5–0.7	➡	1–1.2

SOURCE: The Boston Consulting Group.

matic improvements within 36 months—and many within half that time (see Exhibit 3). What follows is a short list of questions, amounting to an instant audit, to help your company get started on its own innovation revival.

- How many truly breakthrough products have you launched in the past five years? We define a breakthrough product as one that generates incremental sales that are greater than 1 percent of a business unit's total sales.
- How many active projects are in the pipeline? What is the average commitment of scientists' time to each project?
- Are there clear points at which appropriate metrics and reviews are required?

- How many projects failed to clear the hurdles in the past year? How many of these projects were actually killed?
- What proportion of your innovation dollars is devoted to breakthrough projects rather than line extensions?

The answers may surprise you. The lesson will be clear: before throwing more dollars into the innovation process, make sure your company is achieving maximum returns on its current investment.

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