
Strengthen Your Innovation Capabilities to Drive Performance
BEGIN READING

INTRODUCTION

Organizations invest enormous resources to strengthen their capabilities and capacity to innovate but are often disappointed by the results. Consider the recent case of a global bank that committed publicly to increasing the volume, speed and quality of innovative ideas in its pipeline. A centerpiece of this initiative was the launch of a companywide "hackathon" that engaged thousands of employees in spontaneous idea generation, shaping and evaluation, facilitated by outside consultants and an expensive piece of idea management software. Employees were excited about the opportunity to contribute their ideas, and leaders had high expectations that it would stimulate a vibrant "culture of innovation."

One year later, not one of the ideas had been implemented, and the culture, instead of being more engaged in innovation, was more cynical about it. When the organization assessed what went wrong, it found a lengthy list of causes. Everyone had their own interpretation of what an "innovative idea" looked like, leading to a diverse mix of suggestions, many of which were incongruent with what the leadership team really wanted.

Another challenge stemmed from a lack of defined standards for innovation. For example, there was no clear definition about what constituted a "good idea" or even a "complete idea," making it hard to compare one idea against another. Other issues were deeper, such as the lack of clarity on what strategic priorities should be used to evaluate submitted ideas or what the governance model would be for conducting these evaluations. Most fundamental of all were unanswered questions related to resource allocation. *How would the organization fund prioritized ideas? Who would work on them? And what would the organization have to stop doing to make this possible?*

There are comparable failure modes in other common corporate innovation initiatives (see figure 1). Incubators or new-growth teams stumble because the connection to strategy is unclear or because the process, metrics, funding mechanisms and people involved are more suited to the near-term needs of the core business than to longer-term, more transformational opportunities. Corporate venture capital or innovation funds disappoint because leaders, in the absence of appropriate goals and metrics for success, pressure it for short-term financial results. Innovation training or coaching programs leave participants with new skills and tools they cannot

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implement because of management resistance or lack of integration with broader company processes. Lean startup sprints hit a brick wall when promising ideas attempt to transition to a business unit (BU) where they can be resourced and scaled. The appointment of a "chief innovation officer" to the corporate center (outside of the profits and losses) leads to organizational confusion around where the decision-making power really sits to resource innovation.

The problem is not that these interventions are intrinsically bad ideas. On the contrary, each can play an important role. Rather, the problems arise when they are implemented without a full consideration of the broader set of enablers that must be in place for any individual initiative to be successful. In other words, building an innovation capability is a systems design challenge that requires a system solution; if instead you try to build it by cobbling together isolated point solutions, each is likely to fail in entirely predictable ways.

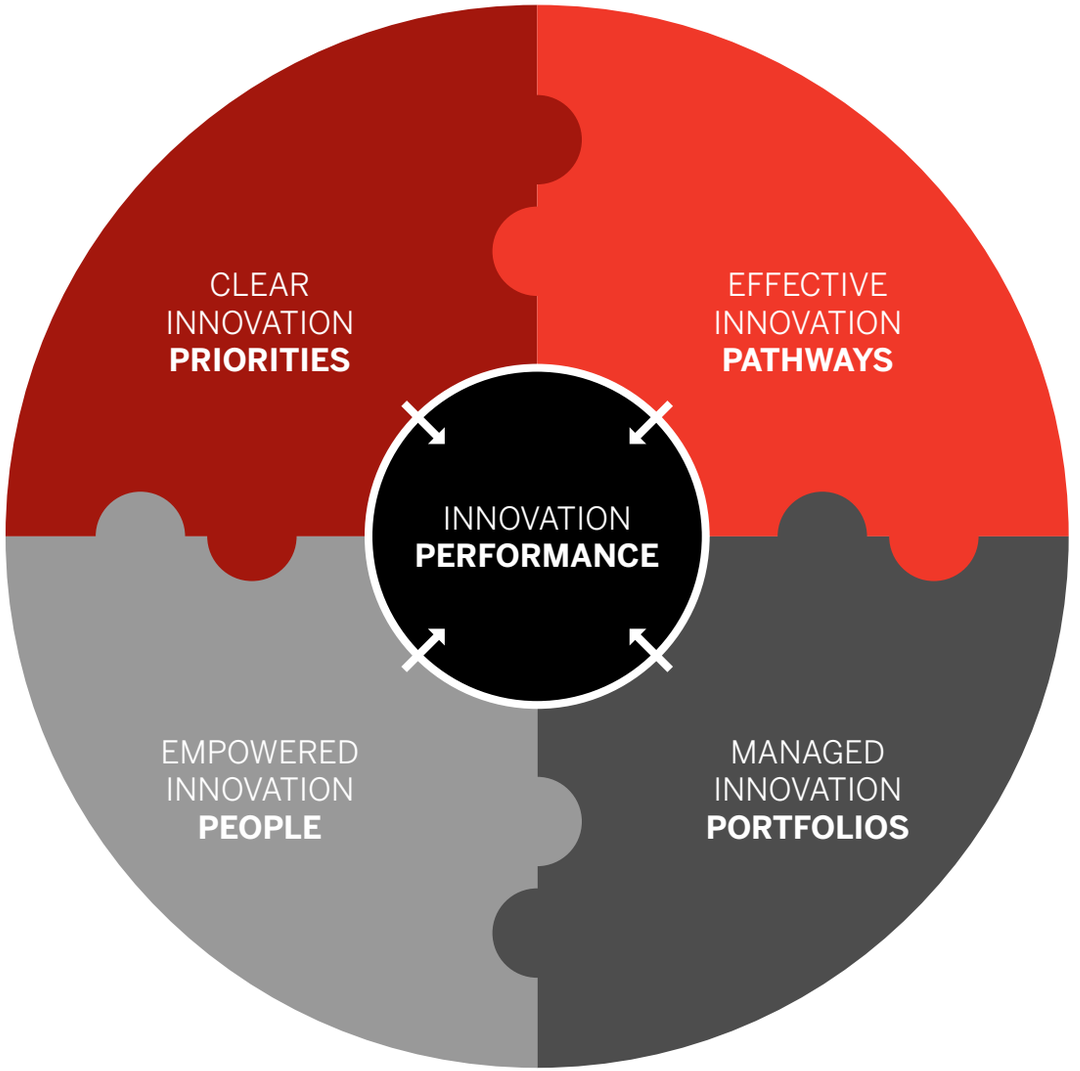
Figure 1. Innovation Initiatives Fail for Predictable Reasons

Common Innovation Initiatives	Predictable Failure Modes
Develop an Innovation Strategy	Misalignment between enterprise strategy and innovation strategy leads to a portfolio of ideas that are never prioritized for meaningful investment and scaling.
Run a Hackathon	No appropriate governance to oversee decision making and resource allocation means great ideas have nowhere to go or are inconsistent with strategic priorities.
Create an Inovation Fund	Leaders put pressure on funds to be reallocated toward core initiatives with clearer short-term return on investment (ROI).
Build an Innovation Team	Flawed interaction model between the innovation team and the core business results in the team getting sucked into incrementalism or pursuing opportunities that are ultimately rejected by the business
Implement Lean Startup Sprints	No mechanisms to transition the post-sprint projects into business units
Build a Culture of Innovation	Underlying beliefs about what it takes to be successful create resistance to behavior change, leading to increased cynicism about the organization's ability to innovate.
Appoint a Chief Innovation Officer	Organizational confusion and frustration are created when the new role isn't clearly integrated into strategy and resource allocation decisions.

To address this, leaders need a model to help them understand the components of a well-functioning innovation system, how they fit together and their connections to the rest of the organization. In this e-book, we introduce the innovation performance model (fig. 2), which can be used to map an organization's current approach to innovation, assess what's working well and identify areas for improvement. This, in turn, can help leaders to strengthen their own systems for innovation, building on the foundations already in place.

The innovation performance model describes the five primary components of a complete innovation system — performance, priorities, pathways, portfolios, people. The model is best understood by considering each "P" individually, including the unique role it plays, the enablers that comprise it and how it relates to the rest of the system.

Figure 2. The Innovation Performance Model



Component 1: Innovation Performance

Innovation should always be a means to an end, not an end in itself. These goals will vary from one organization to the next, but defining them clearly is a precursor to building the right capability and being able to measure its effectiveness. For this reason, innovation performance is at the center of the model.

Specifically, an organization must clarify and align on two types of performance for innovation:

- **Desired performance outcomes** corresponding to the business results the organization is trying to achieve from innovation.
- **Leading system indicators** that help the organization assess if it's on track to achieve those results.

Desired Performance Outcomes

There are a range of business results innovation can support, and organizations typically innovate for more than one reason. Common examples include business growth, enhanced efficiency, improved culture, reduced environmental or social impacts, and strengthened brand perceptions (fig. 3).

Figure 3. Common Examples of Innovation-Supported Business Outcomes

GROWTH	EFFICIENCY	CULTURE	ESG	BRAND
Growing current businesses, creating entirely new sources of growth or improving the valuation multiple by changing the business mix	Reducing costs, innovating internal processes or changing the business model to drive greater efficiency and higher margins	Finding ways to drive greater employee engagement, satisfaction or participation in enterprise innovation systems	Reducing negative environmental or social impacts via corporate governance (ESG), or pursuing new ways to strengthen local communities	Strengthening the perceptions of customers, employees and analysts of your organization's commitment to and effectiveness at innovation

The leaders of a global financial services firm, for example, sought to proactively clarify the desired outcomes from their innovation program. The list reflected the different vantage points of the leadership team:

- The chief executive officer (CEO) wanted to increase the enterprise valuation by a significant multiple over the next decade, primarily via an increase in the organic growth rate.
- The chief financial officer (CFO) was looking to allocate capital in a more strategic and thoughtful way by having more visibility into the vast pipeline of innovation projects.
- The chief human resources officer (CHRO) was interested in creating a stronger culture of innovation to make the organization more attractive to current and potential employees.
- The business unit president wanted to increase the speed to market of innovative new products and services.
- And the chief operating officer (COO) aimed to enable high-potential innovation projects to be quickly scaled globally.

Each outcome was translated into a measurable key performance indicator (KPI) to track and assess the performance of the innovation system. These metrics also served as a guide for where leadership should focus efforts to further strengthen the system.

Leading System Indicators

Leading system indicators can be used to evaluate, on an ongoing basis, if the system is running effectively. To identify appropriate metrics, it is helpful to work backward from the desired performance outcomes by asking "What must be true to know the organization is on track to achieve them?

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As an example, the aforementioned financial services firm had set a goal of achieving a 10% revenue compound annual growth rate within two years. Some analysis revealed how much of this growth they could expect from expansion of existing products and services, how much needed to come from mergers and acquisitions (M&A), and how much needed to come from as yet unidentified new products and services. This latter target became a performance outcome — desired growth from completely new products and services.

This suggested a number of possible leading system indicators that could be used to answer the question "Are we on track?" including:

- The expected value of the pipeline.
- The number (and approximate size) of projects.
- The rate at which new ideas must be added to the pipeline.

Regardless of the specific metrics tracked, teams must be careful to focus on the few that matter and avoid the twin traps of metric proliferation (tracking too many metrics simultaneously) and vanity metrics (tracking easily achievable measures that deliver a false sense of progress).

DIAGNOSTIC QUESTIONS FOR LEADERS

Innovation Performance

Use the diagnostic questions at the end of each section to evaluate your organization's innovation maturity and identify opportunities for improvement.

DESIRED PERFORMANCE OUTCOMES

Have we defined and aligned our organization on the business outcomes we need innovation to achieve and the KPIs that we will use to measure success?

LEADING SYSTEM INDICATORS

Have we identified the activities that lead to the innovation performance outcomes and the corresponding KPIs we'll use to measure them?

Component 2: Clear Innovation Priorities

Once innovation performance has been clearly defined, the next step is to clarify the organization's innovation priorities. Placing constraints on innovation might seem counterintuitive, and indeed there has always existed a natural tension between innovation and focus; one seeks to go beyond boundaries, the other to establish them. Tuning this tension to the right level is the key to innovation productivity.

We often hear managers assert they do not want to constrain their innovation teams. However, our experience suggests the highest-performing teams are those that are given "just enough focus" to ensure they work on the most valuable ideas, while still giving them ample flexibility to explore creative new approaches to achieving that impact.

The word "innovation" means different things to different people, so the first step in defining organizational priorities is to clarify the types of innovation the system should produce.

Clear innovation priorities require:

- **A Common innovation language** that ensures everyone in the organization understands what types of innovation are being pursued, and why.
- **Strategic focus areas** that guide innovators towards problems aligned with the organization's strategy.
- **Clear innovation boundaries** that provide further clarity as to what types of innovation are most desirable and, just as important, what the boundaries are.
- **Dynamic priority management** to ensure priorities adapt over time in response to changing customer needs or competitive threats.

Common Innovation Language

The word "innovation" means different things to different people, so the first step in defining organizational priorities is to clarify the types of innovation the system should produce. There will inevitably be more than one kind that is strategically important for any organization, and therefore, it is essential to define — with precision — multiple, distinct innovation types.

While these will vary across industries and companies, common examples include:

- **Core or sustaining innovation:** Strengthen and grow the existing business (e.g., each successive generation of the smartphone being brought to market by companies like Apple or Samsung, or the recent development of "curbside pickup" offered by grocery stores).
- **Transformational or business model innovation:** Address a new customer demographic or need and require a different business model than the core business. This innovation type is characterized by a significantly higher degree of uncertainty and risk and therefore must be pursued in a different way (e.g., the migration of many media companies like Disney, CBS and even Microsoft from traditional distribution toward recurring-revenue models).
- **Efficiency innovation:** Reduce internal costs by leveraging technology or streamlining processes (e.g., implementing robotic process automation).

This is not an exhaustive list, and it is not uncommon to see organizations define other innovation types focused on new technologies, customer experiences or even time horizons. Regardless, clarifying precisely what innovation means in the organization has a number of benefits, including:

- Ensuring everyone understands exactly what leaders mean when they talk about "innovation," thereby avoiding the often rampant confusion that accompanies calls for more of it.
- Acting as a fundamental input into the design of your system (e.g., if transformational innovation is important, the business needs the capabilities to pursue it).
- Helping employees understand their own role in supporting it.

Figure 4. Innosight's Strategic Focus Area Framework

Strategic Focus Areas

We often hear concerns that an organization's innovation pursuits are not aligned with its strategy. To address this, it's helpful to define strategic focus areas (SFAs) that provide the right balance of focus and flexibility needed for innovation. An SFA is analogous to a "fishing hole" where you'll look for high-value innovation opportunities (the "fish").

We define an SFA by answering four questions (fig. 4):

- Who is the target customer?
- What priority problem or "job to be done" will we solve for them?
- How will we solve this job (i.e., with what general type of solution or capability)?
- Why is this strategically attractive, and why do we have the right to win? (Answering this question is what turns a potentially interesting focus area into an SFA.)

Well-constructed SFAs share a number of characteristics. They are:

- Connected to an explicit point of view about the future environment in which the company expects to compete, and where it believes it can win.
- Focused on the priority customers' jobs to be done that define the opportunity area rather than specific solutions (e.g., "enable transportation" vs. "build trains").
- Large enough to contribute meaningfully to future growth.
- Broad enough that a portfolio of projects (perhaps across multiple regions or even business units) can be developed (rather than just individual projects).
- Sufficiently constrained that an innovation team searching for opportunities within this space can anchor to a specific set of customers or customer problems.

A retail bank, for example, identified an SFA related to helping freelancers (i.e., "gig economy" workers) overcome the challenges of unpredictable incomes (e.g., lack of paperwork such as a W-2 or 1099) to borrow money in order to finance large purchases (e.g., a car or a house). This SFA neatly satisfies each of the criteria above. It is consistent with the strong point of view held by the bank's leaders about the rise of the gig economy and their conviction that this customer group was large, growing and increasingly dissatisfied with existing solutions. It focused on a relatively specific job to be done (buying a car or a house) — an area where the team felt there was plenty of scope for innovation. However, the SFA is not so focused that the team would be constrained in its pursuit of a solution, but it is focused enough that it would be very clear where the team might start the process of customer discovery.

Clear Innovation Boundaries

Consider the challenge faced by an innovation team inside a global logistics company. The team had diligently pursued an innovative new product concept for 12 months in an agreed-upon focus area. After receiving steady encouragement from midlevel and even senior-level executives, it finally reached a decision point at which a significant investment was required to proceed further. It was at this critical juncture that the case was brought to the CEO for signoff.

As soon as the CEO realized what was being proposed, the project was swiftly stopped — not because the idea was a bad one but because he believed the new service offering would create confusion in the mind of the customer and, worse, the potential for cannibalization. This project could have been shut down within weeks of being conceived, saving months of time and investment, if the organization had defined clear boundaries for innovation, including the types that were desirable, discussable or out of bounds.

Figure 5. Goals and Bounds Table to Capture Project-Level Constraints

Goals and Bounds Per Project	DESIRABLE	DISCUSSABLE	OUT OF BOUNDS
FINANCIAL CHARACTERISTICS	• Financial evaluation on a project-by-project basis • Clear path to profitability in <5 years • $30M to $400M gross revenue while building prioritized capabilities • 30% gross margins	• Clear path to profitability requiring a 5+ year time horizon	• Projects without a clear path to profitability
RELATIONSHIP TO CORE	• Complementary	• Disrupts core strategy	• Dismantles core strategy
ROLE OF M&A	• Organic growth • Technology acquisition • Talent-driven acquisition • <$250M	• Inorganic with organic potential • Niche vertical acquisition (e.g., e-commerce, fresh, healthcare) • $250 to 500M	• Inorganic: small to midsize competitor to boost gross revenue • >$500M
TYPE OF OFFERING	• Same industry vertical as core business • New or expanded entity	• Industry adjacencies • Consulting, financial solutions	• Nonadjacent industry verticals
PROFIT MODEL	• Subscription/maintenance • Fee-based platform	• Transaction; cost-plus • Bundle, value-add service • Subsidized offerings	• Managed services/head count
GEOGRAPHY	• Developed markets (e.g., America, Europe, North Asia) • Later-stage developing markets (e.g., Indonesia)	• Early stage developing markets (e.g., Africa)	• All others

Figure 5 illustrates one approach to capturing innovation boundaries: a "goals and bounds" table. Each row represents a different dimension against which an individual project might be assessed, and the columns define "desirable," "discussable" and "out of bounds" project attributes. Defining these values in advance of embarking on multiple initiatives helps align all stakeholders and reduces the likelihood of discovering too late that a project might violate an unwritten rule.

Dynamic Priority Management

Together, strategic focus areas and clear innovation boundaries help align leadership and innovation teams by clarifying expected outcomes and providing guardrails to help the team realize if they are straying from the path. However, they are not static, single-use documents but dynamic tools that should evolve over time to reflect the necessary changes in leadership priorities. As such, they must be owned and managed by a corporate or business unit team (typically strategy or innovation), refreshed as a part of annual strategic planning efforts, or updated based on external market triggers or other early warning mechanisms.

DIAGNOSTIC QUESTIONS FOR LEADERS

Clear Innovation Priorities

Use the diagnostic questions at the end of each section to evaluate your organization's innovation maturity and identify opportunities for improvement.

COMMON INNOVATION LANGUAGE

Have we precisely defined the distinct types of innovation we must pursue to execute our strategy? Does everyone in the organization understand these types, their rationale and whose job it is to pursue them?

STRATEGIC FOCUS AREAS

Have we defined the strategic focus areas for our innovation efforts? Are all current innovation projects tied to our strategy in a clear way?

CLEAR INNOVATION BOUNDARIES

Have we quantified how much of each type of innovation we need to reach our goals? Do we have clarity on what types of innovation projects are desirable, discussable or out of bounds?

DYNAMIC PRIORITY MANAGEMENT

Do we have a way to update our innovation priorities regularly based on changes in our environment or strategy?

Component 3: Effective Innovation Pathways

An innovation pathway is the set of steps an innovation takes from initial idea to implementation. Innovation pathways exist in all organizations and can be formal, informal or somewhere in between. The key is to ensure all pathways are intentional, explicit and optimized to the type of innovation they are intended to produce. Specifically, effective innovation pathways require:

- **Explicit pathway architecture** to ensure each type of innovation the organization needs is supported by the system.
- **Optimized pathway operations** that incorporate best practices customized to each type of innovation.
- **Constructive pathway governance** to ensure innovation projects receive the right types of support through funding, access to talent, and the appropriate level of oversight.

Explicit Pathway Architecture

Many organizations design explicit pathways for different types of innovation. For example, a global chemical company has formalized a "step out" process, designed to manage the uncertainty of introducing a new process innovation into the standard operating procedures of large chemical plants.

Another organization customized its implementation of the Lean innovation process, while yet another established a tailored new product development (NPD) process. Some organizations build custom pathways by combining different best-in-class tools (e.g., Amazon's press release and frequently asked questions (PRFAQ) and the business model canvas combined with milestone-based funding models).

Pathways can extend to include open innovation and customer cocreation models as well as corporate venture capital and new growth incubators (e.g., the German software company SAP has a set of pathways that define how it engages with customers and startups through its SAP.iO unit, the various SAP.iO Foundries, and their account team that cover various industries and markets). In short, any time there is a desire to invest resources in bringing an innovation to market, a pathway will emerge to make it happen.

The following figure (fig. 6) depicts one pathway an organization defined for business model innovations. It was built on many best practices that already existed in different parts of the organization but was further customized to reflect the discovery-driven nature of this type of innovation. By establishing a standard approach

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that everyone could use, it enabled better coordination of global and regional pipelines, better allocation of resources, and best practice sharing across the organization.

Optimized Pathway Operations

These real-world examples of pathways are typical of those found in many organizations. However, the actual pathways that innovations take to get from initial idea to market are often very different. It is not uncommon to discover that

Figure 6. A Defined Innovation Pathway for New Business Model Innovation

	Spot Opportunities	Design Solutions	Test, Learn and Adjust		Scale	
			Test and Learn	Pilot	Growth	Efficiency
OBJECTIVES	Identify a customer problem worth solving	Detail solution that best solves the problem	De-risk assumptions with select customer(s)	De-risk assumptions across foothold market	Scale solution for growth	Drive efficiency at scale
KEY ACTIVITIES	• Ecosystem analysis • Customer jobs interviews • Quick-hit financial and strategic analysis	• Design thinking ideation sessions • Business model and use case development • Concept testing • Assumption prioritization	• Test design and execution • MVP development, testing and pivoting • Synthesis of test learnings	• Pilot with expanded customer group in foothold • Business case development • Scaling plan development	• Market expansion • Develop go-to-market capabilities • Operating model design and decision rights	• Identification of major cost drivers • Optimization and/or redesign of processes and structures
METRICS TO TRACK	• Priority job to be done • Market size and potential • Strategic value	• Complete business model design • Customer feedback on concept • Business model assumptions	• Customer validation that solution addresses priority job • Solution feasibility	• Customer adoption • Technical issues for growth resolved • Business case profitability	• Revenue (growth) • Sales pipeline value	• Margin improvement • Earnings before interest and taxes (EBIT) growth
STAGE GATE EXIT CRITERIA	Priority job to be done identified with high value for the company	Business model with assumptions identified	Deal-killer assumptions de-risked and/or business model pivoted	Growing adoption of business model in foothold with conceivable profitability at scale	Line of sight to revenue targets at scale	Line of sight to margin targets at scale

high-value innovations resulted from ad hoc, informal and even hidden pathways that succeeded in spite of the organization's best attempts to bring discipline and repeatability to the process. This observation fits neatly with the concept of the frequently maligned "innovation theater," in which superficial best practices are overlaid on existing governance and resource allocation systems with the expected results.

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For an organization to repeatedly bring new ideas to market with speed and capital efficiency, it is insufficient to have a documented, formal innovation process. In addition, businesses must develop a comprehensive understanding of how innovation actually gets done, inclusive of both formal and informal mechanisms, and optimize pathway operations accordingly. It can be helpful to begin this process by answering honestly the following questions:

- How do ideas get identified and selected?
- How do resources (people, capital, functional resources, leadership attention) get allocated?
- How are ideas supported as they progress from idea to implementation?
- Where do ideas get stuck?

While formal processes are often what organizations point to when asked why they are successful, it is often the informal activities, relationships and support structures that prove most critical to success. Common patterns emerge as companies map out the actual pathways their innovations follow, some of which are effective and some of which are not. The following table (fig. 7) highlights some of the most common pathway patterns we have seen, which fall in the latter category.

Figure 7. Common, Ineffective Pathway Patterns

PATHWAY PATTERN	SYMPTOMS	ROOT CAUSE
DARK PATHWAY	New products or services frequently struggle to gain traction with customers.	Strong solution bias, reinforced by leaders asking the wrong questions, results in teams overly focused on product development and testing at the expense of building empathy for customers and their underlying jobs to be done.
SILENT PATHWAY	The team seems to charge headlong into mistakes that were easily predicted by outsiders.	Overconfidence bias, combined with the lack of a learning-oriented operating model, and inadequately trained leaders allow the team to execute vs. discover.
ROAD TO NOWHERE	Projects get shut down the moment they become visible to leadership.	Lack of clear innovation priorities allows projects to proceed that are misaligned with strategy, violate implicit third rails, or are just too small to matter.
TOLLBOOTH HIGHWAY	Slow progress and long delays in getting approvals and resources to proceed	Poor innovation governance and core-biased support models create unnecessary bureaucracy and significant opportunity costs for innovation teams who need to move quickly.
PAPER TRAIL	Slow progress and burdensome meetings and material preparation	Poorly designed innovation governance and leaders focused on the wrong metrics result in teams spending too much time on activities unlikely to create value in discovery-focused pathways.
SPAGHETTI JUNCTION	Balls get dropped during the transition from one project owner (e.g., a research and development lab) to another (e.g., business units).	Insufficient clarity in pathway definitions and ownership combined with a weak link to business unit strategy results in a lack of clarity around ownership, objectives and resourcing.
UNDERGROUND TUNNEL	Lack of visibility into progress. The project will fail if the sponsor leaves or moves into a new role.	Inadequate innovation governance and lack of portfolio visibility results in projects that are “hidden” and depend on the support of individual leaders.

Mapping an organization’s real pathways provides a clear view of what is truly driving progress against performance outcomes (e.g., pipeline throughput or pipeline value) — information that can feed directly into the design of optimized pathway operations.

Constructive Pathway Governance

Even the best-designed pathways can still fail to get results. When this happens, the cause is often related to ineffective pathway governance (e.g., how innovation project teams are organized and led, how leaders engage with these teams, the protocols for how other parts of the organization get involved, and how resources are allocated to individual projects).

Constructive pathway governance requires senior leaders to recognize that many of the processes set up by the organization to manage risk or create efficiencies in the core business are wholly inappropriate when applied to higher-risk opportunities. Even if well intentioned, they often increase the burden (and slow down the pace) of the innovation team to the point that the strategic risk of inaction far outweighs any risks inherent in the proposed action.

Indeed, the previous figure highlights that at least three of these common pathway patterns are caused by governance issues. High-performing organizations take a systematic approach to adapting inefficient processes and, where needed, create new processes (often as simple as direct access to a key functional team member in the appropriate human resources or legal team) to ensure teams have appropriate and timely support.

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DIAGNOSTIC QUESTIONS FOR LEADERS

Effective Innovation Pathways

Use the diagnostic questions at the end of each section to evaluate your organization's innovation maturity and identify opportunities for improvement.

EXPLICIT PATHWAY ARCHITECTURE

Do we have explicit and distinct pathways for each type of innovation we need to pursue? Do we understand how innovation really happens today in our organization? Do we have "invisible," informal or dysfunctional pathways that are hard to replicate, measure or manage? Do we have standards for innovation across the organization, so everyone is using the same language and, where appropriate, the same approach (e.g., common definition of stage gates, exit criteria)?

OPTIMIZED PATHWAY OPERATIONS

Do our pathways adhere to best practices to ensure customer-focused, hypothesis-driven, and agile approaches to idea development and pursuit? Do pathways for distinct types of innovation reflect the distinct best practices for each type?

CONSTRUCTIVE PATHWAY GOVERNANCE

Are our pathways carefully connected to supporting functions (e.g., information technology, legal, human resources) such that they get the support they need without being bottlenecks? Do our leaders empower, protect and ask the right questions of our innovators? Are our higher-risk pathways clearly linked to milestone-based funding?

Component 4: Managed Innovation Portfolios

One of the biggest challenges in a large organization is the need to manage not just individual innovation projects but also the aggregate portfolio of projects. After all, it is this collective set of projects, drawing from the same pool of resources, that together will achieve the organization's desired performance outcomes. This means leaders need visibility into these portfolios so they can answer management questions about them, strategically balance resources across them and manage them dynamically over time.

Managed innovation portfolios require:

- **Strategic portfolio plans** to ensure leaders are focused on the most critical projects that need to be assessed and managed, not just individually but collectively.
- **Actionable portfolio insights** that ensure leaders have ongoing visibility into portfolio-level performance and can use this knowledge to make strategy and resource allocation decisions.

- **Integrated portfolio management** to ensure portfolio considerations are built into the core operations of the organization.

Strategic Portfolio Plans

Before organizations can manage innovation as a portfolio, leaders must first clarify which innovation projects and portfolios are strategic to track and manage. This will depend on the specific industry and company context.

For example, one organization's CEO proposed an aggressive goal that would require the entire organization to significantly increase the rate of revenue growth and sustain it for a multiyear period. Given this objective, the organization decided to define a single innovation portfolio that included the most critical growth-oriented projects at the enterprise level, appropriately labeled "the growth portfolio."

Other organizations identify multiple strategic objectives, each of which gives rise to a managed portfolio. For example, a large software firm defined portfolios for new growth, customer experience improvement and efficiency — each with clearly defined performance outcomes (new revenue, improved net promoter score, and cost reduction, respectively), against which the portfolios would be evaluated.

In most cases, a portfolio typically includes no more than 20 to 30 initiatives, each significant enough to contribute to the achievement of the strategic objective it supports. Leaders should align on inclusion criteria for each portfolio and create a plan that considers:

- Desired types of innovation (e.g., core versus adjacent versus transformational).
- Significance thresholds (e.g., revenue potential, magnitude of resource allocation).
- Initiatives that can be pursued organically versus through M&A.
- Operating expenses versus capital expenditure thresholds.
- Business units and geographies.

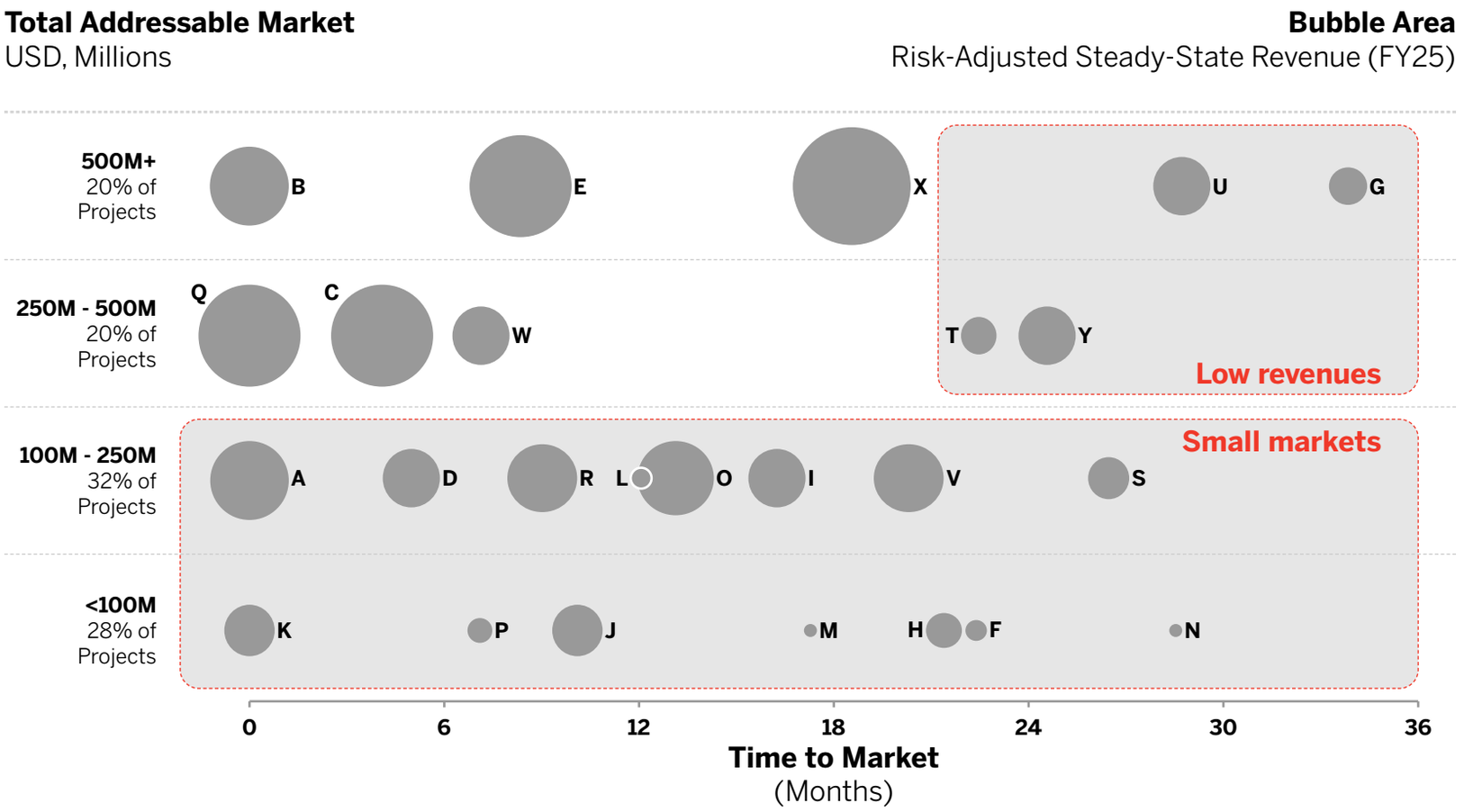
Actionable Portfolio Insights

Once defined, leadership teams should regularly review their strategic portfolios and use the insights to make decisions about portfolio composition and resource allocation. There are three central questions to discuss in these reviews:

1. Are we doing too much, too little or the right amount of innovation?
2. Are we doing the right kinds of innovation?
3. Have we optimized how resources are allocated to innovation?

To support these conversations, it is helpful to develop multiple "portfolio views" that provide insights from different vantage points. The following figure (fig. 8) provides an example of such a view that helps answer the question "Are we doing enough?" This type of view helps leaders quickly identify redundancies or projects that might be consolidated around a single platform while tracking (and communicating to investors) revenue from new products and services.

Figure 8. Example Portfolio View to Address the Question "Are We Doing Enough?"



In many organizations, the simple act of creating visibility into the pipeline creates a huge amount of value by helping executives understand where projects and investments are focused and start to connect the dots between individual projects and broader strategic priorities.

Integrated Portfolio Management

When leaders conduct a one-time analysis of an innovation portfolio, it can be an incredibly powerful tool to drive discussions about long-term growth and resource (re)allocation to support strategic goals. In extreme cases, some leadership teams have discovered up to 30% of their portfolio was being invested in projects that were likely to never see the light of day and could immediately be shut down. Other leadership teams have identified a billion-dollar "hole" in their portfolios, recognizing the need to start investing differently to achieve their aspirations for long-term growth.

However, the real value in portfolio management comes from integrating portfolio views with the existing strategy and resource allocation functions of the business. The most advanced organizations work to systematically include portfolio views into quarterly business reviews and upfront conversations during strategic planning to ensure leaders are making informed decisions about how best to invest to drive growth.

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DIAGNOSTIC QUESTIONS FOR LEADERS

Managed Innovation Portfolios

Use the diagnostic questions at the end of each section to evaluate your organization's innovation maturity and identify opportunities for improvement.

STRATEGIC PORTFOLIO PLANS

Have we precisely defined the innovation portfolios we want to measure and manage? Have we clarified the strategic imperatives against which we will assess the quality and health of our innovation portfolios, including the appropriate KPIs?

ACTIONABLE PORTFOLIO INSIGHTS

Do we have visibility into all the innovation projects in these portfolios? Are we able to ask the right strategic questions of our portfolios? Are we doing enough innovation? Are we doing the right kinds of innovation? Are we resourcing innovation efficiently?

INTEGRATED PORTFOLIO MANAGEMENT

Are portfolio insights part of our leadership and governance conversations (e.g., strategy planning, quarterly business reviews, capital allocation)? Do we evaluate resourcing for individual projects based in part on their impact on the overall portfolio? Do we have mechanisms to assess and balance resource allocation across core and noncore initiatives?

Component 5: Empowered Innovation People

The people component of the innovation performance model falls last, not because it is the least important but because understanding it requires familiarity with the system components previously introduced. Most discussions of the human side of innovation focus on the specific skills, mindsets or behaviors individuals need to be innovative or the corresponding features of an innovative culture. These are certainly important to understand, but if an organization fails to implement all the other components of the innovation performance model, even the most talented innovators can experience frustration.

Without clear priorities, employees may expend energy on nonstrategic efforts that are ultimately sidelined or stopped. Without clearly defined pathways, even the best ideas run the risk of being mismanaged. Without the ability to manage innovation portfolios, great ideas may get overlooked or underfunded while less attractive opportunities get access to capital on a first-come, first-served basis. Strong talent can often compensate for failures within the rest of the innovation system, but this is not a long-term solution as it can lead to burnout as well as morale and retention issues.

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Organizations can sustainably empower their innovation people by investing in:

- **Effective innovation talent** enabled by approaches to hiring, staffing, development, and performance management specifically tailored to innovators.
- **Inspiring innovation leaders** who role model innovation skills and behaviors that are explicitly defined and supported by development programs and incentives.
- **A Supportive innovation culture** that helps innovation practitioners and leaders achieve their goals.

Effective Innovation Talent

Several years ago, a global logistics provider developed its growth strategy and implementation plan, which included the establishment of a dedicated group to pursue new business models outside the core along with a new pathway optimized to the greater uncertainty inherent in this type of innovation. A number of talent-related questions quickly arose, including:

- Should we recruit internally to fill these roles?
- What type of skills and experiences should we look for?
- How should we manage and create incentives for the team?

While these are typical human resources (HR) questions, organizations often struggle to answer them when it comes to innovation talent. For example, it may be unclear what experiences and skills best serve people in innovation roles, leading to inconsistent hiring practices and "blind spots" in organizational capabilities or, worse, placing experienced high performers into unsuitable roles. Organizations also often lack appropriate recruiting mechanisms to find the right types of people to address capability gaps within the organization, leading to systemic biases that inhibit innovation. In businesses that struggle with these challenges, some high performers may simply choose to leave, driving up involuntary attrition rates among those valuable employees.

Organizations that are successful at attracting and nurturing innovators are explicit about how they support them at every stage of the employment life cycle. These organizations:

- Develop clear job descriptions calling out the required experiences and behaviors candidates need to be successful.
- Utilize recruiting mechanisms to identify potential employees from an appropriately diverse set of backgrounds.
- Adopt assessment mechanisms that correctly evaluate relevant prior experiences.
- Define career paths for innovators.
- Develop a portfolio of learning and development programs to ensure all innovators have access to the support they need.
- Think holistically about performance management.
- Modify existing approaches to reflect the nature of the roles that innovators are being asked to play.

Inspiring Innovation Leadership

In many organizations, inspiring innovation leadership is arguably the single most important element to get right. The research shows that inspiring leaders are made, not born, and organizations must work carefully to ensure that leaders in the most critical positions are empowered to inspire their teams.

While there are many traits often attributed to inspiring leaders, there is one that rises to the top — the most inspirational leaders model the behaviors they expect of their teams not because the performance management system creates incentives for them to do so (although it should) but because they have firsthand experience and deeply felt conviction about why those behaviors are essential for success.

They also clearly communicate innovation priorities to their teams not because they must but because they embrace the underlying assumptions the organization has made about where — and how — growth and innovation will occur. In turn, they integrate those assumptions and priorities into their communications and actions. They commit resources to those priorities because they have conviction in those priorities and understand that innovation success requires learning and patience.

It is the job of business leaders and their HR partners to nurture innovation leaders who can then inspire the rest of the organization. Organizations do this, in part, by recruiting leaders who demonstrate the underlying capabilities to be successful.

Even more importantly, they support internal leadership development activities (both formal and informal) by focusing on opportunities to create executive alignment. When leaders have a deep understanding and conviction about the need for innovation, they are more likely to share this enthusiasm with their teams and inspire them to act on this conviction. As such, organizations can empower leaders by creating ample space for them to participate in company strategy, thereby ensuring alignment and a sense of ownership in the decisions they will be held accountable for delivering against.

Supportive Innovation Culture

A supportive innovation culture helps to reinforce priorities, encourage effective pathways and ensure healthy portfolios. For example, strategic two-way communication at every level of the organization creates a deeper understanding of the context behind why the organization has chosen to focus on a particular priority. Town hall meetings, “lunch and learns” and even socially distanced webinars have all proven to be effective vehicles for these conversations, particularly when

senior executives tell personal stories and anecdotes that reinforce the context and the choices that the organization faces.

The effectiveness of pathways can also be enhanced by a culture that values innovation. For example, even the best-managed matrix organizations often struggle with siloed business units or functions. In order to empower innovation people, it is important to help them understand that they are not alone and that there are hundreds of others working on similar challenges. By creating relationships across silos, innovation pathways may benefit from more rapid sharing of customer insights, new potential technologies or solutions, and upgraded tools.

Developing a community of practice around innovation can also be a powerful supplement to formal training programs, and many organizations have found success in nurturing these vehicles to disseminate best practices, share stories, manage informal rewards programs (e.g., prizes for interesting ideas, novel customer insights, creative prototypes, projects that "failed fast," etc.) and create opportunities for people to stretch into leadership positions.

DIAGNOSTIC QUESTIONS FOR LEADERS

Empowered Innovation People

Use the diagnostic questions at the end of each section to evaluate your organization's innovation maturity and identify opportunities for improvement.

EFFECTIVE INNOVATION TALENT

Have we defined the talent and skills required to support our innovation priorities? Do we have mechanisms to address our talent and skill deficit through hiring internally or externally? Do we create structures and roles to allow those innovators to progress in their careers? Do we have formal training and development programs for innovation that map to the full set of required skills across the organization and at different levels? Do our performance management systems encourage innovative behaviors? Do we have other reward mechanisms in place, such as leadership recognition?

INSPIRING INNOVATION LEADERS

Have we defined the desired leadership behaviors to support innovation? Have we incorporated innovation knowledge and skills into leadership development? Do leaders model the right behaviors to support and champion innovation?

SUPPORTIVE INNOVATION CULTURE

Does our culture exhibit mindsets and behaviors conducive to innovation? Do we track and evaluate the state of our culture of innovation? Have we developed a program of events and communications to strengthen our culture of innovation? Do we have mechanisms to diagnose and intervene when we identify cultural blockers to innovation?

Strengthening the Innovation System

With regard to innovation systems, organizations often face similar significant challenges, but the majority have strong foundations to build on and are often better at innovation than they realize. The first step in strengthening innovation capabilities is to create a clear picture of where the business stands today, including how innovation is currently getting done, what's working well and what's getting in the way. The following figure (fig. 9) illustrates how the innovation performance model can be used as a diagnostic tool.

In this example from a global consumer goods company, we see some common challenges, including a lack of clarity around performance objectives, gaps in how the organization linked innovation objectives to the broader strategy (priority management), and most importantly, issues with the ways it empowered senior leaders to drive innovation. This diagnostic is simply an assessment that asks the questions included throughout the previous pages and then uses the answers to paint a holistic picture about the relative strength of the organization across each of the five primary "P" components (and 15 elements) of the innovation system.

Leaders who seek to understand their systems today and take steps to strengthen it across the five dimensions of innovation performance are investing in the engine that will help their organizations own the future.

Every large organization has, at some time, demonstrated its capacity to innovate successfully (or it would never have achieved success). However, that sense of achievement can calcify leadership structures and shift focus away from customer understanding toward product or operational excellence. While innovation systems in smaller organizations often revolve around the persona and actions of a single leader, larger organizations must explicitly build and nurture their innovation systems to ensure they remain nimble and adaptive to the ever-changing environment.

Leaders who seek to understand their system today and take steps to strengthen it across the five dimensions of innovation performance are investing in the engine that will help their organizations own the future.

Figure 9. A Summary of an Innovation Performance Diagnostic

SYSTEM COMPONENTS		MATURITY (1=INITIAL; 5=OPTIMIZED)	ISSUES IDENTIFIED (ILLUSTRATIVE)
INNOVATION PERFORMANCE	DESIRED PERFORMANCE OUTCOMES	1 2 3 4 5	No goals for innovation defined at enterprise or business unit levels. Growth goals are defined but widely regarded as financially driven, and the role of innovation is undefined.
	LEADING SYSTEM INDICATORS	1 2 3 4 5	Pulse surveys capture general sentiments on innovation, but there is no tracking mechanism for progress toward goals as they haven't been defined.
CLEAR INNOVATION PRIORITIES	COMMON INNOVATION LANGUAGE	1 2 3 4 5	There are many different terms for innovation used similarly across the organization, leading to significant ambiguity. Specifically, the term "disruptive innovation" is often misused.
	STRATEGIC FOCUS AREAS	1 2 3 4 5	Focus areas are developed via a predominantly present-forward lens and aren't revisited and refreshed frequently enough, and cross-BU connections at this stage are weak.
	CLEAR INNOVATION BOUNDARIES	1 2 3 4 5	BUs are hesitant to set innovation goals, such as by innovation type, and there is limited accountability for innovation targets; BUs do not define goals and bounds for innovation.
	DYNAMIC PRIORITY MANAGEMENT	1 2 3 4 5	Most BUs do not focus on alignment of strategic goals to specific innovation projects and overall portfolio management.
EFFECTIVE INNOVATION PATHWAYS	EXPLICIT PATHWAY ARCHITECTURE	1 2 3 4 5	The official process for disruptive innovation is defined but is not utilized by all BUs; some view the process as complicated, which hinders overall adoption.
	OPTIMIZED PATHWAY OPERATIONS	1 2 3 4 5	Best practices exist, but most stages of the innovation process require additional refinement, including opportunity areas, idea generation, and assumption identification and prioritization.
	CONSTRUCTIVE PATHWAY GOVERNANCE	1 2 3 4 5	Active management of projects through the funnel is evident, but alignment with strategy and portfolio management is weak, with suboptimal resource allocation and distribution.
MANAGED INNOVATION PORTFOLIOS	STRATEGIC PORTFOLIO PLANS	1 2 3 4 5	BUs acknowledge the need for innovation, but portfolio allocation between "core" and "more" is often informal with limited accountability, metrics and tracking.
	ACTIONABLE PORTFOLIO INSIGHTS	1 2 3 4 5	Portfolio analysis is limited due to the lack of rigorous portfolio design and inconsistent application of portfolio metrics; cross-BU analysis and visibility is also limited.
	INTEGRATED PORTFOLIO MANAGEMENT	1 2 3 4 5	The portfolio management process varies significantly across BUs that often struggle to determine what to invest in, leading to a mix of underinvestment in promising projects and continued investment in zombie projects.
EMPOWERED INNOVATION PEOPLE	EFFECTIVE INNOVATION TALENT	1 2 3 4 5	The organization has defined competencies for founders but can push further in identifying and matching the right talent; innovation skills must be embedded across BUs.
	INSPIRING INNOVATION LEADERS	1 2 3 4 5	Senior management and individuals on the ground celebrate processes; however, the most prominent gaps exist in the band 4s and 5s. Senior leaders share their goals for disruptive innovation.
	SUPPORTIVE INNOVATION CULTURE	1 2 3 4 5	The company has made great progress shifting from being technology-first to consumer-first; there is still work to be done to reinforce priorities, encourage effective pathways and ensure healthy portfolios.

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Innosight

Innosight is a strategy and innovation consulting firm that helps organizations navigate disruptive change and manage strategic transformation. Now the strategy and innovation business at Huron, we work with leaders to create new growth strategies, accelerate critical innovation initiatives and build innovation capabilities. Discover how we can help your organization navigate disruption at www.innosight.com.

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