IDEAS

THE INNOVATION PARADOX AND HOW TO OVERCOME IT

THE START-UP CORPORATION

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Many companies are hidebound by fear of major change, and while incremental innovation is both advantageous and essential, to really get ahead it's often necessary to implement dramatic transformation. Managers must learn to make courageous decisions if they are to take the company into the future.

INNOVATION • ENTREPRENEURSHIP • DECISION ANALYSIS

In the absence of industry revolutions, execution and the ability to manage incremental innovation decide winners and losers, and it is in these areas that business units excel. Being more efficient, more attentive to shifts in customers' needs, and more creative than competitors when it comes to meeting those needs ultimately pays off, and the widespread use of business units as part of organizational structure speaks to their success.

While it is exceedingly hard to argue against smooth, efficient, and low-cost operations, the better a company becomes at executing existing business models, the less attention it often pays to developing breakthrough innovations. This is, essentially, the innovation paradox – the way relentless pursuit of incremental innovation can crowd out the possibility of breakthrough innovation. Managers tend to favor ideas that reinforce existing strategies over those that challenge it.

Take, for example, the rise of the refrigerator. Before refrigerators existed, people kept things cold with ice. From growing ice in lakes, to harvesting ice, to transporting and storing ice, the ice-harvesting industry constantly improved each stage of its value chain. The invention of the refrigerator posed a serious threat to what was a well-established and largely unchallenged industry.

At first, the refrigerator was dismissed as a noisy, expensive, and ultimately inferior technology. Eventually, the idea of the refrigerator grew on customers, and its performance proved to be a real hazard for ice-makers. Rather than shift strategy, the ice-harvesting industry essentially put its blinders on and kept improving the efficiency of existing processes – it got better at making, harvesting, storing and transporting ice. In fact, the most significant improvement in ice-harvesting actually happened when the refrigerator had already shown its dominant position – long after it would have made any difference.

When customers no longer needed ice to keep their food cold, the ice industry largely went the way of the dinosaur. This scenario has played out countless times in numerous in-

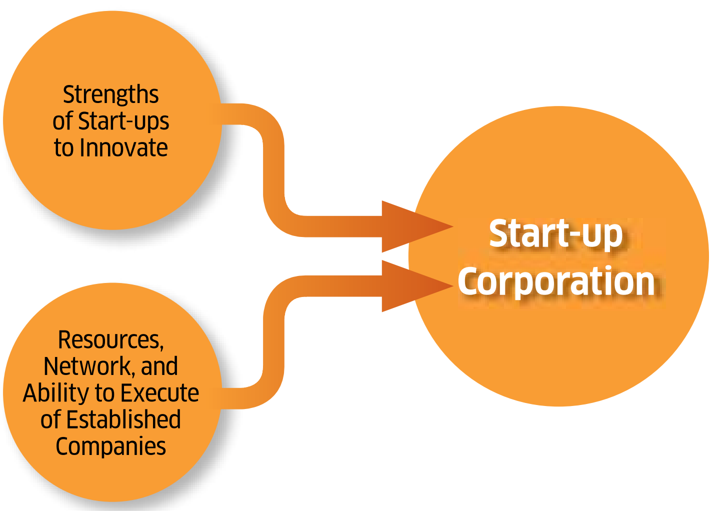
BREAKTHROUGH INNOVATION DOES NOT PLAN IN THE TRADITIONAL SENSE BUT EMPHASIZE EXPLORING DIVERSE ENVIRONMENTS, AND IT DOES ENCOURAGE EXPERIMENTATION.

dustries: a once leading incumbent, rather than work to develop products and services outside its space of traditional dominance, focuses its energies on what has worked in the past, only to lose relevance in a new market landscape.

Of course, none of this is to say that business units aren't innovative – they are, and they need to be to remain competitive. However, the types of innovation that they often support are largely incremental, advancing existing technologies and business models in an attempt to grow a lead over competitors – they improve their ice-harvesting abilities, so to speak. As companies push the business unit model because they bring incremental ideas forward, they often block themselves from the possibility of breakthrough innovation – the potential refrigerators yet to be developed.

Breakthrough innovation utilizes a management model quite different from the traditional business unit. Rather than value efficiency and short-term financial goals seemingly above all else, breakthrough innovation requires a model that encourages discovery and vision. It does not plan in the traditional sense – with specific numbers and metrics to be met by specific dates – but it does emphasize exploring diverse environments, and it does encourage experimentation in both technology and business models. This philosophy is at odds with the methods that make business units and incremental innovation successful, and the frustration of established companies to come up with breakthroughs is often the result of this tension. Business units innovate, and business units ultimately want breakthroughs, but how does a company get breakthroughs from processes designed to deliver incremental innovation?

Figure 1
THE START-UP CORPORATION



ENTER THE START-UP CORPORATION

Some companies perceived as highly innovative have charismatic and visionary CEOs – the **Steve Jobs** and **Elon Musks** of the world. While visionary CEOs can sometimes deliver market-changing breakthroughs, the drawback of this kind of top-down breakthrough innovation is that it seldom succeeds more than once – they can be "one-hit wonders," so to speak. If the first vision is right, but the second vision is wrong, this sort of management model can put the company between a rock and a hard place.

Bottom-up breakthrough innovations, on the other hand, are about harvesting ideas from the brainpower that exists within the company and its networks, and then leveraging the resources of the established company behind them. Whether an organization has 30 or 30,000 employees, going after strategic discoveries – bottom-up breakthrough innovation – requires a management approach that brings the diverse resources available to an established company together with the ingenuity of start-up companies. In our new book, *The Innovation Paradox: Why Good Businesses Kill Breakthroughs and How They Can Change* (Berrett-Koehler 2014), we describe the Start-up Corporation – a set of tools that allows established organizations to leverage their resources behind a management approach inspired by the way start-up ecosystems are designed for exploration and discovery. In other words, the Start-up Corporation is an approach to innovation that emphasizes both the strengths of start-ups when it comes to developing breakthroughs, and the strengths of established organizations when it comes to scaling and execution (*see Figure 1*).

The unique characteristics of the Start-up Corporation give it certain, distinct advantages when it comes to avoiding the pitfalls of the innovation paradox. First, where once-dominant companies have seen their markets vanish with the advent of new ones – the metaphorical ice-makers in the land of the refrigerator, or the flip phone producers in the smartphone world – the Start-up Corporation allows for adapting management to the needs of breakthrough innovation. For instance, it allows a portion of the time, resources, and energy of employees (or a certain group of employees) to be focused on diving into markets perhaps only in their infancy, without the sort of high-pressure, short-term metrics required of incremental innovation. In other words, it sees the value of exploring "not yet" markets with the gusto of a start up, while still allowing the larger organization to focus on the incremental innovations that make and have made it a continued success.

On the opposite side of the coin, once the Start-up Corporation begins to close in on a viable product or service, it can leverage the parent company's resources, networks, and ability to execute. Rather than have to search for specific knowledge, networks, or support activities, the Start-up Corporation has the backing (and resources) of its parent company. Once a viable and promising breakthrough is identified and developed, the Start-up Corporation allows for an easy transition to the kind of execution mentality that has made the larger organization successful – where operational excellence and incremental innovation will determine long-term success. While a strong offense often revolves around breakthroughs, defense is about incremental innovation, and established companies know how to manage it. Companies need to be good at operational excellence and incremental innovation, because without it, survival is at stake. Every year, companies need to incrementally push the boundaries of today's technologies and business models; they need to come up with new products for their customers, reduce their costs, improve their processes, know their customers better, and gain that incremental margin and growth that gives them a lead over competitors – or at least keeps them in the game.

The innovation paradox is sticky, and it can be tempting, as an established organization or a leader, to want to hold on to what is working and forego the kind of costly and uncertain risks that can produce breakthrough innovations. But incremental innovation isn't and can't be everything. Markets can change drastically – and even disappear. The truth is, incremental innovation and breakthrough innovation are both immensely important in their own ways. For an organization to really thrive in the long run, it needs to be able to leverage and capitalize on breakthrough innovations when they occur, while also being able to innovate incrementally and build competitive advantage everyday.

The greatest strength of established companies is ultimately their ability to manage complexity. Where business units get themselves into trouble is when they focus on incremental innovation to the neglect of everything else – they keep ice at the forefront, while refrigerators are flying off the shelves. With the Start-up Corporation, established companies can encourage the development of breakthroughs, and put the full weight of their resources, networks, and management ability behind scaling them.

THE START-UP CORPORATION IS AN APPROACH TO INNOVATION THAT EMPHASIZES BOTH THE STRENGTHS OF START-UPS WHEN IT COMES TO DEVELOPING BREAKTHROUGHS, AND THE STRENGTHS OF ESTABLISHED ORGANIZATIONS WHEN IT COMES TO SCALING AND EXECUTION.

MORE INFORMATION:
This article draws from *The Innovation Paradox: Why Good Businesses Kill Breakthroughs and How They Can Change* (Berrett-Koehler 2014) by Antonio Davila and Marc J. Epstein.