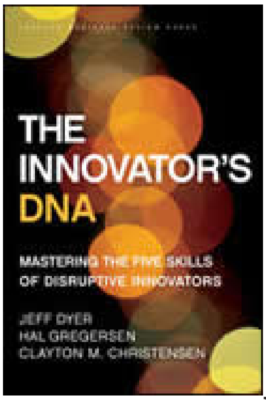
The DNA of the World's Most Innovative Companies

Innovation makes millionaires and undermines monopolies. It raises the profitability of companies and puts a premium on the shares of the most successful. But how can companies foster it? New research sheds light on the innovation process and how firms can tap into it to raise their performance and their share price.

Innovative business leaders typically share certain qualities. They are always asking questions, experimenting, observing and networking. While building on past successes, they keep the doors open to future innovation.

In a world where success often breeds more success, such behaviour can boost the market value of their companies well beyond what current profitability would justify. In a newly published study of what makes a successful innovator, "we looked at people who lead incredibly innovative companies", says **Hal Gregersen**, INSEAD Senior Affiliate Professor of Leadership and Director of the Learning to Lead executive education programme and one of the study's co-authors. "And we realised that these companies seemed to be incredibly valuable."



In reaching this realisation, Gregersen and his co-authors, Jeffrey H. Dyer of Brigham Young University and Clayton Christensen of Harvard Business School, had hit on what they call the "innovation premium". And in their book, "The Innovator's DNA", they explain how for some of the world's most innovative companies it can add 50 percent or more to their market value.

"Investors pay a stock price based upon two things," says Gregersen. "One is the cash flow - the money coming from existing products, services and markets. The other is the belief that the company will develop new markets, new services and new products tomorrow."

More jam tomorrow

Take a company like Amazon. Given its reputation, suggests Gregersen, an investor might well say: "I'll pay you this amount for your stock for the existing products and services, and for the markets that you're in. But I also believe you will do something different in the future. You'll have new markets. You'll have new services. You'll have new products you don't even have today - and because of that, I'll pay you a premium."

Building on this insight, Gregersen and his co-authors worked with HOLT, a unit of Credit Suisse Group, to draw up an innovation premium roll-call of innovative companies based on analysis of the relationship between their cash flow and their share price. To qualify, companies had to be listed on a stock exchange and have a market capitalisation of at least US$10 billion. They also had to have published financial statements over at least the past seven years.

The results were striking. Companies like Toyota, Sony and Samsung, which frequently feature on other lists of innovative companies, sank to negative ratings. In their place emerged a number of unexpected and relatively unknown companies - firms like California-based Intuitive Surgical, which builds systems for robotically assisted, minimally invasive surgery, Natura Cosméticos, a Brazilian manufacturer of cosmetics made from plants from the Amazon forest, and Keyence Corporation, a Japanese producer of electronic sensors for automated factory systems.

Cut-throat car market

The list includes household names like Amazon, Apple and Google. But what makes it different from other similar lists is that it ranks firms not just by past achievements but by what investors expect going forward. "Our list is future-looking, forward-looking and it's based on past performance predicting the future," Gregersen explains. "These are organisations that systematically, over at least a five-year period, have generated this kind of premium. Investors bet with their wallets: this company is innovative, not only now but in the future."

Common to all companies on the list is the fact that their share prices are 25 percent or more above what would be justified by cash flow alone. The leader is cloud computing company Salesforce.com, with its AppExchange that offers more than 1,000 applications for businesses, and which recently launched Chatter draws on features of Facebook and Twitter to provide social software for enterprise collaboration. Market expectations for further innovations have given it a premium based on 2010 results of no less than 75 percent. Bringing up the rear, PepsiCo scrapes in at number 50, with a premium of 25.45 percent. Companies like Toyota and BMW, by contrast, despite their known capabilities for innovation are nowhere to be seen. That, says Gregersen, is because investors expect them to find it hard to earn dividends from new innovations in the face of tough competition from Chinese manufacturers in today's cutthroat car market.

Think different, behave different

So how do companies develop the innovative qualities that enable such results? "There are three elements to this," says Gregersen. "The people in the company, the processes they have and the philosophies they have." The essence of the innovator, he adds, is that he or she not only thinks differently from other people, but also behaves differently.

Take Steve Jobs, the founder of Apple. "If we walked into his world and followed him for a day, we could see him behaving in ways that will generate new ideas. He lives the Innovator's DNA skills. He observes the world really carefully. He talks to all different kinds of people. He's more than willing to engage in different kinds of experiments, constantly peppering the world and the people around him with questions that provoke people and challenge the status quo."

Or take Mike Lazaridis, founder and co-CEO of Research in Motion, the firm that gave the world the BlackBerry, or Scott Cook, the founder of Intuit. They, too, are always asking questions and looking out for the unexpected: "Why not this? Why couldn't we do that? What's going on here? How could we do this better?" When someone "behaves that way, acts differently, asks lots of questions, observes like an anthropologist, experiments constantly, networks for new ideas," Gregersen observes, "they're likely to get incredibly insightful ideas about new businesses, new products, new services, breakthrough processes: things that will make a difference for any company or country."

Down on the farm

That's something most companies in today's environment would pay dearly for. And the good news for those who really want to innovate is that, given the right environment, innovation can be within the reach of anyone.

"About 25 to 30 percent of our innovation capacity is a genetic component, it's our DNA," says Gregersen. "But that's one-third of the equation. The other two-thirds is the world we live in. It's fascinating when we interview these famous entrepreneurs to realise that they grew up in worlds where adults paid attention to these innovation skills." Most often these adults were parents and grandparents, but in about one-third of the cases they were master teachers at Montessori or Montessori-like schools."

To show how curiosity and willingness to experiment can be nurtured, he cites the founder of Amazon, Jeff Bezos, and the chair of Bain & Company, Orit Gadiesh. "Bezos had grandparents who taught him and reinforced to him that experimentation matters. He lived on a farm with them in the summertime and when things broke down, they fixed the things that broke down. They learned that when you try and experiment you can figure out a solution."

As for Gadiesh, "She grew up in a family where questioning was everything and it was reinforced to her that she question. So they both not only had some genetics around these skills, but they grew up in a world that said 'keep them, pay attention to them, use them, do something with them'. And then when they became adults they actually went out and did something with them."

Everybody's job

What lessons does Gregersen draw for other firms that want a piece of this innovation bonanza? Firstly, innovation starts at the top. "Companies on this list are led by leaders who spend at least a day more a week than a non-innovative CEO doing these innovation skills: asking provocative questions, going out there and making real observations and not relying on second-hand data."

Secondly, innovation must be allowed to permeate every level of the company. In a truly innovative company, innovation has to be everybody's job. "It's just part of what you do when you walk in through the door today when you come to work. You need to figure out a better way, a more innovative process, a better product, better service."

Finally, however, a warning: innovation can be disruptive, and in a company with no innovation philosophy, it's likely to be unwelcome. In this case, says Gregersen, a would-be innovator faces a Catch 22 situation. "If I'm in a company that's not innovative and I just do what they ask me to do, I've sealed my fate to not have a future. If I start engaging these skills, on the other hand, I may get a lot of pushback and irritation, and I may even get fired."

In such a worst case scenario, he concludes, it's time to use these skills in a more receptive environment, so as to "create a future that otherwise won't be there".

The book's research led to the publication by Forbes of the Innovation Premium List of the 100 most innovative large companies in the world.

Find article at
https://knowledge.insead.edu/innovation/the-dna-of-the-worlds-most-innovative-companies-1020