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Thought Leader
by Stuart Crainer

W. Chan Kim and Renée Mauborgne: The Thought Leader Interview

INSEAD's strategy scholars parse the line between value and innovation.

Walking through Barbizon, the northern French *village des peintres*, home of the 19th-century painter Jean-François Millet, Professor W. Chan Kim makes an expansive gesture: "This place is a creative hub," he says, smiling broadly, as he watches another pack of tourists disembarking from a bus.

Silicon Valley it isn't. At least, not yet. But Professor Chan and his INSEAD colleague, Professor Renée Mauborgne, believe that their newly created Value Innovation Institute may change the perception of the region to one of a global center for the study of the linkage between innovation and commerce. The institute, he explains, will locate managers from diverse global companies to work on cross-industry and cross-company projects that connect innovative ideas to large commercial opportunities.

Professor Kim, the Boston Consulting Group Bruce D. Henderson Chair Professor of International Management at INSEAD, and his research partner, Professor Mauborgne, the INSEAD Distinguished Fellow and Affiliate Professor of Strategy and Management,

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are particularly associated with the concepts of "value innovation" and "market space." They see value innovation as the ability to challenge assumptions about strategy and to make the competition irrelevant rather than competing on established ground. Their theory of value innovation helps explain the success of many high-growth companies. Market space is the process by which companies can create new demand. It challenges companies to create new markets rather than being preoccupied with those in which they already operate.

The concepts have emerged from the colleagues' cross-industry research over the past decade, which has sought to identify patterns in the way companies create value from innovation, invent new markets, and reinvent existing ones.

"We started off by looking at the companies that succeeded in circumventing the competition," explains Professor Kim. "Then we moved on to how to create new market space — companies need a way to think and act out of the box if they are to circumvent the competition. Our notion of 'fair process' looks at management decision making and what is required to build and execute creative thinking. Most recently we have looked at how to identify a winning business idea and determine which one to bet on. Qualifying innovative ideas for commercial success is a critical strategy component of value innovation."

Interest in the duo's ideas about value innovation, especially among the Europeans, is growing, thanks to a series of well-received articles published over recent years in the *Harvard Business Review* and their presentation last year at the World Economic Forum at Davos. "Here we were at Davos, moderating a discussion on value innovation, and yet only one European, Hasso Plattner [the founder and CEO of SAP AG], was on the panel," recalls Professor Mauborgne. "This raised the question, 'Why aren't there more European CEOs and companies worth listening to on this subject?' What is the problem in Europe? The answer that kept coming back is this: Europe is strong in science and technology, but weak in connecting innovation and commerce."

W. Chan Kim, born in Korea, and Renée Mauborgne, an American, arrived at INSEAD from the University of Michigan Business School, where both had studied and taught. Each came to INSEAD in search of new perspectives. "In the United States, international business still means the U.S. and the rest of the world," says Professor Mauborgne. "Here it is different. We wanted to learn about the reality of international business and understand the role and scope of strategy within that."

It seems fitting that a Korean and an American engaged in a global search for innovative business ideas should make a place like INSEAD their intellectual base. *Strategy+business* met Professors Kim and Mauborgne at their offices at INSEAD and asked about the intellectual stimulus offered by their move to Europe.

S+B: Although your general approach to research seems to look for commonalities across diverse sources and aspects of business performance, you increasingly seem to offer a European perspective on the business world. Is that a fair comment?

MAUBORGNE: Yes and no. True, we study European companies far more extensively than our American-based colleagues. And true, there are different issues at play, different constraints faced by European companies.

But being educated in the U.S. and then coming to Europe, we saw that what happens in the U.S. business world also happens in Europe. There are universal business phenomena. Outsiders coming to the U.S. see it in a clearer light, and the same applies to us coming to Europe. Moving to Europe brought this universality home to us and gave us the confidence to generalize our theories.

Even so, when we looked at

European companies, we found there is a far greater gap between top-performing companies and laggards within the same geographic setting than there is between top-performing European companies and their U.S. equivalents. Striking similarities exist between the strategic perspectives and energy of Nicholas Hayek [the chairman and CEO of SMH/Swatch Group] and Hasso Plattner in Europe and Scott Cook of Intuit or Herb Kelleher of Southwest Airlines in the U.S. All have a strong no-excuses attitude, an obsession with offering buyers leaps in value, and a compelling commitment to create new markets. They are tidal waves of energy. There is a pulse running through these companies that is inspiring.

S+B: When European and U.S. productivity numbers are compared, Europe usually looks worse. Does your experience confirm that?

MAUBORGNE: Europeans, on average, still tend to be supplier driven. The classic example in France is the sign on the shop door *Entrée Libre*. This literally means you are free to enter and a fee will not be charged for the privilege of looking at their goods. In other words, the stores are doing customers a favor rather than customers doing them a favor by potentially buying their goods. This is also manifest in the strong focus on engineering — irrespective of whether customers understand the value in the engineering.

Europeans need to innovate their attitude toward business. There are, however, some signs that this is beginning to occur. In Fontainebleau, for example, in the last few years *Entrée Libre* signs have been removed from more and more stores. That may sound like a small thing, but it is very telling of a new shift that is occurring.

KIM: Europe is as good as the U.S. in terms of technology. Europe is missing the link between technology and commerce. The reasons Europe is poor at commercializing technology have to do with how Europe creates and drives its innovation and entrepreneurial culture. Americans are very bottom-line oriented and very good at value innovation. Europe needs to create a bridge, to drive innovation from the perspective of value. In Europe, there is no Silicon Valley, a place where young and old, clicks and mortar, come together, a place that is driven by entrepreneurship. European industry can — and needs to — be more unified. There are plenty of think tanks and the like, but no unifying theme. This is why the idea of the Value Innovation Institute is so compelling.

S+B: How do you define value innovation?

MAUBORGNE: Value innovation is creating an unprecedented set of utilities at a lower cost. It is not about making trade-offs, but about simultaneously pursuing both exceptional value and lower costs. The Value Innovation Institute will be dedicated to helping companies achieve this strategic mission.

S+B: Although you regard yourselves as pure academics, there seems to be a populist slant to your work. You are asking straight, basic business questions rather than posing abstract hypotheses.

MAUBORGNE: We ask, Who is doing something interesting? What is it that makes companies exciting, confident, and strong? Innovation is the life of a company, and we have fun by looking inside companies — both leaders and laggards — to understand the way forward.

We have a natural curiosity. So, as our research progresses, we create new hypotheses: Why is it that companies stop innovating and growth slows? How can you find the one idea faster? How do you price something that hasn't been sold before?

S+B: Your work suggests that companies often lack insight into the basis of their competitiveness. They don't have all that many answers to your questions.

MAUBORGNE: That's true. Companies are often unclear on which factors they compete on. They rarely think about alternative industries — the broad range of industries that provide similar products or services. Give companies 20 factors they compete on, and they will agree on 10, but dispute the remainder.

That is a large part of the reason organizations are overtired and lacking in creative momentum. Because companies often lack a clear, compelling strategy that everyone understands and that sets the company apart, projects are often undertaken that pull the organization in different directions. Individually, a case can be made to justify each project, but collectively, because they are not guided by a unified strategy, the actions do not add up to significant gains.

S+B: Strategy, in your eyes, needs to be built around value innovation.

KIM: Our point is that value and innovation are — or should be — inseparable. Value innovation places equal emphasis on value and innovation. Value without innovation can include value creation that

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simply improves the buyers' existing benefits. Innovation without value can be too technology driven.

S+B: The mistake has been to equate innovation with advances in technology?

KIM: Yes, value innovation is a strategy concept that is distinct from either value creation or technology innovation. There are plenty of examples of companies that developed technology and then failed to capitalize on it — in video recording technology, Ampex [Corporation] led the way technologically in the 1950s. But value innovators like JVC and Sony brought the technology to the mass market.

There are also many examples of true value innovation occurring without new technology. Look at Starbucks coffee shops, the furniture retailer IKEA, the fashion house of Ralph Lauren, or Southwest Airlines. They are in traditional businesses, but each is able to offer new and superior value through innovative ideas and knowledge.

The power of value innovation is in engaging people to build collective wisdom in a constructive manner. Value innovation means that the range of disagreement becomes smaller until creativity explodes. Value innovation is fundamentally concerned with redefining the established boundaries of a market. If you offer buyers hugely improved value or create an unprecedented set of utilities in order to give birth to new markets, then the competition becomes unimportant. Instead of playing on the same field, you have created a new one.

MAUBORGNE: Value innovation enables companies to shift the productivity frontier to a new terrain. Value improvements get you only so far. Value innovation is concerned with challenging accepted assumptions about particular markets, changing the way managers frame the strategic possibilities.

S+B: Is the driving force behind value innovation the willingness of companies to create new markets?

MAUBORGNE: Fundamentally. Innovation occurs across industries, across countries, across companies. These are universal forces. It is, therefore, irrelevant to categorize organizations by their sector or geographical location. Yet, if you look at strategy literature, industry boundaries are usually regarded as central — think of SWOT analysis or Michael Porter's Five Forces Framework.

When we came to Europe, we found companies that were making the move from being supply driven — outcompeting — to demand driven, to actually creating markets, creating new business space. In the U.S., there were companies like Home Depot that were vaunted for being different and that were creating new wealth. When we came to Europe, we discovered a rich new vein of examples; companies that were breaking the mold — companies like the Formule 1 hotel chain or Bert Claeys in Belgium. Formule 1 looked anew at the French low-budget hotel market and created hotels attractive to both truck drivers and businesspeople. The Bert Claeys Group built new market space around Belgium's cinemas by refusing to accept common perceptions about what was a declining industry. Bert Claeys ignored long-term decline and created the world's first "megaplex" cinema with 25 screens and seating for 7,600.

When we talked to these companies, their managers said much the same things as their American counterparts. There was a pattern to their strategies. The big issue for them was not necessarily innovating in terms of technology or science, but bringing innovation to bear on the value they delivered to buyers.

S+B: Can you explain that further?

KIM: Companies have tended to concentrate on differences between different groups of customers. They have divided them into ever smaller and neater segments so they can customize their offerings to meet the needs of those segments.

We found that value innovators take a different approach. Instead of looking at differences between customers, they focus on the basic commonalities across customers. When companies create unprecedented value on those commonalities, the core of the market is pulled toward them as customers are willing to forgo their individual preferences. Value innovation desegments and collapses established market boundaries by challenging accepted and assumed market order. Unlike the strategy framework built on environmental determinism driven by competition, value innovation takes a constructionist view of the market, where its focus is on shaping the market by cognitive reorderings in managers' strategic thinking.

S+B: How can companies use value innovation to create new market space?

MAUBORGNE: The challenge is to create new demand, what we call market space. New market space is about creating a company's future. Companies can continue to mine their wealth from an existing market space — that's maintenance. They can concentrate on market share. But there is something more — the act of creation. Creating new market space will become increasingly vital.

Creating new market space provides growth. There are two paths to growth. One is the mergers-and-acquisitions path, which often leads to growth but rarely leads to profitable growth. The other is organic growth by creating new businesses. While this path is profitable and necessary, in markets where supply exceeds demand, companies are often hesitant because they don't have a path forward to believe that they could succeed in changing things. They need a bridge to get there. Hopefully, some of the ideas and analytics we have been developing will help companies in building that bridge.

S+B: What else is needed for companies to grow?

KIM: Another element is our concept of "fair process." This has to do with people. Transformation requires that companies earn the intellectual and emotional commitment of their employees. To do so requires a degree of fairness in making and executing decisions. All a company's plans will come to nothing if they are not supported by employees.

If you violate fair process it can be devastating. British Airways lost significant ground in employee morale and customer service after it announced a cost-cutting program at a time when its profits were high and planes were full. It violated fair process in making the plans. There was no engagement, explanation, or clarifying of expectations.

Fair process is based on the simple human need for intellectual and emotional recognition. Without fair process it can be difficult for companies even to achieve something their people generally support.

S+B: What are the basic questions companies need to ask themselves if they are to embrace fair process?

MAUBORGNE: First, they need to ask whether they engage people in decisions that affect them. Do they ask for input and allow people to refute the merit of one another's ideas? Do they explain why decisions are made and why some opinions have been overridden? And, after a decision is made, is it clearly stated so that people understand the new standards, the targets, responsibilities, and penalties? The big U.S. automakers have a history of violating fair process and have paid the price for it many times over.

S+B: Most recently you have moved into the world of predictions with your work on how to spot winning business ideas. Surely this is more of an art than a science?

MAUBORGNE: We have created three analytical tools to help managers identify a winning business idea whatever the market space it occupies or creates.

The first is the Buyer Utility Map, which indicates the likelihood that customers will be attracted to a new idea. This is a matrix based on six stages of buyer experience, from how easy it is to find a product to how easy it is to eventually dispose of it, and six "customer utility levers" — from environmental friendliness to improved customer productivity. Innovations should occupy as many squares on the matrix as possible, although it is unlikely to be more than three or four.

The second tool, the Price Corridor of the Mass, identifies which price will unlock the greatest number of customers. It does this by benchmarking prices not just against similar products, but against different products that fulfill the same function. For example, short-haul airlines compete not just against other airlines, but against buses, trains, and cars.

The third tool, the Business Model Guide, is a framework for calculating whether and how a company can deliver an innovative product or service at the targeted price. It includes options such as cost targeting and opportunities for outsourcing and partnering.

S+B: If you apply the tools, will innovation surely follow?

MAUBORGNE: Not quite. First, innovation, like all other strategic actions, will always involve both opportunities and risks. Ours are designed to help systematically raise the probabilities of success, shifting the odds in favor of the opportunities over the risks.

Innovations also often have to overcome adoption hurdles. There may be resistance from stakeholders both inside and outside the company. Employees, business partners, and the general public can tackle those problems. The key is open discussion with these stakeholders about the impact and ramifications of the innovation. Look at genetically modified food. What if Monsanto had opened up discussions with the stakeholders? Perhaps, instead of being vilified, it might have ended up as the "Intel Inside" of food for the future — the provider of the essential technology.

S+B: Are you still finding new value innovators doing interesting things that are largely unknown?

MAUBORGNE: Constantly. The periphery exists in less-developed countries and in countries not known for value innovation. Peripheral companies include the Hungarian bus company NABI, which is rapidly dominating the U.S. bus market by changing the value curve of the industry, and Cirque du Soleil, the Canadian circus that has led to a rebirth and redefinition of the circus industry. Cirque du Soleil collapses the two industries of theater and circus and in doing so leapfrogs Ringling Brothers and Barnum and Bailey circuses and opens up the entire adult audience to circus at a price point several multiples more than that of a traditional circus.

There is also the French company JCDecaux, which is the leading provider of outdoor advertising space. JCDecaux created an entirely new industry space by converting bus stops and metro stations into very desirable advertising space. Municipalities win by getting outdoor furniture that is stylish and free, while JCDecaux wins by selling the advertising spaces in these desirable prime-location city stops.

S+B: But surely emulating such peripheral organizations is very difficult and perhaps ill advised or even impossible? P&G is not Cirque du Soleil.

KIM: Businesspeople always say there are questions of culture, the stock market, rules and regulations, etc. Yet whenever we show the Formule 1 example, people say, "Why can't we do that in my industry?" The challenge is not to emulate what any of these companies did, but to understand the thinking process that allowed these companies to create a new market and value innovations. Companies find this challenge inspiring. Learning to think differently about opportunities and risks, daring to move forward into the future, that is what keeps people and companies alive, young, and growing.

S+B: You appear quite prepared to commercially share your concepts and the notion of value innovation.

KIM: We gain more by giving people the value innovation trademark free of charge so long as they share their knowledge and research findings. It is an open-system approach. They tell us what works and what doesn't work.

The more empirical evidence and market feedback we have either against or for our hypotheses, the richer the concepts we can build for theory and practice. +

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