

# Innovation Drives Profit

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## A formula for market leadership

Everyday I am approached by corporate leaders who have a common and overriding problem that they seek answers to. It's always the same core issue: How to increase revenue and profits. Having successfully driven growth and dramatically increased value to some well-known companies, many of these concerned executives expect that my "formula" must be some complex algorithm or perhaps blind luck. It is neither. The formula for greater profits and valuation is a process of innovation, and I will outline for you how to grow profits by driving innovation.



As a company, most of you are delivering a product that has essentially already been made by others. You have identified a market opportunity and you (hopefully) have a unique twist to your product that affords it a perceived benefit over the competition. This may be a better specification, higher quality ingredient, lower price, etc., but you are competing against other products for a share of the market and you are relying on an ability to communicate that point-of-difference.

But then there are a few companies that are defining what the market wants but have not yet articulated. These market-making companies are leaders, taking a risk but often making exponential leaps to market ownership instead of incremental steps at staying afloat.

I don't think many companies realize that their incremental improvements are often driving down profits and encouraging commoditization. While one often thinks that they are delivering something new and different, in reality it is usually at best incremental and typically not relevantly differentiated. What winds up happening is these companies resort to selling on price and using "push" sales tactics, resulting in higher sales and marketing costs, lower margins and erosion of corporate profits.

As companies like Apple Computer have clearly illustrated, if you can deliver a product that is truly unique, differentiated and relevant, demand will drive profits (and inherently higher margins) and corporate value skyrockets. This innovation approach is the antithesis of commoditization as it delivers to the innovator a leadership position characterized by high margins, longer product lifecycles, insulation from competition, sustained sales velocity and a differentiated brand that builds long term user (consumer) engagement. In other words, they create raving fans of their brand that actually pay the company to market their brand.

If innovation is the articulation of unmet needs, two key questions must be answered: How do you identify these unarticulated needs and how do you turn them into differentiated products?

I mentioned earlier the term *market-makers* in referring to innovation leaders. In order to answer the questions posed it's important to understand what leadership is. A leader isn't afraid to blaze new trails. If you are not kicking up dust, you are eating someone else's dust. Too many companies are mistakenly looking in the rear-view mirror instead of charting a new course.

I can't tell you how often companies spend huge amounts of money with the worthy objective of trying to identify emerging opportunities. But more often than not they use "rear view mirror" tools, spending on focus groups or industry/category data, which can only provide a snapshot of what has happened or a reflection of current/past awareness. Do you think that Starbucks held a



focus group in the early 80's or read market data that suggested customers would line up down the street to pay five times more for a cup of coffee? No, they saw a commodity category that was ripe for innovation and they redefined the coffee experience. Conventional thinking would have suggested they have to produce a cheaper coffee and or deliver some other incremental benefit (new flavor, new package, etc.).

An essential element required for innovation is an understanding of end-users (consumers), since the ultimate goal is to engage them. By understanding consumer's lifestyles, needs and behaviors we can gain tremendous insight into how, what and when to market to them. Even if you are a B2B supplier whose customers are other businesses, your real value is in driving consumers to your customer's brand; if you are not adding value to their product then you are simply a commodity that can be replaced by your competitors at a moment's notice.

Two tools that are very helpful in identifying unarticulated consumer needs include ethnographic research and Cross Impact Analysis.

Ethnography is a qualitative research methodology that strives to understand how people live and make decisions. It is free flowing and

conversational, often involving researchers going into people's homes or observing them in a shopping environment. While consumers will often provide expected answers, more often than not their behaviors are actually very different. Many times I have witness this paradox first hand; the mother of three who claims that she carefully selects only healthy food choices for her children, yet is observed with a pantry full of chips, soft drinks and unhealthy products; the shopper who claims to not buy a product based upon brand name, but clearly overlooks identical products at lower cost, claiming the branded product is of higher quality.

Cross Impact Analysis is a model that maps behavioral trends and social interests and identifies macro trends. Think of these dozens (or hundreds) of



micro trends like streams of water; when they converge they feed a river. This model illustrates how these trends interact to signal emerging consumer needs. Since consumer behaviors are preceded and supported by changing values and beliefs, this model helps identify "what may happen" as opposed to focus groups or market data identifying "what has already happened".

Once you are able to glimpse where the market is going (or more specifically, what are some emerging needs consumers may have), you must overlay that against your company's capabilities, strengths and assets. For instance, if you identify on-the-go RTD breakfast beverages as an emerging category, but your company has no credibility as a consumer branded player, you would need to evaluate how logical that opportunity may be for you. But if you are a B2B ingredient supplier, perhaps you can formulate a product featuring your functional ingredient and partner with a branded customer to launch it; this is how value is built.

With over 75% of new consumer products characterized as "me too" and failing within a year, it is essential that you drive innovation and differentiate the brand. Which brings us to the second question we must ask: how?


While science is migrating into consumer products, it is critical to understand the difference between a therapeutic ("treatment") and a functional or healthy consumer product ("wellness"). Advances in life sciences are identifying new compounds and the utility of existing botanical constituents that have tremendous functional applications. Furthermore, nutrigenomics is opening new opportunities around the relationship between gene expression and cellular function resulting from food consumption. But consumers eat to enjoy, and everything else is secondary. They don't eat from their medicine cabinets and they've demonstrated that food is not a very good vehicle for therapeutics. Focus on delivering a lifestyle solution, or as I like to call it a *Lifestyle Antidote*, rather than an edible medicine.

The real "secret formula" to innovation is a change of perspective. Create a process that is singularly focused on revolutionary thinking, not evolutionary

steps. Use the consumer insights to think in terms of “what if...”; define what that might look like; test whether such a product would be truly innovative; then identify what components are needed to build it.

Create unique attributes to the brand with a relevant point-of-differentiation that hits on emerging needs...hopefully needs that consumers have not yet even articulated. A good way to do this is by targeting a very specific market segment. And once you can define this prototypical product or brand, focus groups are useful; that’s when, if successfully communicated to the audience, consumers will pronounce, “wow, that’s so cool. I want one”. This bottom up approach to product development should unbind you from the self-imposed confines of convention, allowing you to see the possibilities and create new solutions rather than looking in the rear view mirror.

With all sciences, there is an art to how it is applied. The danger many companies run into is when they follow a herd mentality, misguiding thinking that leads to commoditization. In order to break that cycle, you must apply a new approach to your company; an approach that starts with vision and is driven by data. This is the formula for generating value.



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**Contact:**

Peter Leighton  
[peter@abundasolutions.com](mailto:peter@abundasolutions.com)  
+001 (801) 550-6962  
SKYPE: advana\_science