

Patterns for Success

*Scott D. Anthony on using innovation theory to transform organizations
and create the next wave of growth*

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UBIQUITY: What were you doing before you went to Harvard Business School?

ANTHONY: I worked for a consultant company called McKinsey for a couple of years and I worked for a startup company called WorldSpace. It was a Washington, DC-based company that was trying to launch a series of satellites to deliver audio and multimedia services to the developing world.

UBIQUITY: How did that work?

ANTHONY: It's the same basic technology as XM satellite radio in the United States, just trying to bring that to Asia, Africa and North America. I know a few people who are loyal subscribers to XM and say that they can't imagine life without it. I know other people who say, "Why would you pay \$10 a month for radio?" and then others remind them that that's what people said about cable television a generation ago.

UBIQUITY: It sounds like a version of Musak. Is that unfair?

ANTHONY: It goes well beyond that. Because of the channel setter available on XM, some people have described it as radio on steroids, where you have the music that you might hear on regular radio stations, plus a bunch of other stuff such as talk, music, sports and all sorts of different dedicated stations.

UBIQUITY: What about people who live in a place where the radio reception is bad, so the only time they listen to radio is in the car? I'd love to listen to the radio more.

ANTHONY: With satellite distribution, the quality of the signal is pretty good no matter where you are, as long as you have the ability to see the satellite.

UBIQUITY: The subtitle of your new book is "Using the Theories of Innovation to Predict Industry Change." Did you find any surprises as you tried to apply theories to practice?

ANTHONY: When we use these tools to look at an industry or a company, we either come to a conclusion that we might not have expected or it sharpens our intuition. We understood that something was happening but with the models we understand *why* that's happening. Once you understand why, you can know what's going to happen next because the pattern plays out in other places.

UBIQUITY: To you personally, what was the biggest surprise as you worked on the project?

ANTHONY: One of the things that was a learning experience for me personally is just how -- "difficult" maybe is too strong a word -- but how much art there still is in taking well researched concepts and using them for other purposes. Clay and others have been trying to use these models in predictive ways for a long time, and at one level you think, well, if the model is out there and it's been researched then the job is over, you know exactly what you need to do. But what you realize is that understanding what the model is and using it to look into the future are two very different things. It was a constant surprise to me how intricate you had to be and how carefully you had to think through things in order to be able to use what appear to be very intuitive concepts.

UBIQUITY: What's an example of that?

ANTHONY: As an example, during the late 1990s and early 2000s, which was a funny period to begin with, you had people who would describe just about anything as being "disruptive". They'd say, "I read the book, I understand precisely what this disruptive innovation thing is, and we're disruptive." When asked, "Why are you disruptive?" they'd say, "We're disruptive because we're offering a much better product than anyone in the industry and because of this we're going to disrupt the

industry.” Well, that’s not exactly right, at least in the way that we use the word, where something that’s disruptive will not be better along the primary basis of competition, it will offer some form of new benefit in exchange for lower performance along those metrics. A lot of startups were running around proclaiming that they were disruptive, waving their business plans with the “Big D” on them. These were smart people but they didn't think carefully through some of the models and exactly how they work. The implications of that are important.

UBIQUITY: What are the implications?

ANTHONY: If you think that the world’s going to play out in one way and it plays out in a very different way that can have pretty stark consequences for you.

UBIQUITY: What do you feel the role of the Internet has been in the whole disruptive process?

ANTHONY: When the Internet first began to appear on people's radar screens they intuitively perceived that it was important and would do something substantial to business. Where people rushed to judgment was in saying that anything old is bad, anything old is dead, anything new that has this .com affixed to it is good and will ultimately triumph. A couple of things happened over time. One is people realized that the Internet by itself is neither good nor bad, nor is it something that’s constructive or destructive on the face of it. The impact of the Internet has depended on the specific business model of companies. To someone like the University of Phoenix, a provider of adult education, the Internet is a highly sustaining innovation and makes it easier for them to extend their business model and reach more working adults. But to someone whose business model is built on having integrated services provided at a centralized location, at least in the initial days, it’s less clear how the Internet helps them. My first notion is that the impact of the Internet is relative to the business model of the organization it’s impacting.

UBIQUITY: You said a couple of things have happened over time regarding the Internet. What is the second thing?

ANTHONY: The second thing that's interesting is that a lot of things that happened in the 1996-2002 time period laid a foundation or groundwork. Now that the infrastructure is in place, you will see people coming up with novel business models that aren't necessarily based on the Internet but take advantage of that infrastructure to do things that previously were extremely difficult.

UBIQUITY: Give an example of a novel business idea that has successfully taken advantage of the built-in infrastructure?

ANTHONY: Netflix, for instance, offers a subscription DVD service where you can sign up online and rent DVDs. They send a DVD to you and when you're done watching you send it back. You certainly could have done a business like that before the Internet, but the Internet has made it much easier for Netflix to come up with a viable business model. I think we're going to see more of that as we go into the future; really different business models that pick up pieces of the Internet as their core component. Netflix is a classic example of what makes life so challenging for companies. Netflix came up with this business model that is highly disruptive to Blockbuster because Blockbuster basically makes all of its money from late fees. In Netflix' business model there are no late fees, so Netflix comes out of the gate and has a tremendous amount of success. But even though Netflix has done this, it now has to continue to innovate and think about different ways to reach customers because video-on-demand is coming and that's clearly going to have an important impact on the industry. It remains to be seen exactly who's going to lead that. It's going to be a real challenge for Netflix.

UBIQUITY: Would you be reluctant to make a guess that, say, twenty years from now, Netflix could survive unless it changes absolutely?

ANTHONY: You never know with absolute certainty but if history is any guide, if Netflix does not adapt and continue to innovate and tries to keep following the same model it's following today, the odds of it still being around in twenty years are quite slim. This is not just based on Netflix. Every company needs to constantly innovate in order to survive. In Netflix' case it's even more apparent that there are forces at work that will make it difficult for them to keep doing what they're doing. It's just a matter of time before all content is digitized and can be sent over the network, and if

Netflix' business is still sending actual disks in the mail then at some point in the future that business is surely going to at least shrink quite substantially.

UBIQUITY: Are there companies that can't be completely digitized? I am thinking for example of the online grocery stores that were a rage four or five years ago?

ANTHONY: Online grocery stores is an interesting example. People looked at the grocery business and said, "People don't love to food for shop, so let's find a way to make it easier for them," forgetting that the grocery industry is brutally competitive and that retailers have figured out ways to be profitable on razor-thin gross margins. There's not much slack in that system where you can take advantage of economic disparity to make money. It turns out that people don't want to pay huge fees for delivery. So at least until the days where we can have some kind of newfangled machine that produces food in our own apartments, it's hard to see how there won't still be grocery stores. The thing that you can begin to conceptualize is having smart appliances that can sense when you're running low on milk or you don't have any more laundry detergent, and they can place automatic orders with the companies that provide those goods.

UBIQUITY: What about retailing in general -- the Wal-Mart kinds of stores on the one hand and boutique stores on the other? What are your thoughts on that industry?

ANTHONY: Wal-Mart fundamentally disrupted many of the general merchandise retailers with its business model based on low prices and very fast inventory turns. It has taken on a progressively larger part of the retailing world as they've added things like food and toys, where today Wal-Mart I believe is the largest food retailer in the United States. It's certainly the largest toy retailer. Toys"R"Us is considering disassociating itself from its core business because Wal-Mart has hollowed it out so much. Yet, boutique retailers continue to thrive. When the products themselves are not yet well known, and are not yet good enough so that consumers can be sure that wherever they go they're going to get adequate quality, there still is a role for a focused retailer. Best Buy is successful because consumers know that Best Buy can help guide them to make the right purchase decisions on electronic devices. Customers know that Williams-Sonoma does a better job than anyone in the world of

buying and assembling the right type of kitchen merchandise, so it makes shopping for that type of goods very easy. Whereas Toys"R"Us has struggled tremendously on the toy front, their Babies"R"Us division is booming because for a long time people haven't been able to tell when they go into a store whether they're getting good products or bad products. A focused retailer like Babies"R"Us can be highly successful when it makes sure that the best products are in those stores.

UBIQUITY: What do you think about the computing industry -- not computing itself -- but manufacturers such as Apple and Gateway are the two that jump to mind?

ANTHONY: Take as a contrast Dell and Gateway. About ten years ago those companies were about in the same place, but today Dell is a poster child of a hugely successful company and Gateway is less so. Why is that the case? The answer is that Dell has taken the low-cost business model and tried to race up market to compete against other high-cost, high-margin players such as Hewlett-Packard in the server market. Gateway has stayed more focused on the consumer end. It has lived almost a profit-free existence because Dell has beaten out all the profits from that business. The only way you can make money when you're a low-cost provider is to have the privilege of competing against higher-cost providers. Gateway has not been able to follow that same path and not been able to succeed as much.

Then you have Apple. Twenty years ago they kept their computer closed and lost out a leadership position to companies such as Microsoft and Intel. Today, of course, Apple has a massive success with its iPod, where it has come up with a clever way to combine some very commoditized components to create a new value proposition for consumers. One of the things that strikes me about the iPod is that people often forget that Apple was certainly not the first in that industry. In fact, my Apple iPod is the third different MP3 player that I've bought. But Apple was the first company to get it right; they were the first company to integrate the device with the software and the provision of content in a way that made it easy to listen to exactly what you want when you want. That integration made them the first to nail that value proposition and be able to create a leadership position.

UBIQUITY: How long do leadership positions last in the face of competition from somebody like Microsoft, which is entering that category?

ANTHONY: It has been interesting to watch. Sony, the traditional leader in all forms of music devices, entered into the hardware side, and a bunch of different companies come in on the provision of content side. At least for the moment, my sense is that Apple has an advantage because it still can combine things together that make it easier than anyone else. What's interesting is the way Sony tried to compete against Apple. They decided to make a device that has higher capacity and a longer battery life than Apple's iPod. I don't think those are dimensions that customers are looking for. I think they're looking for things that are simple and easy to use. Apple has a substantial edge on those dimensions. But if Apple stands still it will lose. So Apple has to continue to innovate and continue to come up with new devices like the Mini and other products to be able to succeed.

UBIQUITY: Thinking of Apple not on its music forays but in the old-fashioned computer business -- that's sort of an oxymoronic phrase -- is it conceivable that Apple could recover from the disastrous mistake it made of having a closed technology?

ANTHONY: It's hard to imagine it happening because of their market share in the computing industry; it's a big mountain to climb up. My sense is that if it's about the traditional computing industry, then the sins of twenty years ago still permeate in Apple's business today. They continue to have a great product that's loved by customers, unfortunately there are not that many of them. But today's computer is not what tomorrow's computer will be, and if Apple could think about a completely different way to conceptualize what computing services are, there could be an opportunity to create a leadership position.

UBIQUITY: What could you say was Apple's biggest mistake in the last ten years?

ANTHONY: Maybe it's not anything related to computers; maybe the problem is how Apple didn't get it right when it went into the handheld device industry, that its flub with Newton will be remembered as much more of a mistake than its decision to keep its Macintosh computer closed. As you see these handheld devices continue to get better and better, you could chart a course where these are the computers of the

future. I've got an integrated device that I bring with me on trips and if it got a little bit better, my laptop would be left behind.

UBIQUITY: What device?

ANTHONY: I have a PalmOne Treo 600. It's an integrated e-mail, PDA, telephone device. It's not that far away from being more than good enough for almost all of the computing needs that I have when I'm on the road. Apple getting it wrong with the Newton I think is going to end up costing them more than keeping their operating system closed.

UBIQUITY: What are the top things that you do on the road that you find it easy to do with that device and what are the two or three things where it's still not possible?

ANTHONY: It's certainly easier on the back because you don't have to carry around a big computer case and all the cords and stuff with it. In terms of portability, it can't be beat. The mobile phone is a much better phone than the phone on my computer, so along those dimensions it's significantly better. If I've got to do something real on a document, if I need to edit a Word document, or look at an Excel spreadsheet, or do a PowerPoint presentation, the quality is nowhere near good enough. But if I need to send a quick e-mail or I need to quickly read through a Word document done by one of my colleagues, then the portability makes up for a lot of the deficiencies.

UBIQUITY: Is there a keyboard attachment?

ANTHONY: It has a small, integrated keyboard. If you are unfortunate enough to have big fingers, you are in trouble. But it's quite a nifty little thing.

UBIQUITY: Do you do Web surfing?

ANTHONY: I do. Most of the Web Surfing that I do, I will admit, is looking at baseball scores. It is very good when you're out somewhere and you want to see what's happening to our Red Sox.

UBIQUITY: Let me ask you to talk about life on the road. Where do you go mainly?

ANTHONY: There has been a lot of travel recently. You go wherever the clients will take you. Clayton founded Innosight back in 2000 to function as his arms and legs; to go out and help companies put his ideas into action. We work in all industries because the challenges of growth and innovation are not industry-specific. The other day a client asked me what industry we work in, and I wrote a list of all the industries that we've served in the past year. The list included primary materials, software, retailing, high-tech, telecommunications, oil and gas, defense, national governments and all sorts of different things. The problem of how to create the next wave of growth affects every single firm. Large firms, small firms, US firms, international firms, it doesn't matter; every company needs to solve these problems.

UBIQUITY: What could you do for national intelligence?

ANTHONY: There are a couple answers to that. One is to think about what are some of the organizational implications of a changing environment because our environment most certainly has changed over the past decade. One thing you can be sure of; if you optimize your intelligence or defense to fight against a large monolithic enemy, then some of the systems and processes that are put in place will be weaknesses when the game changes and you have to fight a shadowy, nimble enemy that's diffuse in many different places. Some of the problems that the intelligence agencies have had in the past few years were one hundred percent predictable because when you solve the same problems for forty years and then you're asked to solve a very different problem you must overcome organizational structures that have become ossified and difficult to change. That's one area to think about: What are the organizational implications of a change in the nature of the challenge?

The second, where the CIA is following an interesting approach, is to try to tap into some of the technologies that exist today to come up with novel solutions to try to help them in the things that they're doing. I believe the CIA has set up an almost venture capital-like fund called In-Q-Tel that seeks out technology ventures to develop technological solutions that could help them. There are many things out in the "regular world," not just in the defense community, that, if adapted, could help in some of the battles that the intelligence agencies are trying to help fight.

UBIQUITY: What about consulting? How is your company following your own advice?

ANTHONY: In a bunch of different ways. You always, of course, want to avoid being too self-serving when you say some of this stuff. But what we're trying to do is to take consulting from unstructured experimentation -- where a large team of consultants gathers huge amounts of data, beats that data up and sees what it confesses, and uses their big brains to come up with an answer -- and instead move it more towards a world of pattern recognition where we can recognize patterns of success and failure and utilize those patterns to help companies in a more effective fashion. We hope to teach companies that it's not about gathering more data; it's about looking at the information through a different set of lenses, so you can interpret that data in different ways. Importantly, we can also teach you how to do this on your own. I used to work for a big consulting firm called McKinsey. I would say not an ill word about it. But the name of the game there is because there are so many people there, you've got to keep selling business and you've got to keep all those people busy. So you do project after project with large companies where the goal, after doing sterling work, is often to sell the next project.

One of the benefits of being a relatively small firm is that we don't have as many mouths to feed, so what we tell companies is that our goal at the end of a project, if we've done our job well, is that you never hire us again because we've taught you through the course of this project how to use these theories and models on your own. So you can now go forward and put these ideas into practice without needing the assistance of a consultant. They like to hear this because, of course, if you really want an organization to be transformed, the organization has to do the transformation; it can't be just external people because once those external people go away then the transformation goes away.

UBIQUITY: But they'll have to transform themselves again, right?

ANTHONY: That's true. "The Innovator's Solution" talks about how at some level it's a risky book to write because no one has ever done systematically everything suggested in the book. But our belief -- and this is still a belief because we don't

have the proof points yet -- is if a company understands these concepts and puts in place the right infrastructure to support them, that they can create a growth engine that can create new growth businesses with a much higher degree of predictability than historically was possible. If you get the engine humming in the right way, we believe that you can solve problems that historically were deemed unsolvable.

For more information about the new book, "Seeing What's Next: Using the Theories of Innovation to Predict Industry Change," visit <http://www.seeingwhatsnext.com>.

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