




A CEO's Guide to Creating New Growth

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I.	INTRODUCTION.....	3
II.	WHAT IS DISRUPTION?.....	4
III.	WHAT IT IS NOT.....	6
IV.	LIMITATIONS.....	6
V.	ASSESSING A POTENTIALLY DISRUPTIVE INNOVATION.....	7
VI.	ABOUT MICHAEL URLOCKER.....	8
VII.	ADDITIONAL RESOURCES.....	8

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I. INTRODUCTION

Disruptive Innovation offers the best way for companies to grow by creating new markets.

But what defines successful disruption? What are the limitations? Is this just another marketing buzzword? And most importantly, what can it do for your business? These questions will be explored in this guide.

First, a quick example of a disruptive innovation to highlight the business gains that can be achieved.

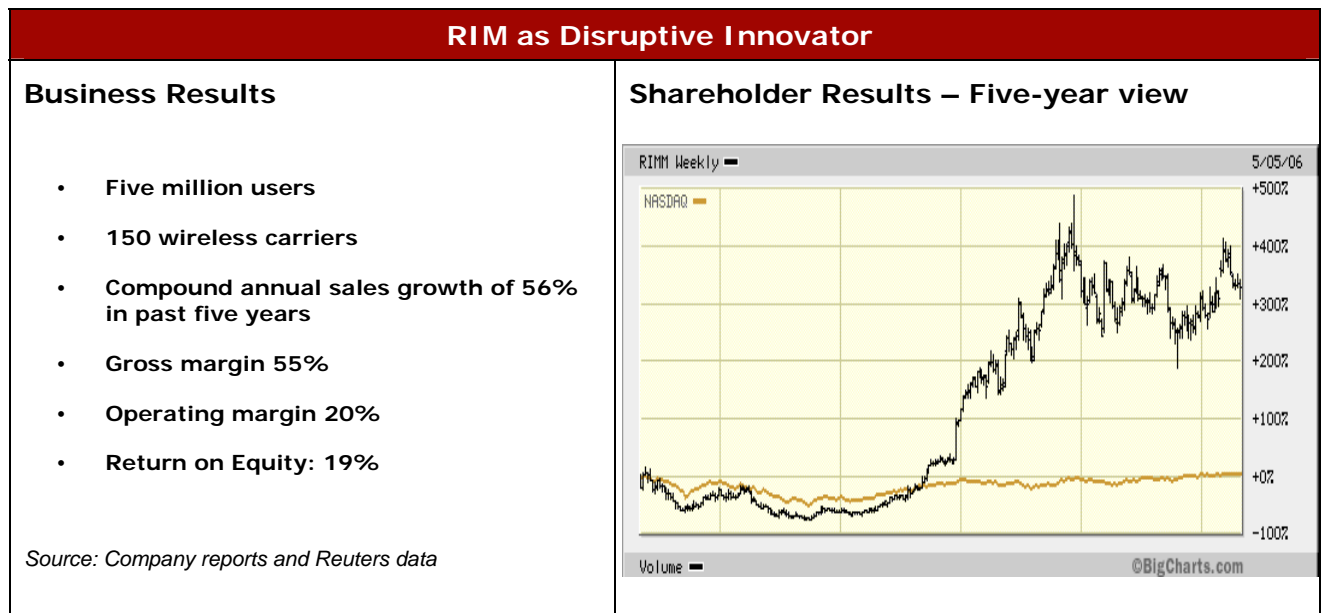
CASE 1: Research In Motion's BlackBerry Wireless E-mail

Released in 1999, the initial reaction from many prospective customers and competitors of BlackBerry was:

- It's not a phone
- It doesn't have a color screen
- The calendar is inferior to Palm Pilot

Further, the early BlackBerry was incompatible with cellular networks and was sold mainly by data-only companies in the U.S., not mainstream wireless carriers.

Yet BlackBerry achieved tremendous success by creating a new market. Why? RIM had created a new context for a known service (email anywhere) for a group of early adopters (Wall Street) who valued instantaneous information more than any of the product's limitations. And its channel, which operated 90%-underutilized proprietary data networks, was desperate for a hit. The result was that RIM disrupted the wireless data market.



II. WHAT IS DISRUPTION?

The framework presented here for analyzing disruption is based on 10 years of technology investment analyst experience and inspired by the breakthrough work of Harvard Professor Clayton Christensen. The key issue is that for new entrants today in many markets, superior product or service just doesn't matter. Disruption offers a framework for thinking about new growth.

Many markets are saturated by non-differentiated competitors with good or good enough products. Therefore to attract attention, companies should consider disruption as part of a strategic plan for new markets.

Disruptors				
Disruptor	Market Disrupted	Dismissed As	Success Factor	Annual Sales (\$M)
RIM BlackBerry	Wireless data	Not a phone	New context for email	2,065
Amazon.com	Book selling	Not for book lovers	New context for shopping	8,490
Whole Foods	Retail grocery	Hippy market	Underserved market	4,701
Blogger software	HTML web design	Amateur websites	Enabled amateur websites	NA(*)
Edward Jones	Retail stock broking	Low-value accounts	Underserved market	4,065(**)
Nortel optical gear	Long-distance	Excessive capacity	New interexchange telcos	10,000(#)

*Acquired by Google in 2003
 **Edward Jones: assets
 #Nortel: peak optical sales in 2000

Sources: OnDisruption.com estimates & Company Reports

While new entrants can occasionally crack a market by offering better product, this strategy is tougher now. In many markets consumers and corporate buyers have latched onto their suppliers and their trusted relationships. As a result, they are unlikely to be dislodged from their buying habits unless disruptive alternatives are available. The coffee chain that plans to compete against Starbucks by offering better coffee, faster service or cleaner washrooms just doesn't stand a chance in the mainstream. Likewise, the technology startup that plans to beat Cisco at their own game (faster, more secure routers, anyone?) seems relegated to a marginal position, no matter how much better their product is.

Therefore, disruption is best defined as an innovation that:

- Creates a new market or a new context for consumption
- Initially targets underserved or marginal customers
- Is perceived as inferior by existing customers in the mainstream
- Is highly valued by early adopters because of some new or different attributes
- Is simple to make and use
- Is improving in performance
- Requires a new business model

Disruptive innovation is a gradient and not all of these characteristics are required for success. But the more of these characteristics an innovation has, the greater its potential as a market disruptor.

CASE 2: Amazon.com

Innovations in service or in business model are equally capable for disrupting a market. Amazon.com, for example, disrupted the book market by innovating in service and by creating a different business model.

By the traditional measures of many book retailers, Amazon's business made little sense: Prospective buyers couldn't browse the books before they bought them; They couldn't touch the books; They couldn't get advice from sales clerks; They didn't get immediate gratification.

Amazon.com as disruptor	
Inferior points relative to mainstream <ul style="list-style-type: none">• Can't touch & feel books• No sales clerks to assist• No instant gratification	Superior attributes for early adopters <ul style="list-style-type: none">• Shop any time• Shop from home• Speed of transaction

But Amazon's customers were buying something they judged more important: Convenience. They could shop from home. Or while traveling. Or in the middle of the night. Many early adopters took their first look at the Amazon service during the holiday shopping season when convenience, speed and gift-wrapping are highly valued.

Today Amazon is not just a service used by harried Christmas shoppers. The key issue that brought Amazon into the mainstream is that Amazon's service improved dramatically to match or surpass market needs. Amazon has improved in terms of advice and reviews (from other book buyers) ability to browse (many books can now be searched online, and buyers can browse covers, tables of contents and excerpts online) and speed of delivery (one day for many products.)

III. WHAT IT IS NOT

Disruptive innovation is neither a panacea nor a prescription for all businesses. Many businesses survive and thrive without disruption. Disruptive innovation is difficult to achieve and may not be suitable for established suppliers in established markets because it does not support current customers. In fact, disruption goes against the grain of many business practices, especially the conventions of Total Quality Management and predictable marketing plans.

It's important to identify that disruptive innovation is not:

- A technology upgrade of a mainstream product
- A method to steal someone else's existing customers
- Targeted at mainstream customers
- Based on a known market
- Sold through mainstream channels
- Targeted at a single application or market
- Built on the assumption that mainstream customers will change

Many innovations in technology are branded disruptive when they are merely improved versions of mainstream products or services. Christensen refers to these as sustaining innovations and they are the stock in trade for most incumbent suppliers. Examples are: High-definition televisions, faster PCs, camera phones, organic groceries at Wal-Mart.

CASE 3: The Failure of GM's Electric Car

In some cases potentially disruptive technologies are co-opted by mainstream suppliers in ways that detract from the innovation. For example, General Motors' EV1 electric car failed because it was sold by a mainstream car company and was judged by the market to be inferior to mainstream cars, despite 23 patents, a long driving range between charges and \$1B in investment by GM.

In contrast, a small electric car can be disruptive if it is sold in the right market. For example, seniors living in gated communities in sunshine states already use golf carts to get around their neighborhoods because golf carts are cheap and convenient. So to these prospective buyers, an electric car with lockable doors and windows is an upgrade from the golf cart. And the slow speed and short range of the electric car are not seen as disadvantages.

IV. LIMITATIONS

Disruptive innovation is not an easy process for established suppliers in mainstream markets. It is generally suited to new entrants trying to break into markets. The execution of disruptive business strategy challenges many of the norms of incumbent suppliers, including definitions on target markets and ideal business models. Feedback from existing customers on a potentially disruptive innovation may detract from the innovation.

Take the case of electric cars. Drivers have consistently said electric cars need to have longer range. Why? Because that is the benchmark established by internal combustion engines. As a result, most failed electric cars have been saddled by very heavy and expensive batteries, in some cases, weighing in at over 1,000 lb and occupying valuable space in trunks and back seats. Yet, in the few markets where electric cars are successful, such as in corporate campuses, holiday resorts and seniors' communities, the cars do not have the heavy-duty battery capacity. Why? For these early adopters, convenience is more important than range.

Looking at Blackberry or Amazon, you can see that disruptive innovation can create large, profitable markets. Yet many of the requirements for business planning, such as market size, growth targets or margin requirements conflict with the requirements of disruptive innovation.

For example, established suppliers do not generally enter new markets that are difficult to research, small or unproven. And established suppliers do not pursue business opportunities that threaten their business or that of their customers. It is easy to understand why most record companies turned their backs on the downloadable music market: It threatened the core business and would erode relations with retailers. Yet, for Apple Computer, the downloadable music business made perfect sense because it had nothing to lose.

For this reason, it is difficult for disruptive innovation to thrive within mainstream suppliers, unless a high degree of autonomy exists in terms of establishing a new business model and a new cost structure.

V. ASSESSING A POTENTIALLY DISRUPTIVE INNOVATION

These questions are designed to generate discussion in evaluating an innovation.

Is Your Project Disruptive?	
Criteria	Questions
New market	Is the market unknown and unmeasured?
New customers	Are your customers ignored by the mainstream?
Product inferior relative to mainstream	Do competitors think your product is a 'toy'?
Product superior to early adopter needs	Are customers overjoyed by your product?
Off-shelf or standard technology	Simple? Easy to make?
Integrated product	Do you control or assemble all of what the user gets?
Performance improving	Is performance improving to meet market needs?
New business model	Is the business model different from incumbents?
Discovering the market	Is identifying the target market a work in progress?
New channel	Do you have to build a new channel?
Plan to learn	Can the budget accommodate early market failures?
Independent corporate structure	Are you a startup or independent unit?

Source: OnDisruption.com

VI. ABOUT MICHAEL URLOCKER



Michael Urlocker
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Michael Urlocker is a disruption consultant: Helping companies disrupt markets and helping them understand the forces of disruption in their industry.

Michael is a Chartered Financial Analyst and graduate of electrical engineering and journalism. He has nearly 20 years experience focusing on technology industry management issues and change.

Prior to founding the consulting firm OnDisruption.com, Michael was a senior technology and telecom investment analyst at several global firms, including UBS Investment Bank and CSFB. Michael has also worked as a financial journalist covering the telecom and technology sector and as a marketing consultant to the software industry.

If you want to explore how a disruption strategy can help your company regain growth, call Michael at (416) 363-5611 or email mike@OnDisruption.com.

VII. ADDITIONAL RESOURCES

www.OnDisruption.com, Online tools, articles and resources for managing disruption.

The Innovator's Dilemma, by Clayton Christensen, (Harvard Business School Press, 1997)

"How to Identify Your Enemies Before They Destroy You," Harvard Business Review: Nov. 2002; Farshad Rafii.

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