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Customer related innovations in the 21st century[☆]

Peter Lorange, Jimmi Rembiszewski

THE NEW CUSTOMER

A good understanding of the 21st century consumers seems to be key. In particular, it looks as if the relatively young, computer/IT-literate consumer ("Generation Y") is much different from what we have come to understand as the typical, classical consumer ("Generation X"). This "new" consumer may represent a real discontinuity from the past! The young, new consumer seems to focus relatively more on prestige and quality than on cost. He/she seems to appreciate and be rather willing to pay for innovations that enhance these dimensions. These dimensions, therefore, would be a much higher share of disposable spending among the new generation.

The Generation Y consumer can perhaps be seen as a person where his/her mind and the computer/other IT support work together, i.e. enhancing each other. This means more "capacity" for learning of basic facts, for storage of this, and for fast retrieval. Further, search-options are readily available when the Generation Y consumer would need additional information.

The above also has the effect that the Generation Y consumer can "free his/her mind" to concentrate more on new things, creativity, innovation, even prestige. The basic struggle to be cost-efficient would be more of a thing of the past, however.

We see many examples of this:

- Automobiles: Tesla — the all-electric passenger luxury car — is selling well, above all to affluent, younger consumers.
- Fashion: Branded fashion, such as Lacoste, Hugo Boss, H & M, and so on are particularly appealing to the younger consumers.
- Coffee: Nespresso has a series of fully owned; high-end centrally located stores, primarily for demonstration purposes. They distribute their coffee capsules in ways that Generation Y would be particularly comfortable with, namely via the web. George Clooney is projecting prestige in his promotions of Nespresso, particularly relevant for younger, high-end consumers!

Lego: Even the rather young consumer seems to fit into this. There is more value in today's Lego products from electronic chips than from the basic plastic! The product is adapted to the younger Generation Y-ers, and it is expensive!

This brings us to a key managerial insight when it comes to successfully coping with this emerging consumer, namely to come up with innovations that these consumers would prefer. We found that such innovations tended to represent incremental extensions of existing products or services, typically small innovations, but implemented quickly and with high frequency. The more successful ones do not necessarily follow old fashioned, more "narrow" definitions of benefits, as we, for instance, saw when phones became cameras. Thus, we found little evidence of large, "disruptive" innovations, carried out in central laboratory facilities, and with relatively long time horizons.

Effective communication of the particular innovations to the emerging key customers also tended to be of critical importance. The effective use of social media is a key — the web, blogs, apps, etc. It seemed as if the emerging consumer might act more favorably on communication that he or she saw as individualized, i.e. tailored, exclusively to him or her. More traditional modes of communication, such as advertising in newspapers, magazines or TV did not seem to be that effective. Thus, it seems as if many of the more traditional companies might lack credibility, in part due to ineffective communication!

There are many negative examples of this:

- Consumer goods: Our example might be Proctor & Gamble. Products are typically featured in TV-ads and in printed media, featuring advantageous price!

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- Retail: Again, we see promotions in printed media and on TV for these chains (Wal-Mart — USA, Tesco — UK, Migros — Switzerland, etc.), but profitability seems to be eroding!
- Automotive: Car companies are featuring ads on TV and in printed media — but to what avail? Sales are not increasing, and profit margins do not hold up!

In contrast, here are some examples of firms that seem to "communicate" effectively, in two ways mode with the modern customer:

- Tobacco: BAT build up an impressive market share for its brand KENT over the recent decade. They were not allowed to advertise! But, they made extensive use of social media — for two-way communication. They also became a main sponsor for Formula 1 race cars to add to the prestige of the brand.
- Retailing: FAST Retailing is growing very quickly. They source textiles from Asia. Their most profitable stores are in Tokyo and in Paris — focused on prestige and innovation. For instance, they have designed coats for cold climates (like Canada) as warm as heavy woolen, but as light as a feather. Heavy spending on R&D is key and social media played a central role.
- Airlines: While Ryanair is a discount airline, it focuses on experiential features that typical Generation Y consumers appreciate: flying in a modern, sporty way — in contrast to the more classical carriers. Profits and the number of passengers have never been higher!

We then found that for a company that would be able to pull off all these three features in a "good" way — i.e. a good understanding of the modern consumer, coupled with fast innovations to meet the preference of this group, and also, with effective communication of these innovations to the target customers — would be able to charge a relatively higher price and also to sell more. The result would thus be growth both in the top line (sales) and in the bottom line (profit). This finding seems to be in stark contrast to the conventional business model involving product margins and the use of heavy discounting. Many firms seem to put insufficient emphasis on the task of always "delivering" on innovations. This, in turn, becomes a key reason for margin erosions for these companies.

Let us now discuss in more detail each of the critical steps in this emerging business model, and also with focus on the underlying research.

The result of our study is a preliminary articulation of a theory for coping with today's key challenge when it comes to successfully catering to the modern consumer, i.e. a "post — product manager" theory! While we believe that this integrated theory is realistic when it comes to demystifying today's key dilemma of "higher growth — lesser profits", but, in contrast, offering prescriptions for "high growth — higher profits". We fully acknowledge the need for more research — not only when it comes to modern consumer behavior, cutting-edge innovation management and more effective approaches to communication, but, above all, exploring further the key interdependencies between these factors.

THE EMERGING CONSUMER (GENERATION Y)

There seems to be a discontinuity between the typically, relatively young, fully computer/IT-literate individual ("Generation Y") and the typically, somewhat older, traditional consumer ("Generation X"). Consumer preferences have always evolved. However, until today, there seems to have been continuity here. Now, in the 21st century, however, we seem to find a clear discontinuity between the newer breed and the traditional. Berkup was perhaps the first to denote people who have essentially not adopted these recent technologies as "Generation X", and those who have adopted it in grown-up life as "Generation Y". He further contrasts those with "Generation Z" which indeed has grown up with modern communication technologies. His research, as well as that of others, seems to indicate that there is a discontinuity between Generation Y and this new Generation Z and previous generations (X). Quality, prestige and ability to pull off innovations quickly seem to be relatively more important for Generation Y than Generation X. Brand image is key as well, in the sense that these might reflect quality, prestige, trust and, above all, dynamism.

We found that Generation Y consumers that tends to be where the purchasing power is! They seem to have the economic means. Their professional backgrounds, so often found for this group of young consumers, also make them particularly attractive for appreciating innovations. Even though we did not find the more traditional (Generation X), typically relatively older consumer to be central for our context. These people tend to be more driven by issues such as health, safety, dietary food issues, etc. Costs seem to be a key factor here. It is interesting to note that the typical consumer in leading discount chains such as Lidl or Aldi tend to be relatively old. Thus, the logic here is: Products that are not supported by innovations might typically quickly become commodities, and this would allow for non-branded products to enter the market. For example: Classical Swiss watches that are not making use of the modern electronics dimension might perhaps be expected to gradually fall behind. Apple has just introduced its new electronic wristwatch, a formidable competitor to the Swiss! Some Swiss prestige brands are following suit: Hublot is now working with Microsoft! And, its charismatic CEO, Jean Claude Biever, has become head of the entire watch sector for the prestige-goods-producer Richemont — he is known to make innovations happen!

In contrast, let us take the food industry. Private branding, say, in canned food, has led to an almost non-existence of innovation, and depressed/low prices as well!

These latter might nevertheless capture significant market shares within their categories. This, in turn might lead to the older group of demographic customers buying at discount outlets such as Aldi or Lidl. The owner of a Porsche might thus buy detergent at Aldi/Lidl, and a 100,000 SFr. watch at Cartier! So, for this more traditional group of (older) consumers the conventional concept of lowering one's price (for commodities), in order to sell more, seems to hold.

INNOVATIONS

Clayton Christensen of Harvard Business School has identified 3 types of innovation:

- *Efficiency enhancement* — so as to essentially be able to continue to stay in business. We see many examples here. Some might be retailers such as Wal-Mart, with its new store layout. Others might be firms such as Tesco, with its new home delivery concept. A third group might be retail groups like Migros, with its new Migrolino concept of stores integrated with gasoline stations.
- *Incremental improvement* — so as to essentially improve on the performances of one's product and/or service, to make it more attractive. The automotive sector comes to mind. The Volkswagen group, for instance is "cascading" its technical incremental improvements, typically stemming from R&D, first from its Audi brand, then to its VW brand, then to its Skoda brand, and finally to its SEAT brand. The push-button ignition system, no longer requiring an ignition key is one example — initially introduced at Audi, and not yet diffused to SEAT.
- *Disruptive innovations*: — which are truly earth-shaking, in the sense that these would represent fundamental parameter shifts on "game changers" for a given business. The classical example here, of course, is Apple. Not only did they come up with a disruptive innovation when it comes to the design of iconic new products such as the Macintosh, the I-pad and the I-phone, but it has also come up with disruptive innovations when it comes to distribution — cult-creation, in marketing to early adopters, for instance, drawing heavily on social media. Prestige stores for demonstration, and "to be seen" are also key

We found that such fundamental disruptive innovations could be rarely observed among the companies we considered. Rather, the primary emphasis seemed to be on carrying out incremental innovations, each one typically relatively small in their own rights. What seemed key is that these typically were introduced on a rapid pace. The task of pulling off innovations tended to be the responsibility of the line — and not so much by central R&D laboratories — and with a clear focus on coming up with novelties that the key customers would appreciate and be willing to pay for. Innovations that might fall into this category would be new generations of branded products (fashion, colors), further technological niceties (speed, capacity, features) etc. These would typically tend to satisfy the relatively young customer — prestige and quality is key!

We found one example of what might be seen as a disruptive innovation, coming about as the sum of several incremental innovations, namely the so-called SAVER container ship. Several incremental innovations had to do with enhanced performances for hull, underwater coating, rudder and propeller. Others covered improved machinery efficiency and better fuel systems. Still others had to do with reducing environmental pollution through improved waste energy recovery, ballast water treatment plant, better garbage compactors and tin-free anti-fouling paints. It all came together through a better overall ship design. This also encompassed further hull form optimization and innovations regarding trim and draught optimization. So, in sum, there were several dozen incremental innovations, which, when being put together into one vessels concept for a next-generation container ship, the SAVER, might be considered one disruptive innovation!

The customer was indeed behind this these innovations — in this case the container liner operators who were searching for container ships with significantly higher performance, both when it came to fuel efficiency, cargo-holding capabilities, and improved environmental pollution features. Seaspan, a large ship-owning company, developed the SAVER design, for a relatively large high performing container ship (10,000 TEU capacity), which it offered major container liner companies on long-term leases. Most of the various incremental innovations that came together in Seaspan's revolutionary design — aggregating to one disruptive innovation — were clearly more or less available — it was the "putting together" of all of these by Seaspan that thus created the disruptive innovation. In general, the ability to put together several smaller, at first relatively unrelated innovations into fewer, larger ones seems key — often these latter may then be seen as examples of "disruptive" innovations.

We also saw how various specific stakeholder forces might attempt at slowing down the introductions of disruptive innovations — in the case of the SAVER example by at least three such stakeholder groups:

- Shipyards, which were typically making their financial returns through building relatively long series of ships, of relatively standardize design. Innovations were not on their agendas! This could only be done, however, as long as there would be a relatively strong backlog of new orders for ships. When this backlog shrank, the yards would typically be much more willing to discuss innovative designs, such as SAVER.
- The liner companies. e.g. China shipping, Cosco, Evergreen, MSI, Yan Min, and others, just to name some container liner names that have adopted SAVER.

  These would already own or have taken in on charters more conventional fleets of ships, i.e. with more conventional performance characteristics. With the emergence of the disruptive SAVER innovation, they would have no choice but to adapt to SAVER, so as, to stay competitive. The old fleet, however, would have to be sold or chartered out at relatively unfavorable prices. Several container lines thus resisted the SAVER innovation and especially that this was forced onto them!
- The banks. Similar to what was the case for container lines, the ship values of the old fleet would typically fall dramatically — economic lifetime would become significantly shorter than technical lifetime! This was resisted by several banks, which would face potentially significant reduction in ship value as a result.

We also found that there were often a built-in conflict between those that were key drivers of the various innovations initiatives — typically from the marketing side — and those who represented the operations of the company — this latter group typically having a propensity for more stability and fewer changes. This sense of balance between adaptation/change/complexity vs stability/simplicity was utilized by B.A.T., with its Kent brand, in its efforts to make competitive in-rounds on Philip Morris (Marlboro Brand). B.A.T. introduced many relatively small innovations for Kent (multiple flavors, tar strengths, color codes of packaging's, etc.) Marlboro had developed a very efficient operation involving a highly standardized purchase offering for Marlboro. Philip Morris's organization found it difficult, accordingly, to suddenly have to shift mode of operation, to now being able to respond, fast to a multitude of relatively small competitive moves from Kent. Philipp Morris had standardized its production and distribution to a large extend, based on the fact that they basically only handled a few products (Marlboro) and only in a limited number of varieties. This gave them a clear advantage, on paper, regarding benefits from economies-of-scale. But, as it then turned out, both its production organization and its distribution organization found it difficult to abandon this propensity toward long runs and standardized distribution. BAT, in contrast, with its "guerilla" tactics, were able to adapt faster, and in a more flexible way.

Let us take another example — banking. Social media providers such as Facebook and Google do have banking licenses. And they do not think as a traditional bank either. For them the key is the (Generation Y) consumer — with their needs for insurances, money transfers, etc. — to be fast and done in a, for them, comfortable way! A typical bank, on the other hand, tends to be more "trapped" by its history and tradition — "this is the way we have always done it", i.e. built up over a long time to be serving Generation X!

There are several implications from our findings regarding innovations:

— Central R&D organizations seemed to be in the decline. The once-upon-the-time focus on coming up with truly earth-shaking major innovations, often as a result of multi-year processes, seemed to be on its way out. The search for disruptive innovations was generally not that much pursued.
— Line managers, being close for the customers, would in contrast then typically have a major responsibility when it came to innovations. These line executives would primarily be focused on achieving increased sales, and would hence emphasize innovations that might support this — typically relatively incremental/small, and launched in a speedy way.
— Key customers can be found anywhere around the globe (although one might argue that certain specific geographic areas might be particularly central when it comes to particular industries — California for modern IT technology, Paris/Milano/London/NYC when it comes to high fashion, for instance). We saw a clear trend toward so-called reverse innovation. John Seely Brown calls this "innovation blowback". These are innovations that initiated away from the central headquarter, even often at quite a distance! Let us take packaging at Nestlé as an example. Nestlé is headquartered in Vevey, Switzerland. But, its major packaging expertise comes out its Brazilian subsidiary in Sao Paulo. The Brazilian market would call for more varieties in packaging, above all, convenient smaller packs to provide inexpensive innovations. It turns out that this approach has world-wide appeal! Another example would be the trend for many traditionally Europe-based shipping companies to relocate their shipping operations to Singapore, even though headquarters would still be located in Europe. The ability to operate large fleets in more cost-effective ways, including better recruiting, more effective training and the setting of more modern work routines seems key.
— Although not based on strong empirical evidence, it seemed to us that what might be labeled as formerly Eastern European consumers might often be faster adapters of innovations from their Western European counterparts. Regulations to "protect" the consumer might, for instance, not be so "light" in many of these markets. Japan Tobacco International (JTI), for instance, exports almost 80% of its cigarettes produced in Switzerland to North African and Middle East markets — these cigarettes being considerably stronger in nicotine content than what is allowed in Switzerland. To produce high-strength cigarettes in Switzerland is however allowed. Consumers might be ready to adopt innovations, such as cigarettes with high-strength nicotine content, when national legislation allows for this.

We were however not able to detect more detailed specific step-by-step processes when it came to the task of executing innovations. Furr and Dyer, for instance, "have attempted for chronicle the process of innovation from beginning to end — laying out the static and dynamic interdependencies that historically have made innovations so hard". Exhibit 1 gives a snapshot of the model for the innovator's method.

We were specifically not able to come up with these specific stages, nor with the associated key activities, tools, tests for each stage. Our sense is that Furr and Dyer, seem to consider the tasks of innovation as primarily one that would be carried out by a cadre of specially assigned innovators, and with these having their own and different DNA. At Nestlé, for example, the bulk of the innovations seems to be driven by the line, often through Nestlé's country organizations, but at times also by its SBUS. Innovations thus seem to be clearly linked with improving specific market positions.

We also did not find any resemblance with Spar et al.'s phases for earth-shaking developments. First, Innovation, then Commercialization, then Creative Anarchy, and finally Rules. Rather, our findings seemed to be different: An ongoing, almost circular process of customer wishes/demands, followed by incremental innovations in business that already exist, followed by effective communication of this to an

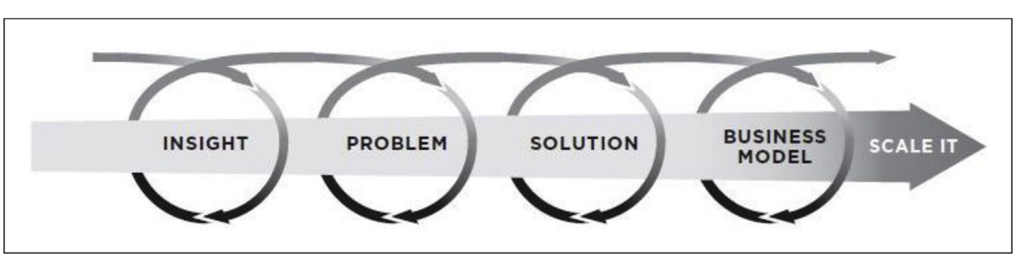

Exhibit 1 The innovation process.
Source: Furr and Dyer, 9.

already established customer group. Thus, while the process that we found might be labeled "making good even better", i.e. incremental, building on already established businesses, other researchers, in contrast, seem to be focusing on the creation of something "entirely new". Thus, we found that the tasks of pulling off effective innovations might be seen much more as part of the line's general efforts to be successful in business (achieving a competitive advantage, gaining market share, securing more robust profit margins, etc.). Let us refer to Nestlé again. This company has a large, central R&D facility outside Lausanne, Switzerland. In the past this was truly central, serving the entire firm. Now, however, each global products SBU "controls" part of the facility — R&D is thus now much more driven by the particular market/key customer considerations that each particular SBU is facing.

Let us focus on efficiency-enhancing innovations. These clearly were at play all the time, but could be seen almost as a condition for maintaining the status quo of being in business. By not adhering to this, one might expect to eventually be forced out of business. For instance, we no longer find once strong brands such as Borgward (automobiles), Sabena (airlines) or Champignent (beer), just to name a few.

Perhaps the most provocative finding was that many of the more traditional companies seemed to be too much bound by (limited by) their own brands, e.g. Procter & Gamble's (Trident and Crest brands). For them, own brand strength typically seemed to be seen as a key part of their strategies. This would be in contrast to many members of the newer generation of companies, from the modern "E"-world, that where "reinventing the game" — from phones to cameras, from computers to play stations, and so on.

EFFECTIVE COMMUNICATION

Essential to communicate one's innovations effectively to the target group of customers. Speed is key here too! We often see that good innovations are left "undiscovered" by the target customers — inadvertently creating "hidden champions". Lack of effective communication is often the reason.

Modern social media are key. A good web page is clearly essential! But, as we all know, to develop a new web page may typically take time. Unless one's web page is designed in such a way that it might easily incorporate the most recent innovations, to rely on a semi-outdated web page may not be good enough. Rather, tailored apps, tweets, blogs, etc. might have to be it! It seems key that the typical consumer in the 21st century actually wants to be part of the communication process. This is a two-way process, not one way! We compared this to the Lego experience where the customers build their own models — the act of creating one's own model might be seen as a part of a two-way communication process!

What is important is that a typical target group customer would expect — and appreciate — individualized communications. They relish exclusivity — i.e. "me only"! Social media is set up to achieve this! Social media-derived communication capabilities increasingly were resting with the line, rather than with centralized communication specialist groups. For example, let us refer to Nestlé again. While a social media expertise is built up centrally at Nestlé's headquarters in Vevey, it is the various line-units that draw on this capability. So, in effect, all social media communications are driven by the line.

The emergence of a new key integrative managerial capability is facing operations: the task of understanding the emerging group customer, coupled with the ability to come up with fast, relevant innovation, and also coupled with an ability to stimulate a communication among them in an honest way. The role of the line, and definitely the role of the traditional product manager have thus fundamentally changed!

It goes without saying, because of its one way communication side, that traditional advertising, via print or TV, does not seem to work well enough any longer. The same can be said about reliance on the press (through press releases). Several classical players, businesses and professions may thus now be on their ways out: the classical advertising-driven newspaper, TV stations funded on TV ads, conventional advertising agencies, etc.

TOP LINE AND BOTTOM LINE GROWTH

We found that, for those business players that had this triplet of challenges "right" (customer understanding; effective and fast innovation cycles; effective communication) the results seem to be dramatic — highly desirable and rewarding, with both growth in top-line and in bottom-line!, i.e. both more sales and more profits! Why? To achieve higher sale definitely seems to be a function of having relevant "modern" products to offer. Sales are achieved when the consumers have their demands met! And, with modern products, which would be in high demand, the firm would be in a position to charge higher prices, and hence, enjoy a larger profit! Other researchers have emphasized the importance of having a modern product offering — but the above-mentioned "triad" of key, interrelated factors (understanding of Generation Y, customers/relevant innovations/targeted communication) has not been discussed before.

Another finding is that classical discounting may no longer be the way (Kotler). The classical product manager, in particular, who bases his/her tasks on a product management model pioneered by P&G and others (Lafley and Martin; Popelka) may no longer work. The dysfunctionality of this model might go as follows: A particular product manager might find him/herself under pressure to show increased short-term sales volumes — his/her annual bonus might even be at stake! The next big strategy innovation may be, say, three years away! Discounting, and promoting private brands might thus be an immediate solution. But, the result would be lower margins, i.e. lower bottom line, even though the top line might be growing! The net effect would be that there might be even less resources available for innovations and further product development, especially, since the often faster erosion of one's premium priced brands! The particular business becomes less-and-less successful. Its customer franchise is being eroded! And, in the end, the business may pre-maturely cease to exist!

CONCLUSIONS

Based on the exploratory study reported in our book (Lorange and Rembiszewski) we have found that the emerging 21st century, youngish, fully computer-literate consumer ("Generation Y") is different from what we traditionally might find. He/she thus values different forms of innovations from what has become the key in the past: relatively more focus on fast, unexpected features and quality, and on fast delivery! All of this must be communicated to this target group, again — fast. Social media, with its focus on two-way/one-to-one communication, seems particularly effective.

The result of having this triad of factors "right" and executed in an integrated way by the line, would be more sales and higher profits! This new business model seems to be on its way in, replacing the traditional product managers-based one.

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Peter Lorange is the founder and President of the Lorange Institute of Business Zurich (since August 2009). Formerly, he was the President of IMD from July 1993 until April 2008, where he was Professor of Strategy and the Nestlé Chair. Peter was previously President of the Norwegian School of Management in Oslo and, earlier, affiliated with the Wharton School, University of Pennsylvania, for more than a decade. He also taught for eight years at the Sloan School of Management (MIT). Peter Lorange has written or edited 18 books and some 120 article. He has a doctorate in Harvard, and also holds 6 honorary doctorates. His areas of special interest are global strategic management, strategic planning, entrepreneurship for growth and the shipping industry (Lorange Institute of Business Zurich, Hirschackerstrasse 46; CH-8810 Horgen, Switzerland. Tel.: +41 79 212 9203; email: p.lorange@lornge.org).

Jimmi Rembiszewski spent the first 10 years of his career with Procter & Gamble. His first Board role came in 1988 when he joined Jacobs Suchard as a member of the board for New Brands, Research and Media. In January 1991 he became Business Development Director Worldwide, Confectionery Sector, with Kraft before joining British American Tobacco as Marketing Director and Regional Director Europe in August that year. In 1996 he became a board member of the new BAT and remained as Marketing Director for the group until his retirement at the end of 2009. He is a member of the faculty at the Lorange Institute of Business, Zurich, where he lectures on marketing for a number of executive programs, including the Executive MBA, Modern Marketing and the Executive Master of Science in Management (87 Belsize Park Gardens; NW3 4NJ London, UK. Tel.: +44 7711 411 432; email: rembiszewski@hotmail.co.uk).