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# Managing CUTS and New GROWTH

an innovative approach  
to change management



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Two tips for criteria definition:

1. Since hard cuts reinforce a deficit-oriented attitude, it is important for each target group to ask:
  - What do we want to achieve (e.g. in relation to high performers)?
  - What do we want to avoid by all means?
  - What do we want to preserve?
2. Also include externally orientated criteria that encourage innovation- e.g. customer satisfaction in the downsizing phase.

A core team continues to deal with steering and monitoring the process; the responsibility for the substantive implementation lies above all with executive management. Their interventions are primarily of a clarifying, stabilizing nature, i.e. balancing uncertainties and turbulence, and generating trust and commitment for new growth. This requires new managerial skills in understanding the logic of feelings in changes. Our observations of how managers react personally in these situations have clearly shown us: the way we deal with the feelings of others usually mirrors how we relate to our own emotions.

## 5. New growth

The world market leader in truck cranes has consistently expanded its product range in recent years with new lifting aids for industrial use. Now, a new idea is revolutionizing the entire company. In future, business will no longer focus on developing individual new products, but on acting as a service provider and systems supplier for the entire logistics chain: “E-logistics” is born. A new business area is being established, Internet startups are being bought up and integrated and new distribution channels are being created.

“New growth” describes the side of transformation that is about “reinventing” oneself. Ideas, courage and an eagerness to experiment are what is needed. At the center of attention here is the entire corporation’s innovative force. But here we are not – as is usual – considering this innovative strength directly in relation to product innovation, but rather in relation to the readiness and the ability of the organization and the people involved to develop and test innovations and promote them during implementation.

Not only new products, but also new business models or core processes can be objects of innovation. In other words, it's all about the innovative capacity or innovativeness of the company. Innovation experts (e.g. Tushman), strategy and corporate development experts (Leifer, Schrage or Hamel) and knowledge management experts (Nonaka, Takeuchi, von Krogh, Ichijo – see the bibliography for more details) deal with innovation in this sense.

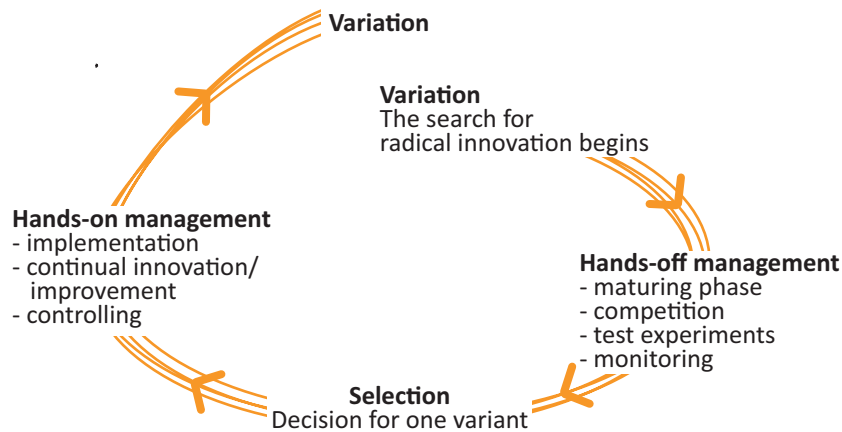
In order to differentiate the intensity of innovations, we find the following distinction important: Evolutionary innovations have the goal of becoming faster, better, larger, more efficient or more comprehensive. It is a matter of optimizing the existing (“exploitation”), regardless of whether one is dealing with products, services, business processes or management systems.

*Radical innovations, by contrast, effectuate new breakthroughs (“exploration”). They presuppose a perception of things and standards that are different from what is customary. This is the variant of new growth that we are interested in here.*

*As the following diagram shows<sup>19</sup> radical innovations call for a steering mechanism quite different from that for continual improvement (evolutionary innovations) or hard cuts. The innovation side of a transformation process follows a logic that is completely different from that of day-to-day operations and also different from that of hard cuts, both in terms of figures (focusing on future potential rather than on short-term cost minimization and profit) and feelings (a spirit of optimism, animated curiosity and a readiness to take risks rather than the worries, anxiety and also aggression associated with hard cuts).*

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<sup>19</sup> According to Tushman; c.f. Hambrick, p. 331.



### What's special about new growth: facts and figures

In Fortune Magazine's annual rating of the "most admired companies", innovative power is the foremost ranking criterion. Financial analysts also rank innovation at fourth place in immaterial criteria for investment decisions.<sup>20</sup>

### Success factor: radical innovation

*"Sometime over the next decade your company will be challenged to change in an unprecedented way".<sup>21</sup>*

Of the nearly 2,500 executives BCG surveyed worldwide in the innovation study 2007, only 46% said they were satisfied with returns on innovation spending, compared with 52% in 2006. Two-thirds (66%) said they considered innovation a top-three priority, versus 72% the prior year, and 67% said they plan to increase innovation spending, versus 72% the year before.<sup>22</sup>

**Radical innovations** result in the highest yields, whereas evolutionary innovations bring an average yield only. Among 108 companies, 86% of business ex-

<sup>20</sup> Becker, Huselid, p. 9.

<sup>21</sup> Gary Hamel, *The Future of Management*, Harvard Business School Press, 2007.

<sup>22</sup> BCG Study Finds Executive Frustration with Innovation Rising Around the Globe  
[http://www.businesswire.com/portal/site/google/?ndmViewId=news\\_view&news-Id=20070801006536&newsLang=en](http://www.businesswire.com/portal/site/google/?ndmViewId=news_view&news-Id=20070801006536&newsLang=en)

pansion emanated from existing competitive business. This type of expansion produced 62% of total revenues but only 39% of total profits. Blue ocean businesses (Businesses that focus on innovations) almost reverse the figures: their expansions accounted for 38% of total revenues and 61% of total profits.<sup>23</sup>

**Radical innovations** particularly emerge in enterprises with: high functional orientation and high flexibility (unbureaucratic), with long-term strategies or visions, highly diverse and creative staff, stronger focus on service than technology, and a high level of enthusiasm for change.

#### **Radical innovation as the invention of new business concepts**

*Who has been most able to exploit the changes in your sector in the past 10 years?* The most frequent answer to this question is: newcomers, by “changing the rules of the game” (discontinuous, radical innovation). There are definite limits to one’s own power of imagination. Most members of one sector share a common blind spot, focusing on or disregarding the same areas. This marks the other side of radical innovation: the difficulty of breaking free of the daily routine of day-to-day operations and perceiving things in a radically new way, thinking and making decisions “out of the box”. Pushing forward radical innovations is one of the greatest challenges in management.

#### **Best practice – top performers’ strategies for more innovation**

Promoting – or even better, provoking – new growth of this nature is no trivial matter. On the one hand, it means abandoning unquestioned elements of day-to-day business (reality constructions, implicit images and assumptions about oneself, customers, competitors, the market, managers, employees, as well as action & decision-making models that may have proven successful in the past). On the other hand, it also means promoting openness and incentives, so that something “totally different” can emerge and mature. So what type of management intervention is required?

The following features are what makes the top performers among the most innovative companies stand out from the rest.

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<sup>23</sup> Kim, Chan and Mauborgne, Renée, “Blue Ocean Strategy: How to Create Uncontested Market Space and Make the Competition Irrelevant”, Summarized by permission of Harvard Business School Press, Copyright 2005 Harvard Business School Publishing Corporation

**Innovation is a fundamental capacity** in these organizations and not merely a matter of launching new products.

If we make a distinction between managed innovation (systematically planned, focusing on many evolutionary innovations) on the one hand, and open innovation on the other (flexible, less structured, interactive, networked and open for all types of (even radical) renewal, where the development of new things has a value of its own and innovation is a core competence), we see that open innovation dominates among the top performers in innovation.

**Openness and protection for new ideas:** New ideas – no matter where they come from – are gathered, concretized and tested in a protected environment. Top performers assess new ideas much later than others (protection in the vulnerable phase!). Incentives and reward systems promote innovation and attract risk capital, serving to promote the development of ideas without the usual restrictions.

**The company culture and working climate in the top performer companies is characterized by the following:**

**Employee involvement** in setting challenging goals motivates and generates energy.

Generous leeway in the organization of work and communication, and good networking (information, knowledge exchange) are important motors for motivation and innovation (trust and openness as maxims). These companies have defined or standard time resources for the investigation and discovery of ideas and potentials (in contrast to less innovative companies, where high operative time pressure is common).

**Support for ideas and productive debates:** top performers avoid premature appraisal and criticism; instead, they utilize specially developed creativity tools and team processes that promote the flow of ideas, diversity and contributions from all sides (intense utilization of IT in the idea management process, IT as a marketplace), the overall idea being to challenge each other productively with critical questions. The criteria by which performance is measured also permit taking risks and experimenting. Leadership in the top performers is not “top-down”, but rather situational, moderating and encouraging, creating an inno-

vative climate. The development and selection of managerial personnel plays a vital role.

Employees who prove to be “innovation champions” are profiled as role models in the most innovative companies. Customers and value-adding partners are involved in the innovation process.

## 6. Management agenda for the development of radical innovations: what to do?

This section focuses on the developmental phase of radical innovations. These cannot be forced or directly managed. They call for opening interventions that cultivate fertile ground on which innovations can grow and flourish.

- **Challenging images and visions for the future:** these make it necessary to develop new perspectives and to think differently from before. They work like magnets, bundling and aligning energy and attention.
- **Autonomy** provides time and resources for dealing with what is new. Tolerance for errors and freedom of movement enhance motivation to familiarize oneself with and work on new topics. The organization facilitates knowledge access and networking opportunities.
- **Redundancy** (through common language and experiences) raises team’s potentials for finding new solutions. This is often endangered by downsizing processes, particularly when companies centralize or decide that certain competencies need only be fostered and developed by a single agent.
- **Internal diversity** reflects the complexity and dynamics of the external market in the company. Differences are openly acknowledged and freely accessible (open communication, informal, strong communication culture; “Communities of Practice”).
- **Creative chaos, flexible alliances and internal fluctuation** prevent one-dimensional departmental thinking and functional barriers to the perception of innovation (career paths with overlapping functions, opportunities for exchange in informal, self-steering networks).

### Barriers to innovation

Innovations can also make hard cuts necessary. This happens when their implementation requires the abandonment of familiar, historically successful core

elements of identity<sup>24</sup>. Karl Weick investigated this phenomenon in his study “*Drop your tools or you will die.*”<sup>25</sup>

Karl Weick specifically investigated the reasons for the reluctance to abandon accustomed tools when in danger. Basis for the investigation were examples in which experts (e.g. firemen, pilots and seamen) did not drop their profession-specific “tools” in crisis situations, and thus put themselves in great danger, or even died. A frequent example were firefighters who were unable to escape forest fires in time, because – despite repeated exhortations – they refused to leave their heavy equipment behind. After all, it had served them well in the past. “*Drop your tools or you will die*” is therefore synonymous with flexibility and the ability to let go of the “learned and accustomed”. Learning to understand the urge to hold on allows one to create more leeway for innovation. The lessons learned from these accident studies can easily be transferred to organizations. So why are customary tools not abandoned? In-depth interviews revealed the following barriers:

- The message “drop your tools and run” is not heard.
- The rationale and urgency to do so were not communicated.
- If the unaccustomed instruction “drop your tools” comes from strangers or individuals who are not trusted, it remains without consequence.
- The tools give their owners the feeling of acting effectively, of being able to influence their environment; they provide emotional security, especially in dangerous situations.
- There is often not enough practice in letting go of one’s own tools quickly and effectively – someone unused to improvising feels paralyzed and helpless.
- The action that is to be taken without the tools is unfamiliar and frightening, was never tested. The new, which is supposed to take the place of the tools, is unknown. Abandoning the tools would mean admitting a mistake, having failed as an expert.
- Social dynamics take effect – if others stick with their tools, the conviction “*It’s not that bad, we don’t need to do anything different*” takes hold.

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<sup>24</sup> This is probably also one of the main reasons why newcomers to a sector (62%) are usually the ones to fundamentally change its ground rules (Gallup poll; c.f. Hamel, p. 23).

<sup>25</sup> Weick, 1996 (see bibliography).

- The conviction that dropping the tools would not make a big difference is prevalent.
- Tools are the expression and symbol of professional identity. What are managers or experts without the tools, systems and instruments they use?

The BCG Innovation report 2007 lists the four biggest obstacles to successful innovation:

- A risk-averse corporate culture
- Lengthy product development times
- A lack of internal coordination
- Difficulty in selecting the right products to commercialize<sup>26</sup>

But what can be done to make “letting go” easier and to overcome innovation barriers?

1. Increase attention and send out very clear messages, particularly in upheaval. Check whether they have “arrived”.
2. Make a strong case for action.
3. Strengthen trust in stable networks.
4. Steering and the ability to maintain control are based on knowledge: *“If bad comes to worse, we’ll switch to “autopilot” and revert to the old pattern (“panic button”); it’s hard for us to accept the vacuum between old and new.”* Address this phenomenon and provide encouragement with personal examples.
5. Learn and practice releasing the burden of knowledge and tools; being able to let go – as a management exercise, repeatedly create new contexts for practicing letting go.
6. Increase the ability to improvise and to employ substitute actions. Practice error-friendliness (particularly difficult for experts).
7. Scrutinize social dynamics, in particular those of groups; highlight the risk of “majority ignorance”; make dogmas visible.
8. Practice for emergencies (*“what do we do if”...*); achieve a new identity by taking creative alternative action.

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<sup>26</sup> “Implementing your Strategy through your People Innovation” in: The Executive Issue #33, Management Center Europe, July 2008.

Interventions that promote innovation also destabilize and initiate “productive clearout”. They create new challenges for which “conventional approaches” are deaf. And they generate energy, incentives and a productive setting for the development of inventive, new answers. This also means that managers face new challenges. “Un:balanced Transformation” can mean questioning or abrogating “historically successful functions” to create space and energy for new ways of doing things. This requires foresight, thinking outside the box, courage for productive “destruction” and the power of persuasion, coupled with determination. In terms of function and emotion, this is an immense task, as it means utilizing the gap between insecurity, risk and openness for the future. Radical innovations always go hand in hand with positive turbulences.

## 7. Ten ground rules for a climate that promotes innovation

### Incentives and interventions for innovative organizations and corporate cultures – innovation rules

1. **Create challenges by setting dreams and (seemingly) impossible demands as goals.** They make it clear that “more, better, faster” do not suffice, that new thinking is in order and that intensity (speed, energy and resources) is necessary for innovation.
2. **Expand and stretch the limits of your own field of business.** What is at the forefront and drives us on are missions and meaning, not the existing business. These are what gives us the courage to venture out and to write off previously acquired social and intellectual capital (e.g. Virgin Atlantic: “*Our business is about creating memorable moments for our customers*”; Schwab: “*We are the custodians of our customers’ financial dreams*”).  
Radical innovations arise from “new” and creative ways of defining problems and asking questions. New mental images and widened horizons reveal new landscapes for innovation, different from the usual ones which allow only gradual improvements (at best).
3. **Exploit differences as a productive force,** challenge and question contrasts – this is one of the most important motors for innovation. In order

to achieve this, differences must first become visible. Bringing together multi-perspective ways of looking at things in interactive settings makes differences transparent and creates fertile ground for new ideas (“Customer Parliaments”, empathetic customer observation (video) and evaluation by interdisciplinary teams, scenarios with the most innovative customers and partners). Teams and large group events are particularly suitable for reaping ideas and improvement from the productive force of differences.

**4. Let new, revolutionary voices have a say:** Whoever “thinks young”, has recently joined the company, is a specialist in another field or is inexperienced in the area at hand can effectively question and identify the “old boys” perception barriers and – what is more – bluntly bring the most impossible ideas into the game. Inverted mentoring – when senior managers select young, high-potential employees and learn from their views on trends and the future – is an intervention in this direction, as is the “shadow cabinet”, where teams of “young lions” work out the priorities they would set as a management team. This is often discomfoting. “Difficult adapters” and headstrong lateral thinkers often make an unwieldy first impression and are rarely perceived as productive in the classic sense. But innovation calls for people other than CIP experts. Other voices also get a say when companies tune their aerials to the periphery – actively bringing in experts or new employees from the outside (especially from other sectors) and utilizing their resources. This also includes consulting and involving employees who are not part of the established center of the enterprise, but rather act “on the fringes”.

#### **5. Create open markets for ideas, capital and talents**

- **Ideas:** Interactive large group events such as open houses or internal innovation trade fairs – perhaps also with customers, where supplies and demands are negotiated – are examples for open markets.
- **Capital:** “Business Angels” can also be established as risk capital providers within the company; innovation budgets with competition-oriented ground rules create market-like situations and incentives.
- **Talents:** Facilitate personnel changes (e.g. link titles to individuals, not to positions; issue phantom shares for founding teams in new areas etc.); attract resources (pull effect) instead of distributing them.

- 6. Promote a large number of quick, low-risk and small-scale experiments.** This poses two challenges: the protection of ideas (do not submit them to stringent ROI accounts when they are still delicate seedlings) and tolerance for error (experiments that strand are not failures). This developmental phase of radical innovations is concluded by a selection process. An initial idea, judged favorably in terms of value creation, becomes an experiment. The experiment proves feasible, and customer feedback is positive. It now becomes a “venture”, where yield, sustainability and developmental capacity need to be verified (piloted in a genuine operation, e.g. a new business procedure or business model). Positioning the project in a development process such as this provides orientation when it comes to making decisions in its regard.
- 7. Differentiate and divide:** Concentration on small market shares or niches – everybody is an “entrepreneur”. Cell divisions make room for new business models. “Communities of Practice” ensure that knowledge and experience are shared.
- 8. Organize excursions into foreign worlds:** These can be (e.g.) learning journeys that explore innovative topics in other enterprises (innovations need the cycle of “experience-observe-evaluate”/“develop-test-evaluate”/“allow to mature-decide”) or empathetic observation of customers (video and interdisciplinary evaluation teams; observation of customers in their use of products) in order to identify latent, unconscious customer needs. An “innovative alliance” can be formed with leading customers or partners (i.e. those who challenge the enterprise because they are innovative and demanding themselves) – in order to develop future scenarios in workshops, exchange employees (e.g. “high potential”, lateral thinkers) and exploit their experiences for innovations. Sabbaticals and living in new, foreign worlds should be supported, starting with attending specialist conferences from other disciplines and gaining inspiration and implementing ideas (e.g. Japanese car designers living with an American middle-class family for several months in order to understand what automotive needs are central for the U.S. middle-class market). Different spaces for innovative work other than those of day-to-day business also work as a symbol, helping to accelerate the transition from one working mode to another within teams.

**9. Develop and examine innovative strategies by means of indexes:** *What percentage of our products is younger than three years? How much turnover do we generate? How many of the clients we advise are leading innovators in their industrial sector?* These are examples of questions that accelerate innovative endeavors in the focus of management.

**10. Strengthen independence and autonomy in individuals and teams** in an atmosphere of openness, challenge and intense communication: e.g. innovation trade fairs with leading customers and selected partners, competitions with productive debates that utilize conflicts as a motor. Innovations address the “whole person”; pursuing ideas requires being able to try things out, having time for experiments – constant operative pressure hinders the emergence of the new. At the start, ideas need protection from the managers of day-to-day business and from customers. Like seedlings, they require an incubation period: they do not grow faster if they are tugged on. Performance pressure is productive for innovations, whereas operative time pressure is not. Innovations need to mature; they require discipline, commitment, challenge and a great deal of freedom. They flourish in a culture of self-assurance and performance, in which there is latitude for alternating between tension (intense work) and relaxation (letting go – doing something completely different). For many companies, this is something new and unusual. Unlike the tasks of day-to-day operations, innovations cannot be accomplished like agenda items. For them to succeed, organizations need to have considerable openness and be able to accept what is new and different. This is what developing an innovation-friendly atmosphere is all about.

## **8. Hard cuts and new growth as simultaneous and parallel objectives**

We have established how “hard cuts” and “new growth” can fail. What consequences can we draw from this for the planning of change? Does it make sense to carry these two types of change out in succession? First restructure and downsize, then work on new growth, innovation and cultural change? This approach has a significant disadvantage: the whole process takes a long time (e.g. nearly 20 years for GE). Still, the fact that it does eventually lead to a positive future makes this succession more promising than the reverse order. Initiating