Stanford eCorner

Reach Your Escape Velocity [Entire Talk]

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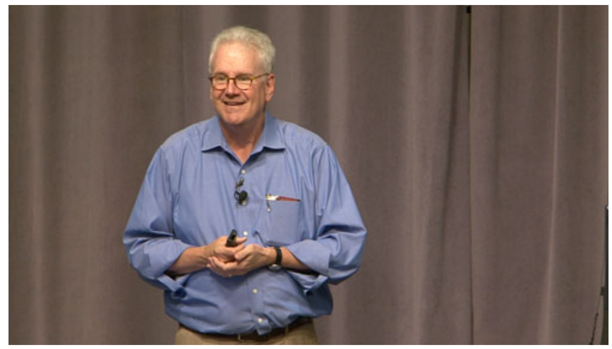
In this high-energy lecture, Geoffrey Moore discusses how companies can build the escape velocity necessary to move beyond the successes and failures of the past. Moore argues that when companies focus too much on performance, they miss out on building the power to become the industry leaders that other companies envy. He shares a hierarchy model through which companies can examine and build power, and examines how product teams can best work to differentiate their company, neutralize the competition, and optimize products and offers.



Transcript

Let's welcome Geoff Moore back to Campus. Thank you. Thank you, Tom. Thank you. OK. Now, usually I try to preview this stuff before it's published so that you guys can help me make sure it's not as dumb as it would be but this time I actually must have missed the calendar. So this is actually now a book that is going to come out in September and Tom said the sixth book. The first three books were written in the '90s and they were all about that -- sometimes they call it the time of the great happiness. There was this unbelievable rush of technological enthusiasm and it seemed like no matter what you did, it was just magically successful. And in the last -- they've been written in the last decade where frankly, there's been a sort of maturation in the tech sector and the larger companies have become more of a part of my world than they were in the first decade.

So this is a book which is written -- if you notice what the subtitle is, "Free Your Company's Future From The Pull Of The Past", and this is a book written to major -- companies that have had established franchises, they're very successful, they can afford to send their employees to places like Stanford for executive ed, but they're kind of stuck. Whatever it is that they're success activity it's kind of created enough inertia momentum that it's hard for anything else to get on board. and so this book is about how would you address that. Now, it's a whole -- it's a book and this is a short talk, so what I've decided to do in this talk is do two things. The first half of the talk, I would like you to think of yourself as either you're on the board of directors or you're the CEO of Microsoft, you're John Chambers, you're Steve Ballmer, you're Leo Apotheker, you're Carol Bartz, you're the head of a big company, and I kind of want you to look at it from kind of the top-down. And then half-way through, I'm going to switch to a chapter which is more oriented toward, I'm in the middle of a big company, what can I do to change things from the position I'm in as opposed to the very top? So let me kind of kick this up with an overview. This notion of the problem of we're stuck and it just -- I have to say it's virtually universal. People kind of get, look, we have a successful franchise but you can't stand still intact between technology and globalization. Things are really, really moving. Now, that's great news for opportunity but it's also for people that stand still, it's a threat.

As our friends at Boarders, for example, discovered this year and numerous other companies. So everybody gets that they've got to engage growth. It's not like, hey, I've got an idea for you. They got it. What they don't like talking about which they universally acknowledge is there is massive internal resistance to moving resources away from established activities into new activities; massive. And so that's kind of like the innovative dilemma idea. You know, the corporate antibodies that kind of stuff. So we've talked about it for a long time, we haven't been very good about doing much about it. So year-in, year-out, the experience is, man, it's Windows again, it's Office again, it's routers and switches again, it's, you know, direct adver -- display advertising for Yahoo again, and it's like -- and even if something is young and as vibrant as Google, why did they -- why did Larry Page come back in? I think Google is beginning to feel like we need to -- when we're 10 years older, barely 10 years older, we need to escape from the pull of our past. So the problem is the new stuff, it's not that there's not new stuff, there's tons of new stuff but it doesn't ever reach materiality.

Meaning, in never reaches like being 10 or 20% of the total company's revenue. It gets announced, it gets started and then somewhere along the line it dies from the vine. And so that's where we came with this notion. These are questions that basically our clients ask us. That's where the title came from. How can we achieve a escape velocity? How do we free ourselves from the pull of the past? So just to make clear, this is not a trivial problem nor is it trivial companies that have struggled with this problem. These are some of the very, very best companies that tech has ever put on the playing field. So the notion that you are smarter than this problem, that a Stanford student would not have this problem, even though -- because you are very smart, it's not true. You will have this problem. So the question then becomes, what the heck is going on? And that's about the nicest language I will use tonight.

So what's the mistake we keep making over and over again? So it turns out the way that the global management system works, and largely this is a management system that was developed in the United States, but it's become completely global. It's a performance-oriented management system. That's how people get compensated in large corporations. So performances -- and by the way, not a bad idea, right? I mean, performance is critical to success, right? And we're good at managing it, but here is the second sense, power fuels performance and performance consumes power. That is not visible in a large corporation. It's a little bit like this -- you know, when we have this carbon cap when it taxed carbon emissions? Because right now, if you pollute the air, it's free. And as long as it's free people will continue with the behavior. Well, consuming power in most compensation systems, in most corporations is free. And further more, creating power, say around a new strategy, is not compensated. So I get compensated for consuming power for my performance.

I do not get compensated nor do am I held accountable except in the most kind of qualitative ways for generating power. So why would you be surprised that large organizations systematically consume their power? Now, the interesting thing is, in a mature industry you can do that for a long, long time. General Motors consumed its own power for 40 years. Eventually, it ran out of power. Eventually, the battery will go dead. But it takes a long, long time. And the performance metrics don't track against that. So we need to replenish power if we're going to go for the long-term. People get that conceptually, behaviorally, it's hard to integrate it into the corporate systems. And part of the problem is we don't have a very good vocabulary for talking about power, right? People recognize it when they see it.

This is the Supreme Court justice about pornography, right? I can't define it but I know when I see it. Well, the same thing with power. But the problem is if you can't define it, if you can't articulate it, how the heck are you going to hold anybody accountable to it? How are you going to make sure -- and by the way, when you lack power, it will show up in your stock price. Not in the earnings because performance creates earnings in the P of the PE ratio; the Price to Earnings ratio. It's the P that -- P is for power, right? And so if you have a lot of power, you will have a high PE ratio, you'll have a high multiple on your stock. When you consume power and don't replenish it, you'll see it going to one and even below one as you get into trouble. And so what happens in a world in which we don't consciously manage power, is we continue to put anxiety and pressure to perform, perform, perform, but every quarter it's a little harder to do than the last quarter. And then if you eke out that quarter you get to try again and the numbers keep going up and your power keeps going down, and so you become kind of neurotic. I mean, and there's kind of a sort of a collective neurosis around the end of the quarter and it becomes this incredible event which you must not sacrifice anything to. And when you're that desperate, you've already missed the quarter.

You just question which quarter are you going to miss because you're so far behind the power curve, you've lost touch with the engine of your own company. The people kind of get this but they can't translate it into behavior. So this is what we call the performance trap. And many cultures are very proud about being a performance culture. So it's a little bit provocative when we sort of put this out there but we're pretty confident in the case we're making. OK, so what would you do? And the answer is you need to manage power explicitly or directly. We have to find the mechanism to do that. What you discover is the performance activity begins when you start next year's annual budgeting process by handing out last year's budget and saying, you see the fourth quarter numbers, multiply them by four and start there. And that immediately starts a zero sum game about resource allocation which is why it's so hard to move resources inside the company because the person is looking at, I have a bigger number to make next year than I have last year, they froze my resources, at least in theory, the last thing I can contemplate is using my resources for something else. And so immediately -- so if you're going to get ahead of that problem as a management team, now you're the CEO and you're running your annual calendar, the quarter before you would start your budgeting strategy process, you start the power process.

And by the way, in that -- if you don't have a specific resource allocation pressure or sword of Damocles hanging over your head, there's lots of stuff to do here. People have lots of ideas about the next category, the next things you want to get into, how we could be successful, there's lots of opportunities. The key idea is allocate resources to those initiatives before you allocate anything else. In the last book, we called this fund core before context. But that's not what happens at large corporations. Once the budget goes out you're funding context before core. So do it before, drive accountability for power into the operational plan. There are metrics of power. Sales velocity you know, share capture and target segments. There's a bunch of stuff that even market share itself, there's a bunch of stuff that demonstrates that you have accumulated more power but you have to create those metrics and put them in the comp plan.

Today they're not in the comp plan. The comp plan is based on revenue and earnings generation in the current quarter and in the current fiscal year. It is a consumption-oriented comp plan, it is not a replenishment oriented comp plan. The fact that you got stock options is intended to incent you to want to replenish but is too indirect. It's just too indirect a metric to make it work. But you can do it. You can add power metrics to performance, you can earmark resources for power program usage only, and you can modify the comp program to hold people accountable to do it in ways that people will sign up for it. But to do it and kind of where this book comes in, is you kind of need a better vocabulary to talk about power. And so what the -- we created a model called the hierarchy of powers. It's kind of a framework of frameworks.

And the intention of this hierarchy is to let people sort out the power equation in a set of levels that make sense. So the hierarchy of power is just five powers but you talk about each power separately from the other four and you talk about them in sequence from top to bottom. The reason why that sequence exists from top to bottom is actually a lesson we learned from the investment community. When investors allocate assets the first thing they do is they allocate it by category. Actually, you mean by category, they'll say bonds versus equities versus cash in hand or whatever. But within equity itself say you want to be in retail, do you want to be in natural resources, do you want to be in tech, do you want to be in whatever. And so category power has to do with how fast are the categories that you are in growing? Because if you're in a category that's growing 100%, even if you're kind of a doofus, you're probably going to do pretty well this year. And investors aren't stupid. By the way, vice versa, if you're in a category that's growing at 4%, you have enormous pressure on you to make sure you make every penny of your earnings. And it's very, very hard for you to do much better than that because the category is giving you no lift whatsoever.

You can take share in a category that's not growing but not forever. Eventually, you run into a wall. So investors at the margin would prefer your company to be in high-growth categories, not low growth. So a company like General Electric would routinely sell off low-growth businesses in order to get capital to buy high-growth businesses and they would kind of migrate the footprint of the corporation going forward. That's in order to have more category or power. You can hold your company accountable to what category is you're in. The board of directors can hold the management team accountable to that. The next one is company power. So in the categories you're in, how powerful? Do you control your own destiny or somebody else is calling the tune and you're just trying to keep step and keep pace with them? This is market share. This is Jack Welch saying, you want to be number one or number two or you don't want to play because you wouldn't have enough company power to get the return on being in that category.

You ought to get out of that category and get into some categories where you can be number one or number two. So it's about power. The third one is market power that has to do with, are you in the markets that are the fastest growing segments or the more strategic segments? Now, category and market sometimes get confused but category is defined by a group of competitors and markets are defined by a group of customers. And as long as you kind of keep that sort of simple quote in your head, you will not confuse the two of them. So a market is about getting a group of customers and the idea here is a little bit like winning primaries for a presidential nomination. You want to win in New Hampshire primary. There are not very many delegates in New Hampshire but is a very strategic primary to win. And in markets, there are always segments that are early bellwether segments that are different for different markets, different technology, different categories, well, there's always some. And so winning those early or maybe there's a segment that's in transition where the segment like this particular part of the economy is completely being disrupted by the Internet this year so whatever they're going to buy, they're going to buy this year. So get in there and be successful if it's the kind of stuff that you sell.

That's what market power is about; winning segment shares in the critical segments. Offer power is based on how compelling is your offer compared to the rest. We're talking about differentiation. How different is it, but then also how comparable is it to the -- are you living up to the norms of your category? That's sort of table stakes and then how different is it. I'm going to come back to offer power so I won't say more about it right now. And then execution power is, when you guys set yourself out to do something, when you're going to enter a new category, when you're going to do one of these transformational initiatives, can you actually get it done or do you find yourself kind of redoing it? So if you look at this thing, we often sit down with our clients and we'll say, let's just ask you a couple of questions kind of among us kids and the door is closed and there's no recording devices going. So the questions go like, are we in the high-growth categories or do we have category envy? HP right now must have Tablet envy, right? It has to, right? Everybody looks at Apple going, like that, OK. Category envy. OK. Company power.

Do customers and competitors see us as the team to beat or is that somebody else? Let's just be honest with each other, where are we and think about your company or the company you may have been in before you came here or the company you're in now, the company you intend to go to. Market power. Are we winning the key primaries definitively or -- and are we winning them fast enough? I'll tell you, "Yeah, we're going in the right market," but it's like one year, two years, three years, nothing is happening. It's dying. That's not what we meant. Winning meant, you know, moving on. So do your flagship offers, you know, set the bar or are you always playing catch up and not doing it fast enough, and we'll come back to that again as I said with offer power. Can you make stuff happen and make it stick or are you continually pushing the reset button? There is nothing more discouraging than being in a large corporation which does a massive reorg once or twice a decade because the last team couldn't get it done. And it feels like you're watching this very large sort of drain, this water is just going like this. This could take you a long time but it only appears to be one way that this thing is going to go.

And so it's important when you sit here and to say, the questions you want to ask are where are we strong and where do we need help. And no matter how good or how bad you are, you probably have places that you're better than others, and so what are we going to build on and where do we need to go forward? But I hope you can see that each one of those topics is different from the other four because what happened before when people would say, we're going to have a discussion about strategy, and strategy is normally about power, about achieving a position of power. What are we going to do to achieve a position of power? That's kind of what strategy means. But the problem with the dialogue around strategy was it would go up and down through these five levels of category, mixing and matching, making arguments that never ever connected. So it was always like this. And so at the end of the day, we'll, you believe what you believe and I believe what I believe and now let's argue about who get the head count. And so that's why you would default back to a performance model because in the performance model, it's like, we'll, who wins? Well, who ever got the most revenue or the most margin -- the most earnings. So it was a way of essentially saying since I can't talk about this articulately at the level of power, I will only measure it at the level of performance. And that leads to that slow draining of the corporate battery. And by the way, there was a time when these companies all had enormous power.

That's why we've heard of them. That's how they got up to the top of the mountain in the first place. Now, they're kind of going down the mountain, they're not renewing their power but that was a very tall mountain they got to the top of at one point in their lives. And so they have -- Novell at one point was the power company in networking by far. And then it just, you know, year after year after year it's still around but it's kind of toward the bottom of that mountain. OK, so that's the stuff we're talking about just to kind of make it dirt obvious. OK, so let's apply this to Apple because right now they're the golden child. So what categories are they're in? Well, music mobility and media, all of them are still growing at hyper-growth rates. That's pretty cool. By the way, even the Mac they brought back in the hyper-growth.

Company power, so team to beat in all three. I guess or anybody else so you would say would be Apple is trying to catch up too in those things. I don't think so. I don't think so. Market power, we don't need no stinking markets, we got the world. I mean, right now the truth is they are so powerful and now, do they do certain kinds of things? Sure. Are they looking at the business market in some ways? Yes, they have programs but basically not. Like, man, the people are beating the path -- they're waiting outside of our stores at midnight to get an iPhone that is white. OK, enough said, enough said, OK. So the offer powers are like huge -- and by the way, it's not just the products, it's the -- it is iPod plus iTunes.

It is iPhone and iPad plus apps store. I mean, it's a huge -- this is a dominantly powerful situation and they did all of these in less than a decade. So you kind of -- every other leader in tech saying, so what are you guys doing? So what are you up to, huh? No, no, not much, huh. OK, I just want to check. So that's why it is currently -- I think -- this was true earlier this year, I think it's still true. You know what's the most highly valued company in tech. It's about $320 billion. Microsoft is about 220 but there was a time not very long but maybe still, it was the second most valuable company in the world; Exxon and then Apple. So this issue of power -- and if you look at the guy you say, well, what's Steve about? One of the things Steve is about is he cares about power and he assumed performance will take care of itself. Jeff Bezos is the same way to Amazon, that's why periodically, he does stuff that just drive the shareholders crazy because he gives away performance in the short-term because he says, I want the power.

He's always done that. So if you can do it, and there are examples, but the problem is they tend to be examples of companies that are run largely through a charismatic founder who is just -- has a power instinct. Bill Gates being a third to this amazing example. OK, so just to kind of close on this thing in terms of how this category -- hierarchy of power affects the corporate dialogue, there are three things that a CEO is asked to articulate in relation to this power hierarchy. The first is a vision. And the vision is about what is happening in the world in the zone of your category that the other people outside of your company care about and want to interact with. What role is your company going to play in the unfolding of those forces? And which markets are going to be the bellwether markets that are going to indicate how well you're doing? And that's a vision. That's what you talk about a vision for your company, that's what vision does. When you go down to strategy, you kind of go down one level and you say, OK, we're in this category because categories -- strategies change by category. In this strategy, what position -- what's our power position relative to our competitors today, in what markets are we going to fight in order to change that position and what offers are the critical offers that are going to change our power position relative to our competitive set? That's what strategy is about.

And then when you do down one more and it's execution, it's, OK, guys. Now, in terms of which markets -- which offers and how fast and this is back to weekly commits, monthly reviews, quarterly deliverables, we're just going to get it done. And so all three kind of these issues; vision, strategy and execution have a vocabulary of power around them that is useful -- and every one of these things have a bunch of frameworks behind it. So what the book will share is a bunch of models about the -- well, category power, the category, the optionalized cycle, the technology, the optionalized cycle, how do things grow, I mean, I've been writing about that for a long time but every one of these has its own set of models that you can bring out and say, OK, we'll, let's look at our company through this lens and kind of see how we stack up. So the intent is to create vocabulary with this book. It's not to say, we know your business better than you know it but it's just to say, look, look at your business through these lenses; clear, blacker, sharper, which one? Right, that kind of stuff. So these are some companies that we've been working with for the last 20 years. What they have in common is that every one of these companies we work with on an initiative for at least over a year that was sponsored directly by the CEO. So the CEO was in the middle of this initiative and we built these frameworks in conjunction with the teams led by the CEOs. And they did very well.

I mean, this is sort of a little bit of a self -- pat ourselves in the back kind of things, but they did. These things actually work. So I don't want to imply that this stuff is just a theoretical stuff because those are real companies that had a lot of success with this stuff. OK, so the close for this thing at the top level, if you were the board of the directors and you're saying, OK, OK, Geoff, we got this disease, OK, great, great, great. What do you do? How do we start? You can start at any point in this hierarchy. You can start with the category power level which tends to be we need to look at portfolio. We tend to have way too much money in aging categories with the Boston Consulting Group calls, cash cows and we don't have enough rising stars. So that could be the problem. Or we can say, no, it's a company power problem and the problem is we can never -- first of all, we can kill nothing and second of all, we can never really make any big bets. Every big bet we hedge and after a while we're like the person at the roulette table who put the chip on every single square.

So we win every time. Except, we just lose money. So on the market focus, we can actually go after markets in a directive way. It turns out it's extremely hard for large corporations to go after niche markets. But it's critical. It's critical because otherwise, you'll end up coming in second or third in every primary in the entire election and you don't get nominated, right? You must win definitively in places particularly in the right year, in the right place. And then offer power which I will come back to that one, that's a little more we can create highly differentiated offers. I'm going to say something a lot more about that in a minute. And then organization. So how do we actually drive transformation initiatives through the antibodies or whatever to actually get them done.

There are ways to organize inside a large company to create -- carve out an entrepreneurial space not just to incubate innovation because all of them do that but to actually go from an incubated innovation to a material business. That's when they all get killed and so there's a whole thing around execution power and organization for dealing with that. And what I'm going to talk about in the second half of this talk is offer power and how it affects innovation. But before I do, since I've been blasting pretty hard for the last 25 minutes, questions or push back or like if you're crap detector went off, it'll be good to sort of -- I mean, that was a pretty fast explosion but just anything about that model that either calls you to ask -- yes, yeah. Sir, there are like certain empirical metrics for figuring out which sectors of your company are not sort of high-growth...? So the question is are there empirical metrics for which sections of your company are high-growth -- not high-growth efforts? Yes. The first one is simply to look at the average growth rate of everybody in that sector. And basically, it's pretty straight forward. You look at what -- what does it take to motivate growth investor? It's typically 15 to 20% growth or higher. Maybe 15 to 30 might be a better range. And so if it's 15 to 30 or higher, it's definitely -- that's a growth.

If it's single digit, it's almost always low growth and 10 to 15 is sort of a little bit of the muddy area. But what most companies often do is they'll have a portfolio where they'll have fourth businesses that grow 4% and one business that grows at 8%. And they'll call the 8% business a high growth business. It's like, no it's not, it's a taller midget. So don't -- come on, there's no basketball player in the room. So that's how you do it. Yes? How about empirical evidence showing that people that apply these principles are more successful than ones that don't. Because Apple is -- you could apply 1,000 frameworks, a...? If you have an App Store you too will be great. What's the statistical significance is this principle ahead and if so out of the five types of points of entry which is the most powerful type compared to other things? So what are the things... definitely needs to do about it? OK, so you're talking to an English major not a Quad so this is anecdotal, more qualitative more than quantitative.

It's kind of why I put up those 20 companies that I had on that other slide because at least those are 20 stories, not one story, but still it's still qualitative. In terms of which is more powerful, in general, category tramps company, company tramps market, market tramps offer, offer tramps execution. Largely, that's the way it goes. This one is offer power, however, it can -- it's probably the lever that you can use if you're behind to move up as you're going to see in the next section. But you can generally use -- if you say, look, there's such -- you remember that first slide with all the companies? That's kind of the negative proof. That's the proof that there's a common deterioration in the technology sector that appears to take two decades. And the number of companies that were successful two decades ago, I mean, aren't around anymore. So it should take at least 2 1/2 -- in 1985 the leading enterprise software company was called Cullinet. Cullinane, Cullinet, no, John Cullinane, Cullinet. Who knew, right? And number one, right? Novell was number one in local area networking.

I mean, these are not chump change folks. Kodak was number one in imaging in the whole world. Not so much. So that's the best I can do. I mean, and I would love for people who are more quantitative to say, why, I'd like to apply a little more research discipline to this because Geoffrey is Irish and the Irish are kind of famous for waving their arms and he participates deeply in that genome. Other -- yes? You mentioned Jeff Bezos as an example of someone who's power driven, right? That company is also so much spread thin, they are in Web services, they're selling books, they're in the social media business and so on and so forth. How can you reconcile focus with spreading around...? Well, I think the problem with putting yourself too thin is you have the opportunity to gain power but you're dissipating because you don't focus enough. You don't actually accumulate it, you actually end up dissipating it because you trash. You go from thing to thing to thing to thing to thing. And I mean, right now I will argue this, Cisco is struggling without that right now.

They have a management system, they have a -- John laid out an incredibly ambitious agenda for the decade. I think there was nothing that agenda that was stupid. I think the company has felt, man, there was just too much on our plate. And so lots of growth categories. The one thing you would not criticize Cisco for is you're in low-growth category. That is not their challenge. Their challenge is can we get our arms around the categories that are most important? So you're watching them right now sort of try to pull back and achieve more focus. So I think at some point you do go too far. And you can't -- it's a -- by the way, that's a performance culture too. I mean, they have a very strong -- and it is not that you have power or performance, it's -- this is the and and not the or.

This is performance and power. One more then I'm going to kind of go forward -- yeah, OK, right in the middle. Yeah. So in the beginning you have performance culture and said it was a good thing, right, but it went too far. Is there kind of the same thing for power if you go too far of the power spectrum? Is there a danger that -- I think there could be. Yeah, yeah, I think you can get to the point where you are -- you actually lose your operating income to kind of keep yourself going. And so because in the short-term, you often -- you can make sacrifices in performance in order to invest in power. And if you over-invest in power and all of a sudden people stop believing in that, you can't get funding.. You can't get your next round of funding. In general, by the way, venture investing is about power and public exchange investing is about performance if you think about it.

Because in a venture-backed company, there's not enough revenue to really say the performance is the game changer. It's power is the game changer in venture. And that's why I think this was an easier both for me to write maybe than somebody else because every Monday, every dialogue we have is essentially about power. And it's usually category power first and then actually offer power becomes a very, very important to a venture company. OK, I'm going to move on to this notion of now I want you to take off your CEO hat, I hope you kind of enjoyed that moment of leadership and the board of directors and whatever, and liability, I might add. Some of you might look good in an orange jumpsuit, you'll never know. But now I want you to go back and say, you know what, I left this auditorium and next Monday I took on an assignment and by and large, a high tech company and I'm a product manger or product line manager. I am now -- what is amazing about tech by the way, is that product managers -- the unit of wealth creation in tech all of my life has been the product. Now increasing the service as a sort of invisible product. The product and product management is largely conducted by people in the first 10 years of employment.

So all of a sudden, relatively early in a career, unlike most professions, most other industries, you actually have your hand on the tiller that changes that fate of your company. So it's an amazing privilege to work in a high tech company because the amount of power you get short -- particularly if you can get into this role of product marketing and product management. So that's the role you have now. That's the role I'm going to give you for the rest of this conversation. And your job now is you have a really cool product but you're living in a company that makes its living through a very old and boring set of products. But they make money. So this is your challenge, OK? So to understand the lever you have, you have some resources and the question is where are you going to spend them and what are you going to get for them. So think about having an innovation budget. Not much but some. Well, you could spend it on differentiation and that means I'm going to spend it on some kind of innovation R&Dand I'm going to create something unlike anybody -- anything that anybody else has and that's going to cost the customer to go, wow, I want this offer.

I don't want those other offers. We'll talk about that a bit more in a second. The second way you could spend your budget is hold on, everybody else in our category now has this new feature and we don't. And people by the way, are noticing it. So if we don't do some back filling of this feature set, we're going to -- and no matter how different we are over here, they're going to go, yeah, yes, it's an amazing car, they have no wheels on it though. You know what I mean? You kind of need wheels, don't you? So that will be that part. Now you've got you're budget is getting pulled in two different directions and you've got a third idea which is, you know, if I could figure out a way to do some productivity things, maybe I can get some more money to spend on red and blue. And so basically, those are the three things you can -- the three levers -- the kinds of initiatives that you can go. I'm going to -- charter differentiation thread, neutralization thread or a productivity thread. And I'm going to kind of walk you through -- there's a lesson at that end of this which is an amazingly -- it seems like it's such an obvious lesson.

It is almost universally not followed -- the principle you're going to follow. Which just to give you a head's up on it is these three things are not mutually compatible with each other. And whenever you charter a single team in a single project stream to do two or more, you're screwing up. And I would say that 99% of all the project streams I see are combinations of those three things which is a fairly high ratio for screwing up. But let me kind of walk you through, that's the place where this is going to end. So differentiate, why do you do that? To separate from your competitive set. Pretty obvious and pretty exciting and by the way, every engineer in the world wakes up thinking that's what I do for a living. I'm the smartest person on the planet and I will be able to demonstrate it. Neutralize, catch up with the competition, nobody likes to do this. Nobody likes to do this.

But they get -- but it's part of being an adult. So you say, OK, I'm an adult, I guess I have to make my bed, I have to do a few things, OK. And then optimize, again, even worse for engineers, like what? But the point is there's a big return on this if I can increase -- for you as the product manager, product line manager, if you can get this done because there is a bunch of places where you have resources reporting to you doing stupid stuff. Too much stupid stuff and if you could actually get that initiative going, you could free up more budget to do the top two. So in each one of these areas people make mistakes. And I mean, I'm not this -- everybody makes mistakes. I mean, they make perceptual, conceptual mistakes. They think about it wrong. And so the intent of the next few slides is to say here is the most typical way you think about this thing wrong and I want you to think about it differently. So differentiation.

First of all, well, it's different but the thing is if you've ever actually noticed the world, everything is different. There's no two things that are the same, right? So different isn't a big deal, OK? This differentiation along a vector value, OK, so how much differentiation do we have and can we go beyond the limits of the competitive set? What that means is, you'll see in the next slide. I want to be the iPhone. I don't want to be the Samsung or the LG or the Rim or the whatever the other guys are. I want to be the one that's really different. Then however, you've got to realize you've got to subtract out the unneutralized competitive threats. I'm an iPhone, I'm on a ATT network and there's no coverage. Oops, that's not so good. You have to have coverage it's a rule. So well maybe it isn't, maybe it's not an iTouch but the point is that you have things where you fall behind and you go, that's not -- it's a Macintosh but it's slower than dirt.

That kind of problems. So you can't just say I'm different, you have to say I'm also meeting the norms of the category in the stuff that I'm not trying to differentiate on and then as I said, if I can add back in optimization, I can spend it more in one of the two above. So the net differentiation is what -- as an offer manager, product manger, service manger, that's what I want you to think about. Every year my power increased because my net differentiation increased relative to my competitive set in my category. So this idea by differentiation is most of the time most offers live inside the yellow circle here which means that they have to compete against each other, mano-a-mano for winning a customer's business. Shell gasoline, Chevron gasoline, Union 76 gasoline, you don't go like, whoa, that was amazing gasoline, right? That's not what happens, OK. But periodically, people do get separation from the competitive set. And your job as an offer manager is to imagine that blue arrow and that blue asterisk and to say what could we do with my offer to take it that far. Now, you may not get permission but the company may say back to you, you know what, I'm sorry, it's your first product you every got, we're not spending any money on your product. Rats.

But sooner or later as a product manager you will get an offer that says, you know what, if you could do that I would like to see your plan for doing that. So do that and if you don't do it, now you're just back in to doing mano-a-mano So if you look at some case examples, the people on the left all got competitive separation and the people on the right did not. So IBM PS/2, it was not quite compatible with everything else. It never kind of made it. The Kindle versus Sony's PRS 500, OK, good. Got a glass screen, OK. iPhone versus Palm Treo and this is really tough if you're Palm because it was very different but it just didn't get the separation. It just didn't happen. Cisco TelePresence versus HP Halo, almost identical but not quite. Not quite.

So in innovating to differentiate, separate yourself from the pack so stay in the gap. This is an investment moment, you get to champion the idea somebody above you is actually will give you the go ahead or not but you need to champion, you need to create a vector that somebody could believe, wow, you really are going to get separation. And typically, what you have -- the reason why they believe it is there's something that the company owns that's unique to that company that can create what Andy Grove called the 10x effect. So Andy Grove will say 10x will get you apart from the crowd. So sales force was using SAP against Siebel against SAP, Oracle whatever, and they put themselves up. SkyPad, peer to peer technology, Wikipedia had its open source model and look how massively these things have changed the planet. VMWare with its virtualization technology, Akamai with its overlay routing network, all of these companies are like do not have any -- do not have -- they have unmatchable offers at this state in the game. Now, are people catching up? Yes. Are there CDN people attacking Akamai? You bet. Are there virtualization technologies attacking VMWare? Sure, of course there are.

But look where they set themselves apart and how long -- how much power those offers had to change the trajectory of a company. So -- because there were companies that didn't have company power. They were all kind of start-ups. Who'd heard of Skype? Who'd heard of Akamai? Who -- VMWare? And Wikipedia for God's sakes had no money, right? How could they take the Encyclopedia Britannica and Encarta and make them irrelevant? Through offer power. Offer power did it. Crown jewels. Now the neutralize thing is the one that I think people make the most mistakes with but with crown jewel -- the problem with the previous one is sometimes there aren't many crown jewels around. And sometimes you can't find a way to be unmatchable. You just have to suck it up. Neutralization is a different problem.

Neutralization means you know the world's progressing, competitors are innovating and now all of a sudden, it's my job to get back inside that yellow circle because I've kind of fallen out of favor. And I've got to at least -- I don't have to try to beat the blue asterisk. I just got to get my asterisk back inside, back in gears as it were. And so we're focused -- and once I get inside there then I can talk about my differentiation, again, but if I'm missing -- if I'm still out here the market won't talk to me at all. They'll say, you're not even qualified to be in the conversation because you haven't met the minimum table stakes to be in this game. So failure to neutralize, there's some real cautionary tales on this one. So Microsoft brilliantly neutralized the Mac with Windows but Nokia, did you see the memo from Steven Elop a couple -- this was last month or the month before? There's a sentence in that thing, the new CEO of Nokia, he writes a memo that's a public memo to the world which says how is it possible that Apple came out with an iPhone in 2007 and Nokia does not have response? Would you want to answer that question? Gee, Steven, I wasn't the product manager. But the point was -- so ask yourself why. Why do you think? I don't know but my bet is because the engineers at Nokia were too proud to neutralize because they wanted to differentiate. They wanted to over leap the over leaper.

And when you do that, you leave year after year after year of no effective response in the market which is absolutely fatal. Microsoft in the Web -- remember there was a memo when Bill Gates -- where software company were not a Web company and then it was like, oh, no. And then it was like he immediately neutralized Netscape Navigator. Now, Internet Explorer 1.0 was a farce. It was a pathetic attempt to pretend it was a browser. The second release, not much better. But the third release, better than Navigator 3.0. So Microsoft actually is a brilliant neutralizer. Lotus Notes did not make the same kind of response. Lotus Notes kind of went inside the IBM world and it's kind of doing its General Motors thing.

Netflix -- Netflix with the Web, didn't you think when all of a sudden this stuff comes over. I'm not saying Netflix, right? Netflix is a CD distributor. Not so. Mr. Hoffman is still the scourge of the media industry. He is Conan the Barbarian, they hate -- I mean, they were just like -- they would love to -- but I won't go into assassination, not this week. But they're thinking about it. But Blockbuster -- when Netflix came out, Blockbuster just stood there like a deer in the headlights and charged more for late stuff. Google apps versus Microsoft Office, Google is not trying to beat Microsoft Office, it's just trying to annoy them. It's just trying to keep them busy and to kind of keep something going.

Yahoo on the other hand, was more like Nokia. Yahoo wanted to overtake Google Search. It was kind of like Captain Ahab and the white whale and it was a quest. And it was a fatal quest. And so what Carol had to do is get in and sell off the business because she had to free her company's future from the pull of the past. That was a really, really important thing for her to do. Apple and Kindle, so what did Apple do with Kindle? It co-opted it. Kindle -- most people -- most read their Kindle books on iPads because they co-opted it. Whereas the borders and their thing, no -- and borders -- OK, next. So the game here is catch up fast and assimilate the innovation.

It's a game of speed. It's how fast can you do it. How fast can you become good enough. I'm going to skip over this slide, more separate. I better go to the third one. So the third one is productivity. Productivity is when the category gets more efficient and now you're too expensive. And you've got to get yourself back in gear here and we have a bunch of stuff -- this is actually a place where large companies have a ton of money tied up in the pull of the past that you can free up. There's the whole long tail problem they have. That's 10% of the revenue of this chart.

It probably consumes 30% of the resources. It's an amazing -- the long tail wags the dog in large companies. So if you just crop off the tail and with some discipline you could centralize and standardize that will change it. Then there's the middle part -- now this is real business but it's real business done in very sloppy ways. And by the way, the reason it's sloppy, big companies buy other big companies or they buy middle-sized companies and they merge them. How effective is a process do you think that starts in one company goes to the other company and goes back to the first company? Do you think there might be a little waste in there somewhere? It's crazy. I mean, the amount of craziness that happens inside the world's best companies. When you work inside these companies you should go, how is it possible that we're winning? Gosh, the other people must be like really bad because everywhere you look it's just like there's just massive waste and it drives you crazy except you can't seem to do anything about it. Again, that's the re-engineering button. Modularize, optimize, just pick the low-hanging fruit, go after it and then finally, just outsource it.

You can take and say, look, we're just not going to do this anymore. We are not going to manufacture -- by the way, that little iPad, iPhone whatever you got, it says designed in Cupertino. It doesn't say it's manufactured in Cupertino because it's not. It doesn't say supported in Cupertino because it's not. And so you start figuring out what are the things I don't have to do and those things I need to stick -- keep visibility but need to outsource it. That turns out to be, as you can imagine, that is an enormous amount of work to do. But there's lots and lots of resources available and inside your own organization as your product line managing, you don't have to do this for the world. You just have to do it for your team. Your team does stupid stuff all the time and they hate it. So it's not like there isn't low-hanging to go after.

So here is getting to the sort of the money slide in the path punch I've telegraphed. Three different tracks, each one value creating. If you said I don't do one of these columns, you've made a mistake, you must do all three. But notice that we're playing to three very different goal lines. With differentiation it really is unmatchable and it is how far can I separate. Because if I'm too close to the herd, the problem is they catch up -- like remember when AMD had the first Quad Core, it just kicked ass and Intel sales went down for two quarters. Oops, then they came back with their Quad Core now they're back inside the yellow circle. So it's really important if you're going to spend -- take the risk and spend the money to get outside, get way the hell outside. It's very dangerous to be just outside the yellow circle -- yellow circle is being like in an amoeba, it'll go like that. Then neutralize, OK.

You've got to get comparable not better than, just good enough but you've got to do it fast. Amazingly fast. That's the one everybody misses. People don't pay enough -- they don't pay enough time on the speed thing and they don't frame the project to be fast except the ones that are brilliant. This is what Microsoft does better than any company in the world by about an order of magnitude and maybe not so much anymore as they used to. But this is the thing, this is why Microsoft could routinely let anybody innovate anything and say I'm going to take it away from you. I'm going to take it away. I'm going to be good enough very quickly and then eventually I'm going to assimilate it either Windows or Office. One of the two. All life will be part of either Windows or Office.

So when you mix mode to create waste and one of the most obvious ones and this is -- you see where the key metric for productivity is you want to be best in class, and you do. On productivity metrics the goal is to be best in class and you benchmark yourself against other companies and that's exactly what you should do. But what happens if you try to be best in class as the goal for neutralized project? Well, you spend way too much. Best in class is a lot more than good enough. Good enough is all we need and worse, not only do you spend too much, you spend too much time. Every quarter that you do not neutralize that threat is a quarter it gets to build up more momentum against you. This is just dumber than dirt but it is the standard operating procedure in company after company after company. And then best in class is not good for differentiation because you've got to be on class. Best in class is the kind of the biggest midget in the yellow circle. So, yeah, yeah, I'm the best in class! Yeah, but I don't get the charge anymore money because -- so it's really important to separate with that thing.

OK, so this leads to a concept we call one playbook per project. Now, the way you fund things in the world probably you have one budget that has to be split among those three things. All I'm asking you to do is don't tie the differentiation train to the neutralization train or either of them to the optimization train. Have three trains manage them separately. You manage it one for speed, one for distance and one for fuel. That's the game you're playing. Now, just to close on this thing, in addition to the three good things that can happen when you spend money on innovation, two bad things can happen. One is you fail. And some amount of failure has got to be built the system but the one that drives you crazy is when you waste. And basically, wasting is just doing the opposite of all the things we've been advocating.

So how do you waste? You do a differentiation project but you don't really get outside the yellow circle or you get just outside, you wasted that entire budget. Because as soon as the yellow circle catches you up, all that power you're going to have, you don't have that power. So you spent you power budget but you didn't get power. Neutralization, you didn't do fast, you went too far, it went beyond good enough and you also took too much time. The competitor was like just dancing in the aisles thinking, wow, we got another free quarter from those bozos, amazing. I mean, you've got to -- no matter. I have to be careful. It's public. As you said, it's public Internet, OK. I didn't -- Not you, you're not a bozo, sir.

You're a client. Very different, OK. Or optimization -- optimization projects that don't really go after the sacred cows. So you optimize everything except sales and engineering. So you just beat the -- out of the people that are in the cafeteria but if it's an engineer or sales person, oh, wow, I can't touch those two. Well, 85% of your head count it's 100% of the things that are making the difference, so it's like crazy enough to optimize important things. Now, this is my favorite slide to show the clients what they kind of have done the mea culpa and doing the flagellation and the, oh, God, we're terrible. You said, OK, here is the thing that you've got to realize and you as the product line manager have to realize. That wasted money, it's in your budget. That's your money.

It's all -- you don't have to go ask people for more money. You own that money, right? If you stop wasting it nobody is going to come to you and complain. You're not going to get a letter saying he stopped wasting that money. What's the matter with you? And if you spend it on better things there is an upside so what the heck are you waiting for? And that's kind of a call to action as an offer manager which is there is no excuse for you not to act now because you don't have to go get more money. You have the money already, you're just wasting it. So, yes, you have to go through extraction thing and, yes, you've got to make sure it's repurposed. And by the way, if you just extract the money, you just optimize and don't innovate, I mean, you don't differentiate or neutralize, you won't get to keep the money. The CFO will take that money and say thank you very much. Give me some more next quarter. So you've got to take that money and immediately put it into neutralize or differentiate.

So this is the kind of stuff where we've got frameworks around you know, the neutralization, the differentiation, productivity frameworks, the waste framework and the net differentiation idea. That's a chapter in the book, it's a chapter written for people who have offer power in their purview, they're product line manager kind of person. And it's intended to create a vocabulary and a set of models to have a better conversation and think about your management opportunities from a power point of view not just the performance point of view. And so that's one chapter in this thing and as I said, there's these five core chapters in the middle of this thing and with that, I think I'll once again sort of throw it back open to questions, so. Just a little... No, we're over time. We're a little overtime. So can you stick around and just -- I will stick -- OK, so thank you very much, OK, good.