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When companies get big, they stop innovating. In this episode, Eric Ries, author of *The Lean Startup*, talks with Stanford Professor Bob Sutton about ways to fight back against the sluggishness of scale. If you really want employees to come up with new ideas, Ries says, workplace posters and glib slogans won't cut it. You've got to measure innovation and reward it, failures and all.



Transcript

- And I was sitting there being like the entrepreneurs that I admire and our tribe.. What would our mug say? If we had our own mug, what would it be? It would be, "I eat failure for breakfast." - Right.. - If I only fail four times by the time I get to lunch, that's actually a pretty good day on average.. - Friction is a huge psychological burden.. - Without friction we would not have fire, and we would not have sparks.. - I gotta get a knife, I gotta hide it.. - I end up spending a lot of time ruminating.. (radio distortion) (hip hop music) - Hi, I'm Bob Sutton.. I'm an organizational psychologist and Stanford professor, and this is The Friction Podcast.. (mellow hip hop music) On today's episode we have Eric Ries..

Eric is the author of *The Lean Startup* and *The Startup Way*.. Eric has helped start a movement in government and corporations to bring the entrepreneurial mindset into large organizations.. Eric is on a mission to add rigor to the way we think about innovation and product development.. He wants to get companies to stop wasting people's time and money, to stop frustrating them, and to add as much humanity as possible into their daily lives.. Let's start with just the word, friction.. When you hear the word organizational friction, how might you define it? What are some of the emotions that come to mind? - Well, it's funny when you say organization friction.. I actually think in most organizations there's more friction than there is organization.. (laughing) It's almost all there is, because the overhead of getting anything done is unbelievable.. I was talking to a product manager, and I said to him, "What percentage of your time "do you estimate, do you spend defending "your existing budget that you already "have for your organization?" He said, "At least 50%." And that's actually the most common answer I get from people.. - And these are probably in profitable, highly healthy organizations..

- In highly profitable, well-run, well-managed organizations.. So organizational friction to me is like the natural, automatic consequences of the way we structure these organizations when they get to scale.. And we just assume that that's how it is.. It can't be improved on.. Which is so wrong.. - My take, and I'm sitting to be corrected, is that you're making an argument for bringing in an entrepreneurship mindset into large organizations.. Is that accurate? - Sure.. So when you say that we're going to bring an entrepreneurial mindset into any organization, people immediately think you're full of crap.. It's like, it sounds so B.S.. You're like oh, great, what are we going to do, are we going to put up posters and say, everybody think more creative? Be an entrepreneur or whatever, like, there's so much cliché and business nonsense and fads that come around these ideas every few years, as you well know..

But I think what we have to be like more rigorous about our terms and about what it means, because the details of this really matter.. So when we talk about entrepreneurship as a corporate capability, that I think is the place to begin.. When I meet CEOs, and I ask them who in this organization is responsible for the following things? Creative brand new products, that could have disruptive potential.. Commercializing research that's happening in your labs.. Taking existing products to radically new markets.. Building brand new internal procedures and IT systems, and I give them a list of things.. Like, if I'm really lucky, and it's a very well-run company, they'll be, a couple of those things, will be somebody's part time job.. But I say, who's responsible for making sure that we do innovation in this company the right way? They generally will tell me, well, that's everybody's job.. Everyone in this company is supposed to think in an innovative way.. Everyone's supposed to be an entrepreneur..

- You're supposed to be innovative at your desk every single day? - Everyone's supposed to be.. And I'm like, oh, that's

great.. Why don't we just apply that same standard to marketing? We don't need a chief marketing officer and a marketing department.. Everyone can be in charge of marketing.. That will be fine.. And people look at me like, that's not going to work.. Obviously that's not going to work.. And I'm like, well, let's do it with finance.. We don't need a chief financial officer.. Everyone in the company is responsible for finance..

It's going to be fine.. You know what, I have an idea.. Let's create a finance lab.. Let's have all the finance people get bean bag chairs, and whatever, accountants probably think foosball is not as cool as, whatever.. Just put them in a lab, in a different city, somewhere else, far away from headquarters.. All the financing can happen over there, and the rest of us can go about our regular jobs.. People would be like, that's insane, you'd be in prison in no time.. Of course.. Because every one of us has that intuitive understanding of what corporate functions are for.. Right? You simultaneously need a way for people who are specialists in that function to have a career path, you know, if you're a finance professional, to grow up and eventually become the CFO..

And also, the functions are responsible for financial literacy across the entire company to make sure that finance considerations are baked into everything that we do.. Budgetary decisions, financial controls, FP and A, the whole thing.. Same with marketing.. Same with IT.. Same with HR.. - So if you sort of cut everything aside and had a magic wand, and you could just do one thing to every organization that you've ever dealt with that would reduce friction and make life better and more profitable for everybody, if you had the power to make that one little change in everything, what's the one thing? - If I could pick one thing, I would change the way that CEOs hold their own staff accountable for these kinds of outcomes.. - Ooh.. - Because most CEOs are very happy for other people in the organization to change their behavior.. But accountability is the foundation of management.. So the way you hold people accountable is ultimately what determines what culture you're going to have, what kind of process you can achieve in a company..

And if you have the CEO set the tone from the start, from the very top, that I'm going to treat my staff, I'm going to hold them responsible for portfolio thinking, and have them report to me how their portfolio breaks down from low risk to high risk.. If that's just a requirement for being on my team, then that's going to be a requirement for being on their teams, and that's going to cascade down.. (mellow hip hop music) Imagine, just visualize for me.. Imagine you had the true God's eye view of a modern company.. Like, you could really see each silo from way up on high, and they're literally like grain silos.. Picture a giant.... - So you actually had complete information which no executive ever can have.. - Right, you could see everything.. You see the design function, the design silo, the engineering silo, the marketing silo, all the silos.. And any time you wanted, you could like pop the top off one of those silos like a Pringles can, and just like zoom in and oh, look, hey, I see the designer doing this highly iterative design thing and it's amazing..

Pop off and look at these agile, doing these highly iterative amazing things.. Imagine like you pop off the manufacturing.. Oh, this is lean manufacturing.. It's so iterative, and say, oh look, in what they call DevOps, in software deployment.. Look, that thing is so agile.. Like this must be such an incredibly iterative and scientific and customer-centric company, but zoom out again.. How does work pass from silo to silo? - So it's the hand-off problem, and it's the language problem.. - Right.. In every silo, we pass work product to the next silo in this totally linear, waterfall way.. Even though individually, each silo's highly iterative..

And now you're the CEO of this company.. - Yes, yes.. - And you meet with, your weekly one-on-one with, I talk to CEOs and I'm like, how frequently does this happen? Is it at least once a month or once a quarter? Every single one of your functional VP's will come into your office and say, you know boss, you know what would really make this company work a lot better? If you put my function in charge of all the other functions, and you made them all learn my method.. - That's right.. Everybody does design thinking.. - Everyone does agile.. Everyone designs things.. We're tribes.. You're not going to put that tribe in front of my tribe.. And the language that we use is not applicable across the board..

You ever try to get designers to do a burn down chart? Cannot be done.. - Okay, so how do you do about it? - So two things are required to solve.. First, you have to build and organization system that is built to learn, not linear.. So you have to build the culture of iteration and customer-centricity, scientific decision-making.. It has to be an enterprise-wide function, not a siloed thing.. And the second thing you need is your question about language.. You have to create a conceptual vocabulary including the most important thing, the unit of progress, that is something that everyone in the organization get bought into.. And if you look at how organizations are organized, the only possible language that can be used there is financial.. - That's really interesting.. - You have to be able to talk about the financial impact of everything..

That's the oxygen that companies consume to be.... And not even companies.. Organizations, non-profits, governments, like it has to be in financial terms.. - Even for non-profits? - Even for non-profits.. Like, how do you make payroll? If you can't make payroll, you don't have a non-profit anymore.. If you just admit that your funders are your customers.. - Okay, okay.. - Then it's actually very simple.. And the model still works.. And again, it's not to value financial impact as the only kind of impact that matters..

It's to be able to quantify how the work that you do translates into financial terms.. So if you were producing outcomes at a non-profit that funders won't pay for, then they might be the greatest outcomes in the world, but you can't produce them anymore.. Like, you will die.. So impact can still be our North Star, our true, we still have a purpose and mission-driven

company, but we have to be able to quantify the impact that we have in the projects that we do.. And that requires a lingo and a set of concepts that are not derived from any one function's thing.. - So you're telling me that those damned bean-counters who drive me crazy, that I actually need them and have to respect their language more? - Yes.. (upbeat hip hop music) - I really want to zoom in on the silo part, because at least for a lot.... - Yeah, these are a huge source of friction.. - And I'm actually, I did do this with a group last week, and these two people, I was in the room with them, they were fighting so much they weren't on speaking terms.. - Oh, that's very common..

The first step towards incubating this new culture is you have to pilot it.. You have to give people the lived experience.. So I'll give you an example.. Since you mentioned people who hate each other and won't speak to each other.. I was once working with a bio sciences company who was building a new high-tech healthcare gizmo.. - Okay.. - And it was all engineers and product people and scientists on this team.. So their nemesis was this guy in the compliance department, who they viewed, the called him The Troll.. - The Troll? - Whatever we want to do, he hates our guts, he only does ever say no.. So like, we can't innovate in this company, we can't ship anything, do anything, because he always says no..

So I said well, remember I said about ports of working across functional team? - They're like, yeah.. We are cross-functional.. We've got engineering and we got science and product, we got this kind of science, and that kind of science, we got software over there, and I was like, okay, but cross-functional means all the functions necessary to produce this product.. Is not legal compliance one of your essential functions? And they're like, you want us to put someone on our team from that department? I was like, yeah.. Fine, so they put in an official request on our expense to have someone transferred.. Guess who gets transferred? Of course, the compliance department puts The Troll on their team.. And they were looking at me like, you were supposed to be our coach, you're supposed to help us, and now you've got-- - Now you've got like-- - You put the viper in my desk.. And I was like listen, do me a favor, come out to San Francisco.. We'll do a workshop.. Bring the guy..

We'll have a whole day together.. So they come to San Francisco, we got the beam bag chairs, the whole thing.. You can imagine The Troll is not so excited to be asked to do this workshop.. This is not like the greatest day of his life.. But this workshop, he is giving me the death stare the whole time, not saying one word.. And finally after several hours of workshop he's like, "Okay, I have a question." "Please." "Are you telling me that I'm going to "get to be involved in this team "like the ridiculous experiments "they're always coming up with "and foisting on me in the eleventh hour? "You're telling me I'm going to "get to be involved in the design of those experiments "from the very beginning?" And I'm like, "Yeah." He's like, "Interesting." Goes back to death stare.. Go about workshop, workshop, workshop.. Breakout time.. Okay, all teams, everyone have a breakout.. Get my team together, and they're starting to brainstorm different experiences they could do..

And one of the teams said, they're like, oh we have this amazing idea that they're going to presale this device to only three hospitals, and it's going to get this experimental data from the hospital, and one of the team members says, "Ah, shoot.. "We can't do that." "And why not?" "Well, everybody knows you can't "presale a medical device before it gets FDA approval.. "So nevermind, can't do that." And they're about to move on, and The Troll's like, "Excuse me, pardon me.. "Does this strike any of you as "the kind of thing that the United States "federal government would do to put out "a rule or a law that's one sentence long?" And they're like, "Well now that you mention it..." And he's like, "So have any of you actually read "the relevant FDA guidance document for" the blah, blah, blah.. They're like, "No." He's like, "Well, guess what, I have.. "It's my job." "And did you know that it's not 900 pages long? "And on page 350, sub-bullet C, "sub-clause seven, footnote two, "that there's an exception to that rule, "and in fact the MVP you just described is legal." - There you go.. - Whole team, like a full minute of silence as everyone picked their jaws up off the floor because now he's being helpful.. I'll never forget when the engineer said, "Are there any other exceptions?" And he's like, "Step into my office, my friends.. "In fact there are seven different exceptions.. "And did you know you can design," and like, off to the races..

And all of a sudden this guy, after the workshop they're like, what did you put in the water to trick him into being helpful? And I was like, "I didn't do anything." All we did was change his context.. (hip hop beat) I really care a lot about the next generation of companies.. Can we help them have a better blueprint that they build to, so that they don't recreate this problems in the first place? - So that blueprint, that's what I want to talk about.. - That blueprint is so important.. So I'll give you an example.. I was working at GE on a project to build a new gas turbine in a new way.. And I was sitting with a room full of engineers and marketers, and I got the whole team together, and we're doing a Lean Startup workshop over the course of three days.. Over the course of three days, we agreed to dramatically change the cycle time to get the first product to market.. We co-develop much of the product with an individual customers.. It's just like, a way better plan in every way than the previous plan, which was going to take like 30 million dollars in five years..

Now we're going to take much less than that.. In 18 months we're going to be in product market.. So much sooner we're going to get feedback from customers.. At the end of the workshop, I said, "Okay, so we're going to present this new plan "to our executive team as the plan." And they said, "Of course we're not." And I said, "I'm sorry, haven't we just worked "for days, we've been laboring for days "to make this way better plan.. "Isn't it better?" And they're like, "Oh, it's way better for sure." And I'm like, "It's way better economically.. "Better engineering." Every attribute I could name, they're like, "Yes, definitely better "in every conceivable way." So I'm like, "So we're going to do this, right?" And they're like, "No.. "This is just an exercise.. "We're not going to do it." I said, "Well, why not?" They said, "Well, EMS." And I was like, "I'm sorry, who's EMS? "What is that?" And they all looked at me like I was like, "What's gravity?" They're like, "EMS.. "GE's legendary employee management system." And I'm like, "What does that have to do with "anything we're talking about here? "You're telling me

that some HR thing is going to" and they're like, "Yeah." And I'm like, "But, as a shareholder, "I'm a GE shareholder.. "Isn't this better? "Isn't the purpose of a corporation as you understand it "to create shareholder value?" And they're like, "Uh-huh, yeah, for sure." "So like, wouldn't the shareholders, "if they were in the room with us right now, "wouldn't they really want you to do this new thing?" They're like, "Definitely, of course..

"Yes, so glad you understand." I'm like, "Okay, so we're going to do it." And they're like, "Didn't I just say no? "Of course we're not going to do it." I couldn't understand what was happening.. So someone finally graciously takes me out of the room.. Like, let me explain to you what's going on.. Every engineer in this company has a personal OKR in the database of the employee management system that says how much rework they case in a given year.. That's part of their engineering functional evaluation.. If you do set based concurrent engineering, there will definitely be more rework.. And I was like, "Oh, got it.. "Now I can fix the problem." I go back in the room.. "Engineers, I now understand that we're "going to have more rework and "you don't want that for your careers.. "Can someone quantify for me "the amount of rework we're talking about?" And they said, "No problem." It's engineering, a highly precise estimate of blah, blah, blah, blah, blah..

This could be a million dollars of extra rework.. And I'm like, but isn't this like a 50 million dollar program? Isn't that right? And everyone's like, "Yeah." So like, "Isn't this a great trade? "Let's embrace the rework for "the sake of improved product." And they're like, "No, of course we're not going to do that." And eventually someone's like, "You idiot.. "People want to be promoted.. "They're not authorized to unilaterally "violate this system." And I remember sitting there like, "Oh, this is no problem.. "Who do I talk to to get an exception made?" And it was literally as if I'd been like, "Who do I talk to to get "an exception made to gravity?" They're like, "You don't make exceptions." They just couldn't understand it.. So that was like, it was such a good lesson for me about a concept I call career equity.. The true way that individuals in organization context are compensated is not with their current cash bonus, whatever incentive plan you think they have.. That is generally dwarfed by their perception of future advancement opportunities.. So you put up a poster that says, hey, everyone be more innovative.. You say, I'm going to pay anyone who innovates at 10 thousand dollar cash bonus..

That's actually insulting.. You're saying to me, I should risk being perceived as a failure by my peers, which over the course of my 10, 20, 30 year career with this company is going to mean millions of dollars in lost earnings, and more importantly, way lower probability of me getting that dream job that I've always wanted to have in exchange for this paltry bonus? F you.. - But in a lot of the big companies that I work with and have studied that are innovative that have management systems much as you talk about, what happens is there's the official system, but then there's two things that happens.. One is, in one company they call it the submarine projects.. These are projects where you go beneath the surface, you don't tell anyone what you're doing, and sometimes even lie to your boss, or you have a boss who lies.. - Who lies for you.. That's one of the most prized attributes of a good boss.. - Of a good boss.. So that's one.. And the other model I can use the example of Steelcase..

I spent a few days wandering around Steelcase at one point about a decade and a half ago trying to understand their stage gate system.. And it was explained to me that if something was really important, it didn't have to go through the stage gate.. If the CEO really wanted it.. - You have to have that exception, because-- - So those are both systems for, or solutions for removing the systems and both of them are ignoring the existing system.. (hip hop music) - I wish I was creative enough to have made this up.. I was literally, this is a true story.. I was sitting in the office of a six sigma functional leader for a manufacturing company.. And his job is to make sure that there's no defects on the factory floor.. He has a very-- - Which makes sense-- - A very important job in the company.. But of course six sigma claims not to just be a manufacturing methodology but a general purpose management philosophy..

So his job was to make sure that everything the company does has six sigma levels of precision.. And he had on his desk an item which made it impossible for me to focus on the meeting, and I was really having a hard time paying attention to him, because he had a mug, an actual coffee mug on his desk, and said, "Failure is not an option." Printed on this mug.. - It's like Apollo 13.. - Yeah.. Failure's not an option.. And I was sitting there being like, wow.. What an amazing reality it must be to live in that you think that's something you can put on a mug and proudly display, right? Because the underlying assumption of owning that mug is that you believe that failure is always preventable through diligent preparation.. Always.. And I was sitting there being like the entrepreneurs that I admire, and our tribe, what would our mug say? If we had our own mug, what would it be? It would be, "I eat failure for breakfast." - Right.. - So if I only fail four times by the time I get to lunch, that's actually a pretty good day on average..

Like that's pretty impressive.. - So this is actually a good friction conversation, because early in my career, I wrote a book called Weird Ideas that Work, and I went down to Disney Imagineering.. So you know, Disney got the parks, they run perfectly, got Imagineering, and I talked to some other executive about Disney Imagineering versus the parks, and this guy looks at me, and he says, "Those people are idiots.. "Almost everything they try fails.. "And everything we do works.. "Why are they of any value at all?" - And that point of view, from the mainstream corporate, is correct.. The fear of failure is a very common obstacle.. And it's funny, you ask people, why don't you do something innovative, people say, well, I'm afraid, you know, this company punishes failure.. And I talked to executives, they're like, I wish we punished failure more.. Like what are they talking about? We don't fire anybody around here, right? So there's already a misperception from the different levels for what gets rewarded and not..

So we can't just put up posters that say everybody take chances and be risk-takers and failure is great.. I don't buy into the whole embrace failure, fail fast.. I don't use that language as much as I can avoid it.. What I think you have to do is first you gotta find people who are willing to do it even though it's irrational, to pilot the new way.. So you gotta show, like in every organization there's certain people who, for whatever reason-- They'll try new stuff even though it's nuts.. - It is actually bad for their career equity, and they just can't help it, they do it anyway.. So you gotta find those people and you gotta start piloting programs with them to show that there is this new possibility.. You have to reward them publicly, to say hey, this thing failed, but actually that's not that bad.. And eventually you have to start to incorporate it into people's performance review.. I always recommend a line in the performance review matrix that's just, how many productive failures did you have this year? - Okay..

- Someone who says they didn't fail all year long is lying to you.. So okay, first of all, that's helpful to know if someone's lying to you.. That's good to know.. Or they were so unbelievably conservative in their work that you got to ask yourself, is this a job that I want the maximum conservatism? Because there are some jobs where you're like, I'm fine with that.. - Airplane pilots.. - Yeah, very conservatives, all good.. Many, many jobs, that's not what you want.. And then the second thing is it forces people to be like, well what's a productive failure? And then you're like, okay.. Failures due to incompetence are bad.. But failures that led to some kind of useful learning, a pivot that allowed us to build a more successful product, or the most common productive failure is simply a realization that this is a bad idea..

So like I was working with a team that asked for a million dollars to build a new product.. And the company was going through a lean startup thing.. They say, well, we'll give you a hundred thousand dollars for an MVP instead.. And they're all like, the first customers they showed this concept to were just like, "This is idiotically wrong, "in ways that you have no idea." And they're like, oh, this is not looking good.. They did two or three more of those MVP's, and they're like, oh, our whole concept for this thing, how the market works, how you get paid.. Like this is a horrible, horrible idea beyond belief.. And they went back to the company and said, we don't, we think we're going to shut this project down.. And they were about to get in trouble, because finance was like, you just wasted a hundred thousand dollars on this stupid project.. - We saved you 900 thousand dollars.. - And luckily those others say, whoa, we just saved 900 thousand dollars because we were willing to admit this is a bad idea..

So that actually like, you give people the experience of that, the reward that you talk about that, you make it part of their promotion attributes.. Structural and accountability systems drive culture.. (upbeat hip hop music) - Thank you very much for joining us for The Friction Podcast, Eric.. - Thank you so much.. The admiration is mutual, so thank you.. - That was fun.. Friction is often caused by misguided incentives.. An incentive that may make sense to a leader can trickle down and create fear and stagnation.. The great thing I learned from Eric is that if you're a leader, sometimes you've got to look in the mirror and realize that your favorite incentive, the one you're enamored with, is actually making people's work harder to do.. Please spread the word about The Friction Podcast..

Rate and review us on iTunes and share your favorite episodes with your colleagues, your family, even your therapists.. On the next episode, we'll be joined by Michael Arena, chief talent officer for General Motors, and author of a new book, Adaptive Space.. Michael is going to talk about how large organizations can harness creativity and innovation to compete in today's market.. And now for the final tangent.. What do you do to set the path so that people who do entrepreneurial work can actually function without getting squished, abused, ruined and driven out by the other, albeit necessary functions? - We have to create a corporate function that can contain that energy and create professional standards and metrics of accountability.. - Okay, so what are some of the metrics that will actually allow entrepreneurs to flourish rather than get crushed? - The Excel spreadsheet is still very valuable because it is actually a set of deductive arguments for why a specific set of customer behaviors, when aggregated together over time, leads to a financially valuable business impact.. So you have a spreadsheet, and it says what's supposed to happen, and I found a cell in the spreadsheet that said 10% of customers are going to sign up for the free trial when given the opportunity.. Now, that is not something that I think should be kept in two point font in appendix B of the business planner.. That's what we call a leap of faith assumption.. - Right..

- So important to the success of the business because what happens to your beautiful spreadsheet if I change that 10 to a zero? Like can you visualize the nuclear holocaust of zeroes if they spread out across the entire, like, customers won't sign up for their free trial.. Does it matter what the average lifetime value of the customer is? Does it matter what their retention rate? Like, so that's a really important number.. Now, imagine I do a minimum viable product experiment, and only one percent of people are willing to sign up for the free trial.. Now, normally, in corporate studies that's like terrible news.. You want to hide this bad news.. Don't tell anybody, because oh gosh, we're way off.. But in innovation counting we actually start to see that is the accomplishment of a milestone.. At least now we know where we are.. Knowing where you are on the map gives you a chance of getting to where you want to go, because now you're like, we're on the field, we've not made it to the opponent's end zone, we haven't gone a hundred yards yet, but we have gone one yard, so that's pretty good.. So the spreadsheet allows us to translate these learning metrics about individual customer behaviors into financial terms that even the most hard-nosed and skeptical finance department can take seriously, especially if they are given an opportunity to collaborate on the construction of the spreadsheet in the first place..

(hip hop music) - We can't do this without you.. Tell us what's driving you crazy, and what are you doing to make life better in your organization for yourself and for the people that you work with.. Please send us your friction stories, tips and tricks..

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Thanks for joining us. This is The Friction Podcast...