

Creating Value through Innovation

Master Thesis in Corporate Finance

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Abstract

Innovation is a key value driver of corporations. A review of academic literature presents an overview of present methodologies of innovation management and controlling. Main factors influencing innovation performance have been identified: strategy, structure and culture. In accordance with these findings, a framework has been developed and three companies have been analyzed. The major finding is that innovation processes are complex and require an inside view of the company for a complete analysis. Innovation and customer focus together with efficient knowledge management, entrepreneurship and a clearly defined cross-functional innovation process are the essential factors for successful value creation through innovation.

Executive Summary

I Problem description

Innovation is an important value driver for a company. Within an environment of increasing competition and standardized production processes, technology developing innovative products that serve the customer needs in a better way is the only possibility to reach a competitive advantage and ask a premium for the sold products. Following the Schumpeterian model of Creative Destruction, innovative companies should not exist over time. However, within many industries, companies can be identified as being constantly innovative by developing new products and with that, are able to escape the creative destruction. The set-up of these companies in terms of managing and controlling innovation is a major point of interest. The innovation process is nonlinear and requires a certain amount of risk-taking within an uncertain environment. Mistakes are part of the learning process. This stands in contrast to the value creation of a company, where major actions are taken in order to avoid mistakes and efficient processes are set up in order not to waste any resources. The subject of this thesis is to identify factors that enable companies to be constantly innovative and create sustainable value through innovation.

II Methodology

The first part of this thesis provides a theoretical overview of definitions and sources of innovation. Based on the definitions from classical economists such as Joseph Schumpeter, different sources of innovation are discussed and evaluated. This is followed by an overview of the present academic research, which will be presented in order to identify the essential factors that are influencing value creation through innovation.

The second part of the thesis evaluates different approaches and factors of innovation management techniques. The Stage-Gate as well as the Open Innovation model is considered to be a state of the art method in managing innovation. These two models are deeply discussed and evaluated based on findings within literature. A combination of the two models is described shortly. Leadership, entrepreneurship, and rewards are identified as soft factors that are essential for successful innovation management.

Controlling the innovation process is important for successful value creation. It ensures that

resources are used efficiently and therefore, that value creation is maximized. The thesis includes a set of qualitative and quantitative controlling metrics. Each of them is allocated to a defined section (inputs, process, product and customer, and results) of the innovation process. After having elaborated a diversified theoretical overview of all relevant parts of innovation within a company, a framework is developed based on three main factors (strategy, structure and culture) in order to analyze and identify innovative companies. Moreover, incremental key elements for successful value creation through innovation should be identified. Due to the complexity of innovation, the framework delivers a selection as opposed to an explicit list of possible factors for the analysis. This provides the freedom of customizing the framework with respect to the selected company.

The developed framework is then used to analyze three selected companies (Hilti Aktiengesellschaft, Sika AG, 3M Company). The analysis makes use of two pillars in analyzing the public available data (annual report, Internet presence) as well as internal data collected through interviews with representative employees being part of the innovation process. Finally, the results of the individual analysis are compared with the overall goal to identify important factors that are essential for successful value creation through innovation.

III Results

The review of the academic literature in combination with the analysis of the three companies clearly shows that innovation is a complex cross-functional process within a company. It is therefore not the case that a finite set of unique factors is responsible for a successful innovation performance, but rather that the innovation performance is a result of the defined corporate strategy, the corporate structure and the corporate culture. Through the developed framework focusing on these main factors it is possible to assess companies with respect to innovation performance and to determine key elements that are supporting value creation through innovation. It is essential to get an insight of the analyzed company in order to be able to get a full picture and judge whether innovation is really an attitude within the company. Published information provides hints, but not the required amount of information necessary for a sustainable analysis.

The following key elements have been identified by the analysis: The strategy must have a clear focus on innovation and the needs of the customer. Therefore, the corporate structure

must map the strategy with respect to the customer. In addition, an efficient system where information circulates quickly in order to make innovation available for all units must be set-up. Moreover, a central knowledge pool where all the projects and developments are retrievably stored must be set-up, available for all employees within the innovation process. The innovation process must be well-structured based on clear objectives. Controlling all the different elements of the innovation process with a set of metrics is necessary so as to ensure efficiency and optimal value creation. Furthermore, the corporate culture is a major driving force of innovation. Entrepreneurship, trust and empowerment to take responsibility and being creative with the constant desire for new and better solutions that serve the customer are essential.

IV Assessment

The analysis of the academic literature provides an overview of the latest state of research on innovation. Together with the elaborated framework, it might help to get an understanding of which factors must be considered as important if a company is analyzed with respect to its innovation performance. It is obvious that in order to get robust results for essential innovation factors, the analysis should be expanded to a greater number of companies. Therefore, the analysis must be seen as exemplary. The results show that creating value through innovation depends on multiple factors, with many of them being denoted to be soft factors and their nature seen as difficult to quantify. Nevertheless, by making use of the framework, it is possible to see differences and commonalities across different companies. This might provide a value added either by helping take investment decisions or improving a company's innovation performance.