



*cutting through complexity*

# HR as a driver for organizational innovation

A unique opportunity





# Foreword

# Becoming a key strategic partner

It is widely accepted among business leaders that innovation is vital to both competitive advantage and long-term success. In fact this year, business leaders cited innovation as one of the top three global challenges they faced.<sup>1</sup>

And for most companies, the ability to innovate is the single most important predictor of future growth.<sup>2</sup> It is hardly surprising that investment decisions now tend to be tied closely to how focused companies are on transformational innovation.

So, when it comes to innovation, what do successful corporate innovators have in common?

Contrary to popular perception, success does not appear to be determined by a company's R&D budget. Research has consistently shown that there is no statistically significant relationship between financial performance and innovation.<sup>3</sup>

Nor does technology appear to play the most important role.

Instead, studies strongly show that the most successful corporate innovation strategies are the ones that predominantly focus on people and human capital. These include finding, engaging and incentivizing key talent for innovation, creating a culture of innovation by promoting and rewarding entrepreneurship and risk taking and developing innovation skills for all employees.

## Culture is king

One overriding theme emerges from studies of successful innovation strategies: *winning companies first and foremost have*

*developed cultures where innovation is seen as everyone's responsibility.* As an objective that employees at all levels and in all roles strive to achieve on a day-to-day basis.

Meanwhile, many of these companies also have at the core of their cultures an acceptance of the need to experiment and understand that, with this, comes the risk of failure. Their people see honest failure simply as a learning experience.

In addition, the studies show that winning companies recognize the part played by internal and external networks and have, in a bid to facilitate collaboration, taken every opportunity to connect their people.

Culture, it seems, is key to sustainable innovation.

## HR's big opportunity

All this is great news for HR, which – above all other functions – is perfectly placed to develop and sustain the kind of cultural transformation required if a company is to achieve its innovation objectives.

That is because HR is fortunate enough to be responsible for many of the levers required to bring about this transformation.

For example, performance management can serve as a valuable tool in the creation of a sustainable culture of innovation – as HR managers can ensure innovation features prominently within a company's objective setting and appraisal processes.

Reward, meanwhile, can be used to reinforce the importance of innovation activity and outcomes – while recognition schemes can be used to encourage and

inspire employees to innovate and to share ideas (even if the ideas fail).

Finally, HR's role in organizational design provides huge potential for enabling innovation. Specifically, organizational design can be used to facilitate easier exchange of employees' ideas across boundaries and functions.

These are just three examples of HR levers that provide the function with a unique opportunity to be a key driver of the innovation agenda, delivering sustainable competitive advantage, and becoming a true strategic partner. In doing so, HR can take its place alongside other mission-critical functions such as finance and IT and, ultimately, make the people agenda more important to business leaders than the balance sheet and P&L statement.

## Time to step up

HR, however, must rise to this challenge. This paper, from KPMG's Global HR Transformation Center of Excellence, provides practitioners and advisors of HR with guidance on bringing about the cultural change needed to build innovation into the way people at all levels think and work every day.



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<sup>1</sup> Conference Board, CEO Challenge. 2013

<sup>2</sup> Economist Intelligence Unit: Fertile Ground: Cultivating a talent for innovation. February 2009

<sup>3</sup> The Global Innovation 1000: How the top innovators keep winning. Booz & company, 2010





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# Why innovation matters

Research shows that most business leaders now view innovation as vital to their company's long-term success and competitive advantage.<sup>4</sup>

And with innovation identified as the single most important predictor of the future for most companies, investment decisions now tend to be tied closely to how focused a company is on transformational, as opposed to incremental, innovation.<sup>5</sup>

The C-suite's growing focus on innovation is largely due to executive-level acknowledgement that the days of being able to take growth for granted are over.

Corporate leaders know they can no longer expect established markets to simply keep on delivering, year after year. Now, they are looking for that growth from new markets, products and services.

Organizational innovation is critical to making this happen.

## Innovation: failure and success

Across the corporate world, traditional approaches to innovation have either failed or have simply been rendered redundant by results that are sporadic at best.

Specifically, some businesses have focused on hiring creative people and setting them free to introduce innovation. Others have relied only on luck, simply hoping for the best – or taken ad hoc and unstructured approaches to innovation. Others still have attempted to kick-start the process through a one-off set of creativity exercises or perhaps a 'big bang'-style internal communications campaign – only to fail to build capacity to innovate on a sustainable basis.

Many other businesses, meanwhile, attempt to 'do an Apple' and replicate another organization's successful strategy. However, this approach is also highly likely to fail – if only because innovation looks very different from one company to the next.

For example, under Steve Jobs, Apple had a very controlled and centralized approach to product development. By contrast, 3M has developed a more dispersed approach. Yet both companies are successful innovators. Essentially, there is no value in setting out to copy another company's methodology.

Instead, we believe, you should develop an approach to innovation that is right for your unique set of circumstances.

So, when it comes to innovation, what do Apple, 3M and other successful innovators have in common?

First, it is not about how much is spent on R&D. An annual innovation study has shown repeatedly that there is no statistically significant relationship between financial performance and innovation spending.<sup>6</sup>

Nor does technology play the most important role.

Instead, the research strongly indicates that the most successful corporate innovation strategies are the ones that predominantly focus on people and human capital issues.

<sup>4</sup> Economist Intelligence Unit: Fertile Ground: Cultivating a talent for innovation. February 2009

<sup>5</sup> Economist Intelligence Unit: Fertile Ground: Cultivating a talent for innovation. February 2009

<sup>6</sup> The Global Innovation 1000: How the top innovators keep winning, Booz & Company, 2010





These strategies include:

- engaging in strategic alliances with customers, suppliers, and other business partners
- finding, engaging and incentivizing key talent for the purposes of innovation
- promoting and rewarding entrepreneurship and risk taking
- developing innovation skills for all employees.<sup>7</sup>

The one common theme to emerge from among these successful strategies is that the companies had developed or were developing cultures where innovation was seen as everyone's responsibility – and as an objective that employees at all levels and in all roles strived to achieve on a day-to-day and business-as-usual basis.

In addition, many of these companies had at the core of their cultures an acceptance of the need to experiment. They understood there was a risk of failure but viewed honest failure as a learning opportunity.

Finally, many of these companies had recognized the part played by internal and external networks and had, in a bid to facilitate collaboration and the clash and contrast of different perspectives, taken every opportunity to connect their people, including moving them out of functional silos.

From Pixar to Procter & Gamble, from Tata to Toyota, Apple and Google, culture – it seems – is the key to innovation.

But how do these companies build cultures where every employee sees innovation as part of their job? What steps have they taken to create a culture of creativity? Where corporate values include collaboration and an acceptance of failure as simply a learning opportunity?

What are the pre-requisites for building this brave new world?

<sup>7</sup> The Conference Board CEO Challenge, 2013



# The innovation dynamic



KPMG's Global HR Transformation Center of Excellence has identified 11 key factors common to established innovators.

The Center did this by:

- Reviewing characteristics common to organizations with a successful track record of innovation
- Reviewing academic research into innovative organizations
- Combining findings from these reviews to create an initial list of organizational capabilities
- Trialling an 'innovation dynamic' questionnaire – then using the results to conduct a factor analysis that helped refine the list of key factors.

Each factor relates to either a company's structure, processes or its culture.

Taken together, these factors make it easy to see where a company needs to improve when it comes to developing a culture of continuous and widespread innovation.

## Structure: room at the top

Anyone looking to unleash innovation on a sustainable basis should start by asking themselves how much personal involvement does the top team have in the sponsorship and coordination of the company's innovation activities.

In other words, to what extent do leaders back the innovation agenda and show long-term commitment to the development of the workforce's innovation capabilities?

For most companies, creating a culture of creativity requires a sustained and well-planned change management program. And, at least initially, every successful instance of change management begins with backing and buy-in from the C-suite.

Other key questions:

- How integrated is innovation in the corporate strategy?
- Do top team members possess the capabilities to manage risk and convert creativity into value?

## Structure: connectivity of networks

Collaboration, both internally and with external stakeholders, is also a key prerequisite for innovation.

With this in mind, companies need to consider how well their employees are well-networked.

Are they connected to colleagues and, for example, external advisors in a way that allows them to access other people's expertise and insights?

Other key questions:

- Are employees encouraged to proactively build and manage their internal and external networks?
- What opportunities are there for employees to gain exposure to and build relationships with external partners such as suppliers and advisors?

## Structure: employee discretion

Creativity tends to occur when employees feel safe and positive.

Yet research suggests that only 47 percent of employees are allowed to take controlled risks, and that only 52 percent report that their manager is good at listening to new ideas.



With this in mind, it is important to ask how much 'discretionary space' there is for employees to display initiative and how much flexibility there is when it comes to working practices and job design. Is the corporate culture more 'tell and do' or 'coach and solve'?

Other key questions:

- Is work organized around narrowly defined job descriptions, or looser role profiles?
- Do employees have the time, space, tools and resources to make an innovative contribution?

## Process: 24/7 radar screen

It is also necessary to consider how much time people at all levels think about what is coming next and what is on the horizon.

For example, how much time does the top team spend discussing the company's long-term future? Are employees encouraged

to scan the horizons? Are they expected to look around corners for the next big thing? Overall, what processes are in place to identify emerging trends in technology and the market place?

Other key questions:

- How alert are employees to the strategies and tactics of current and emerging competitors?
- What links does the organization have with trend-spotting gurus, futurologists, think tanks and others at the 'edge of innovation'?

## Processes: nuts-and-bolts obsession

Does the organization actually have a process for innovating? Has anyone defined and communicated an innovation methodology?

A basic methodology remains vital, if only so employees with a good idea know what needs to happen to take it forward.





For example, fashion retailer Nordstrom uses an ‘innovation lab’ to accelerate idea generation, testing and development. And chemical company Dow has developed a ‘talent allocation framework’ to assess individual innovation skills and to ensure the right composition of skills exist in a project team at different stages of the innovation.<sup>8</sup>

Specifically, what processes does the organization have in place for idea generation, and for idea evaluation against a set criteria.

Other key questions:

- Do innovation processes exist?
- What training and development is provided to employees in relation to these processes?
- How often are these processes reviewed and updated?

## Processes: spanning boundaries

Within the organization, is work organized within discrete functional units – or is it delivered through cross-functional collaboration? How ‘porous’ are the boundaries between your company’s different roles, functions, and geographies? And how well do different business areas cooperate as part of an overall organizational effort?

Other key questions:

- Does the organizational culture support cross-functional and cross-regional working?
- What use is made of social media and crowdsourcing to draw on wider experience and wisdom?
- Does the physical infrastructure (buildings, layout, facilities) facilitate collaboration?

## Processes: courageous conversations

Still with processes, anyone seeking to build a culture of innovation within a company needs to ask themselves if employees interact in a way that is open and honest? Or closed and defensive?

Other key questions:

- Does the top team speak directly about the business challenges faced by the organization?
- How are performance reviews conducted? With authenticity? Or do managers simply go through the motions and tick the box?
- Who enjoys promotion? Employees who speak the honest truth or those who opt for an easy life?

<sup>8</sup> Corporate Executive Board, CHRO Quarterly, Q3, 2012

## Culture: current world is not enough

Moving to the third and final category of culture, it is necessary to ask how driven employees are to take the company 'from good to great.' To do what it takes to sustain success.

Other key questions:

- Are individuals and teams encouraged to leave their comfort zones?
- Are stretch goals established to reflect business ambition and how do these compare with the aspirations of established and new competitors?

## Culture: diversity gains

Another key factor displayed by established corporate innovators are top teams featuring diverse backgrounds, perspectives and mindsets.

In other words, does the organization manage diversity in a mature way? Does the leadership value and embrace difference? Does it appreciate diversity of thought and culture?

Other key questions:

- Do different bio-demographic and cultural groups view the organization as inclusive?
- What processes are in place to ensure the proactive recruitment of 'difference'?
- Does the induction and socialization process encourage employees to bring their unique personalities to work?

## Culture: okay to fail

For unsuccessful attempts at innovation, is there a culture of blame and penalties within a company or are individuals/teams rewarded? What processes are in place to review mistakes and capture and share the learning?

To build a sustainable culture of everyday innovation, the organization also needs to look at its history of failure and success when it comes to bringing ideas to life – and ask why this has been the case.

Other key questions:

- What is the organization's philosophy and approach to risk management?
- What has been the track record of organizational success and failure in innovation? Why?

## Culture: everyone's job


Finally, time needs to be spent on considering whether or not innovation is seen as the preserve of specific teams or functions – or if it is instead built into expectations for all employees.

And if there is a specific innovation team, how well does it interact with the remainder of the workforce?

Other key questions:

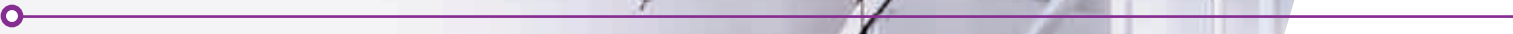
- How prominent is innovation in organizational briefings and updates?
- How well are innovators supported by their colleagues and managers when it comes to workloads and deadlines?
- How are employee innovations highlighted and celebrated internally?





"The Chief Human Resource Officer must be a key player in the company's ability to innovate and outpace the competition."

**Managing Talent for Innovation  
and the HR Function of the Future,  
Heidrick, 2009**







# Key HR drivers for organizational innovation

Set out below are a number of activities HR practitioners can undertake to embed innovation in their organization's DNA.

<b>Performance management</b>	Consistently convey the correct signals about innovation expectations to every employee within the company
<b>Reward and recognition</b>	Reinforce the importance of innovation activity and outcomes through the use of recognition schemes that encourage and inspire employees to share and develop ideas – even if the ideas might fail
<b>Talent management for individuals</b>	Ensure all employees understand the unique skills and behaviors required to successfully innovate in their organization
<b>Talent management for teams</b>	Break down internal silos and promote idea sharing by building career development frameworks which encourage resource sharing
<b>Talent management for leadership</b>	Develop leaders to continually “horizon scan” and adopt a mindset of dissatisfaction with the status quo
<b>Identifying critical roles</b>	Identify which roles disproportionately drive innovation value, develop the people filling these roles and ensure full competence in innovation processes
<b>Organizational design</b>	Architect the organization (structures, processes, roles, capabilities, etc.) to support the innovation strategy, accelerating the idea lifecycle by minimizing boundaries and promoting collaboration
<b>Internal communication</b>	Leverage technology to encourage cross organization networking and collaboration
<b>Change management</b>	Facilitate the implementation of new working practices that drive innovation

# Conclusion: HR's unique opportunity

There is considerable evidence that HR continues to experience a credibility issue and that it is perceived to lack demonstrable strategic impact.

This does not, however, have to be the case.

On the contrary, the C-suite's current and probably permanent eagerness to develop a culture of continuous innovation leaves HR facing a unique opportunity – and a clear and simple choice.

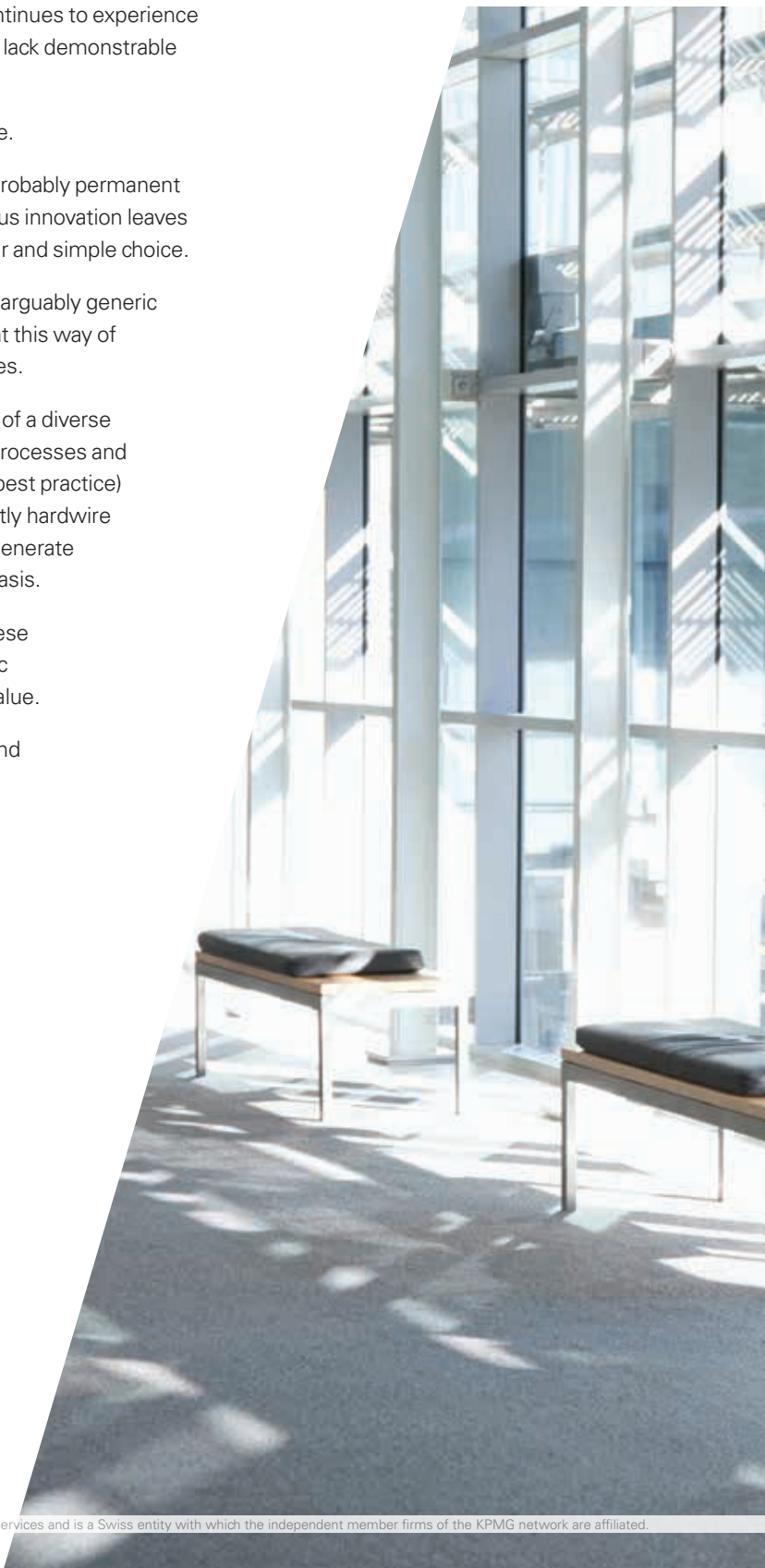
HR directors can either continue to pursue arguably generic models and 'best' practices in the hope that this way of working will deliver their leadership's desires.

Or HR can use its unchallenged ownership of a diverse range of key levers, to uniquely configure processes and practices and deliver a best fit (rather than best practice) approach to innovation – and to subsequently hardwire into their organization's DNA the ability to generate breakthrough innovation on a continuous basis.

In the medium to long term, only one of these options is likely to position HR as a strategic partner that adds significant and tangible value.

One of these options will see HR survive and thrive as an indispensable value creator.

The other is likely to see it wither away.









# About People & Change



KPMG's People & Change teams focus on executing the people agenda on large-scale, complex, transformational change programs, and transforming the Human Resources function through the use of technology, analytics and performance improvement.

KPMG's network of firms offer a broad range of services:

- **Behavioral Change Management** – accelerating and making sustainable the successful implementation of change by developing strategies that deal with the impact on people created by changes to strategy, structure, processes and technology.
- **Talent Development** – developing strategies that can be implemented by identifying and developing the human capital within an organization.
- **Organization Design & Development** – creating organization designs that can deliver the capabilities and performance required by the client's strategic intent.
- **HR Function Optimization** – creating an HR function by developing leading delivery models for the implementation of the broader Human Capital strategy.
- **Workforce Optimization** – includes the workforce analytics required to achieve optimization of employee cost, capacity, capability, connections and compliance. KPMG professionals can offer further insight by helping develop strategic and operational workforce planning solutions.
- **Technology Enablement** – includes developing information technology strategies and roadmap, business case and ROI analysis, technology vendor assessment and implementation, and the facilitation of business performance through the use of information and analytics.

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