Vision & Execution
MARKETING STRATEGIES THAT DELIVER RESULTS

An Industry Survey

After "Internet Time":

5 New Realities for Product Development in the Internet Economy

Studying the Evolution of the Internet Economy

We have all heard about the 'new" New Economy, the Internet Economy, and more recently, the Internet Bubble, Boom, and Bust. Methods of product development, marketing strategies, and other key processes underwent considerable changes during this recent economic period. Through this evolution, some experts suggest, organizations have fundamentally changed the way they do business. Yet others point out that as attention has turned back to "Old Economy" companies¾in reaction to recent economic changes and the stock market correction¾perhaps things haven't changed very much at all.

What's the reality?

Curiosity about this question led Vision & Execution to conduct industry research that explored how companies' product development processes are managed today as compared to how they were managed 18 months ago near the end of the Internet boom.

The companies that responded to this survey ranged the spectrum from start-up ventures to large established corporations. Over 80% consider themselves "new economy" companies or companies whose businesses are based on the production and application of knowledge. The remaining 20% considered themselves "old economy" companies whose businesses are based on the production of physical goods. Nearly 50% of the respondents described themselves as business-to-business companies. Over 70% have 500 or fewer employees and nearly 70% earn $100 million or less.

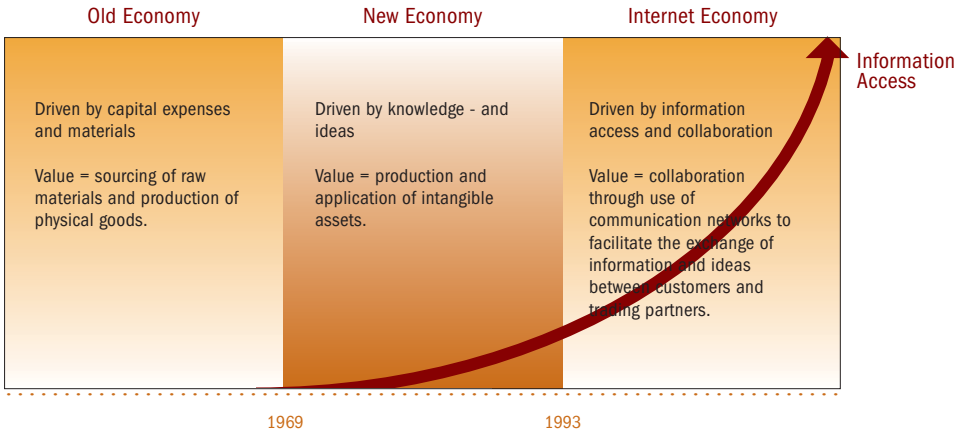
The results of this research provide insight into a set of best practices by companies whose product development processes have allowed them to prevail through these turbulent times. These New Realties can help you achieve your revenue goals and gain incremental market share. They also identify shortcuts that make sense to help you get to market faster without sacrificing the bottom line.

Succeeding in the Internet Economy

Over the past three decades, the speed of business has increased at an exponential rate. Since 1993, with the arrival of the Internet Economy, we have been driven faster and faster to get funding, define strategies and business models, identify and prioritize customer wants and needs, and expand our businesses.

- **The "Old Economy"** is a capital expense- and materials-driven economy in which value is created by the sourcing of raw materials and production of physical goods.

- **The "New Economy"** is a knowledge- and idea-based economy in which value is created by the production and application of intangible assets such as ideas, brands, and ways of working.



- **The "Internet Economy"** is an information access and collaboration-based economy in which value is created by the use of ubiquitous, low-cost communication networks to facilitate the exchange of information and ideas between customers and trading partners.

Internet time is the increasingly rapid time compression for Internet product development, rollout, and the related window of opportunity to gain market share.

Today, the period referred to as "Internet time" seems to be over, but the Internet Economy is really just beginning. The potential importance and duration of this economy is incalculable.

Thus, the challenge for many businesses has become one of finding the balancing point between cutting corners and superior execution. Many schools of thought have come into being in recent years about how to find this balancing point, with such experts as Geoffrey A. Moore and Regis McKenna weighing in on both sides of the issue.

The Survey

Vision & Execution's goal for this research was to examine beliefs about how to be successful in the Internet Economy, and to evaluate how successful those beliefs were for new and existing businesses. Overall, since the "Internet bubble" burst, has anything really changed? Are companies running their businesses differently? How many companies succumbed to Internet hype and changed how they ran their companies? The research also examined areas where shortcuts were taken, and how well companies succeeded as measured by achieving revenue goals or incremental market share.

Some of the questions we asked were:

How are investments prioritized?
During the "Internet Boom" years, the biggest funding challenge was for venture capitalists to give funding before the next VC said yes. This epidemic of funding hysteria led to shortcuts in due diligence of business models and financial cases. Funding for new products was often driven by strategic customers who would help put companies on the map. Were companies that were successful in getting funding without a clear vision of their corporate and product strategy just as successful as those who took time to understand their markets?

How often should strategy be revisited?
The Internet Economy was all about changing the rules, creating a New World order: out with the old, in with a new way of doing business. For some companies, this new way of doing business was about flexibility: being able to "turn on a dime" in response to perceived new opportunities or competitive threats. Were companies that were adept at quickly changing their business models more successful than those who stayed the course?

How important is first-to-market advantage?
"Being first to market is everything!" or so many companies thought. If you get to market first, you'll grow faster and have all the customers. All the mantras espoused the urgency of the Internet Economy. In reality, did getting to market faster have an actual payoff? Was it worth the price?

How much process in the product development life cycle is needed?
Does process matter any more? Or, is it all about rapid prototyping and iterations? How many steps in the product development process can companies eliminate, yet still get a product to market that customers will buy, and be satisfied with?

Does customer input matter?
For the Internet Boom years, getting big fast with viral applications was the goal. Did companies know who their customers really were? And, how much did these customers actually value the service they signed up for or bought? In other words, would they be willing to pay when the venture capitalists stopped funding the market share land grab? Did companies ask customers to test new products to see if they worked, and if anyone would be willing to buy them?

The answers we got were sometimes expected, sometimes surprising, and always food for thought.

Reactions to the "Internet Bust"

Where did companies make changes to improve their success rate at introducing new products? Nearly a quarter of the companies made no changes. Either they were not swept up in the energy of the Internet bubble and had been conducting business as usual, or they are still operating with beliefs prevalent during the Internet Boom and have not adjusted. For the remainder, focus and results were the watchwords.

- 23% stated there has been no change in their approach to prioritizing product development
- 28% stated they are more customer focused
- 16% stated they are more focused on costs/benefits or financial return for their company
- 13% stated they are more structured/process driven
- 10% stated they are more focused on strategic vision or core opportunities

Prioritizing Investments

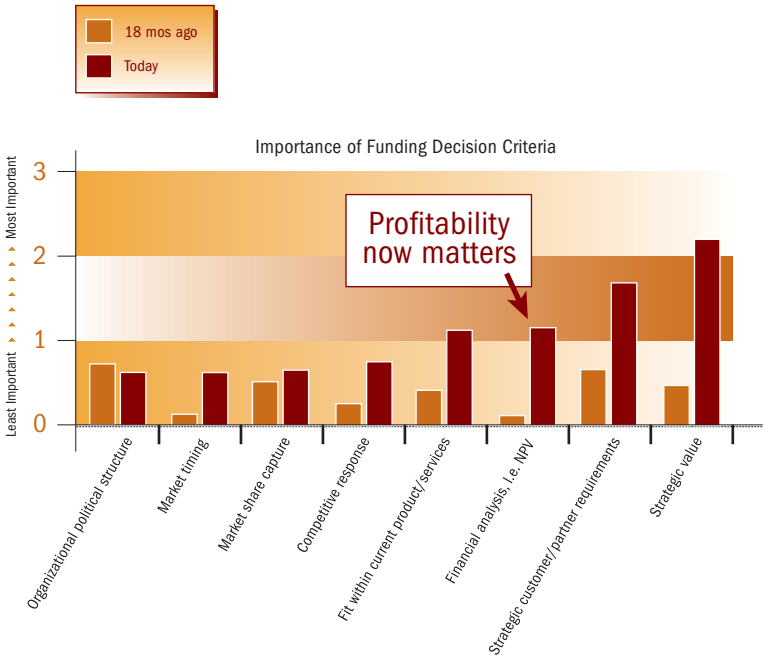
Internet Time Belief #1
If we build something cool, venture capitalists will fund it, and people will buy it.

This first belief is as true of large corporations fighting for internal allocations as it is for start-ups. Even in a good economy, companies struggle with prioritizing funding allocations.

Nearly 60% of respondents have not changed their funding criteria in the past 18 months. Of those companies that have changed their funding priorities, the top drivers 18 months ago had more to do with power and influence of executives and/or large customers to get market presence.

Quantifiable measures resulting from financial analysis had the lowest priority for funding decisions 18 months ago.

Today, there appears to be even greater focus on the strategic value of funding decisions. One of the most dramatic changes from 18 months ago is in the use of financial analysis to assess profitability. Financial analysis was the top funding criteria for companies who gained incremental market share and the second highest criteria for companies who met or exceeded revenue projections for more than half of their products.



New Reality #1
If we build something people will buy, we'll make money.

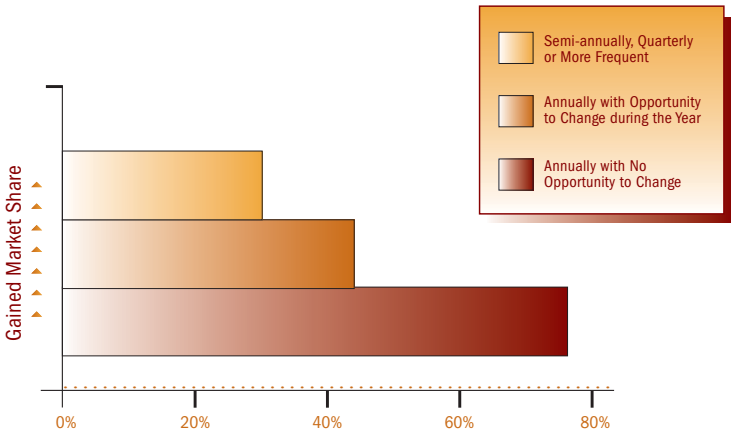
Merits of Flexible Strategy

Internet Time Belief #2
Success is dependent upon a constantly evolving business model.

This belief says that it is better to start with a nucleus of an idea and let it evolve while developing the product or company. Perhaps this is the belief in iteration taken to the extreme. Or perhaps it reflects a belief that competition for funding was greater than the competition for customers.

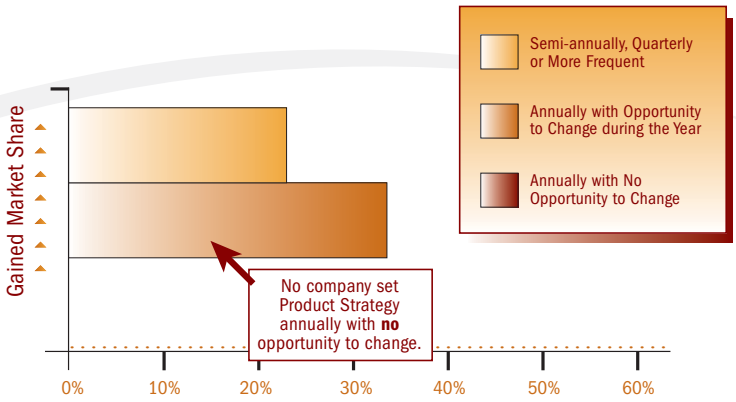
Corporate Strategy

Our research showed that the less often companies changed their strategy, the more likely they were to be successful. Those companies that set corporate strategy annually with no changes or annually with an opportunity to revisit it during the year were more likely to gain incremental market share. They were also more likely to introduce products faster, and meet or exceed their revenue projections for more than half of the products introduced.



Product Strategy

In all cases, product strategy is set on a more frequent basis than corporate strategy. No respondents set their product strategy annually with no opportunity for change. Those companies that set their product strategy annually but remain open to adjustments during the year fared much better than companies that change their product strategy more frequently. These companies were significantly more likely to gain incremental market share, as well as introduce products faster.



In comparing these companies' levels of change today to their levels of change in the past, we found some interesting results.

More than 50% of those companies surveyed changed their strategy more often than in the previous year with poor results. Over 30% of those companies that changed their strategy more often actually lost revenues – either a result of changing focus or a weak focus in need of a change – compared to 1% of all others.

The companies that changed less often or about the same as in the past enjoyed faster time to market and incremental market share gains. The companies that experienced less change were more likely to meet or exceed their revenue projections for more than half of their products. Perhaps we can surmise that this situation resulted from having a better strategy or business model to begin with, and thus not wasting time reevaluating their model.

New Reality #2

Success is dependent on a business model with well-designed stable corporate and product strategies.

The Myth of "First-To-Market Advantage"

Internet Time Belief #3

Being first to market is everything!

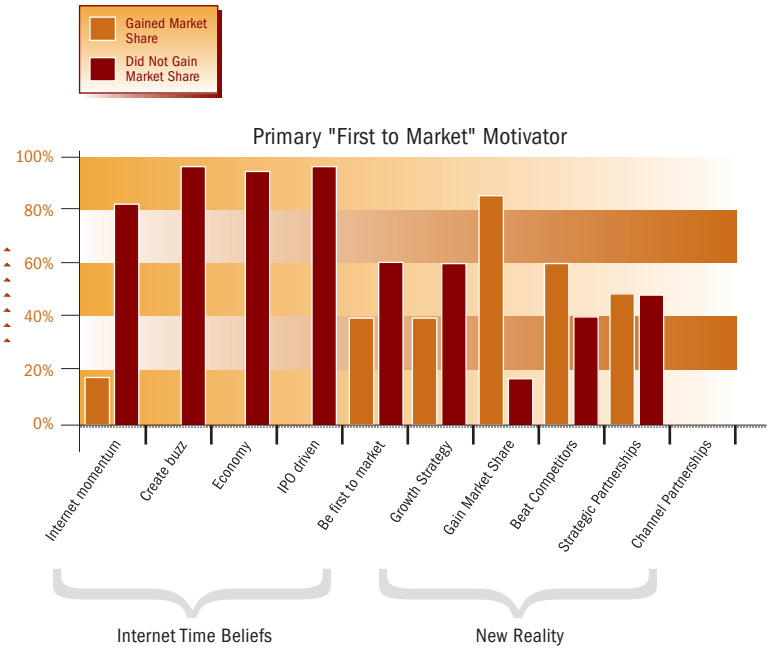
Common wisdom from strategy literature suggests that companies that are first to market have higher returns if they are successful. On the other hand, you often hear cliches such as "the first to market is the first to fail" and "the pioneer is the one with the arrows in the back." This belief often drove companies to speed up their product development process, in some cases for all the wrong reasons.

Companies were asked what their primary motivator was to introduce products faster. Key motivators for companies that introduced products faster, succeeded, and were financially rewarded were:

- Gain more market share
- Beat competitors to market

Key motivators for companies that aspired to introduce products faster and failed were:

- Create buzz
- Response to Internet momentum
- Just to "be first to market"



Companies that succeeded in introducing products faster were twice as likely to gain incremental market share, but somewhat less likely to meet their revenue projections for more than half of their products. None of the companies that met or exceeded their revenue projections for more than half of their products had "be first to market" as a primary motivator for introducing products faster. As a sole strategy driver, "be first to market" does not appear to drive success.

Companies that were not successful in introducing products faster, were more likely to:

- Have a history of changing corporate and product strategy more frequently
- Make funding decisions based on a political organizational structure
- Experience smaller percentage revenue growth

Companies that were the most successful in getting products to market faster also had the most attractive competitive environment. They had enough competition to define the market, but not so competitive as to make it expensive for a company to enter the market or be confusing for the customer. What is often overlooked in the drive to be first to market is the cost of educating your marketplace about the benefits and trade-offs of the new product or category. Introducing a well-differentiated product later can often speed time-to-market since you are entering an educated market.

New Reality #3

The "Be first to market" strategy ***does not*** ensure success. Having a clear strategy for which products to introduce and when, given your competitive environment, ***does***.

The Role of Process in Product Development

Internet Time Belief #4

Market success depends upon rapid iteration rather than formal process.

We tested two schools of thought about commonly used "processes" for developing new products:

The Internet Economy approach:
"We rapidly prototype, iterate often, and design robust architecture later."

The more traditional approach:
"We define thorough requirements first, build interdepartmental consensus, and then build out a robust architecture and a comprehensive solution."

Respondents were asked to rank their product development process on a scale of 1 for rapid prototyping to 7 for process-intensive. Results from this question clearly show two distinct clusters: one at the rapid prototyping end with answers of 1 and 2, and the other just past midway at 4, 5, and 6. While those who rapidly prototype were more likely to be on the extreme end of the prototyping cluster with a rating of 1, next to no one rated themselves 7, process-intensive, on this scale. It seems clear that few companies are following a highly formal process; most are moving toward faster, more iterative development.

Which process fares best, rapid prototyping or thorough definition? Both camps fared about the same, although the "Define Thoroughly" cluster was much more likely to meet or exceed revenue projections for more than half of their products. It appears that process choice is more a matter of culture or life cycle stage of the company.

	Rapid Prototype	Define Thoroughly
Total	46%	54%
Introduced products faster	38%	45%
Experienced incremental market share	38%	32%
Met or exceeded revenue projections*	21%	32%

*for more than half of their products

Not only are processes being compressed, but also many shortcuts are being taken in the product development process. It would appear from the data that important portfolio management steps are missing in the new product development process.

- **More than 80% do not include pipeline screening,** a process to manage the finite development resources of a company to ensure that they are not over-allocated.
- **More than 72% do not include risk management,** which optimizes the product portfolio for the highest rate of return for acceptable levels of risk.
- **Nearly 65% do not include cost benefit analysis or customer segmentation analysis,** which make trade-offs in feasibility of products, features, or customer segments for the highest financial return.

It appears for most companies that the product development cycle has evolved from a lengthy sequential process to a more concurrent, highly flexible process. Both approaches, however, would benefit from incorporating more robust portfolio management into their processes to help achieve their profitability goals.

New Reality #4

Rapid iteration and formal product development processes are equally viable methodologies.

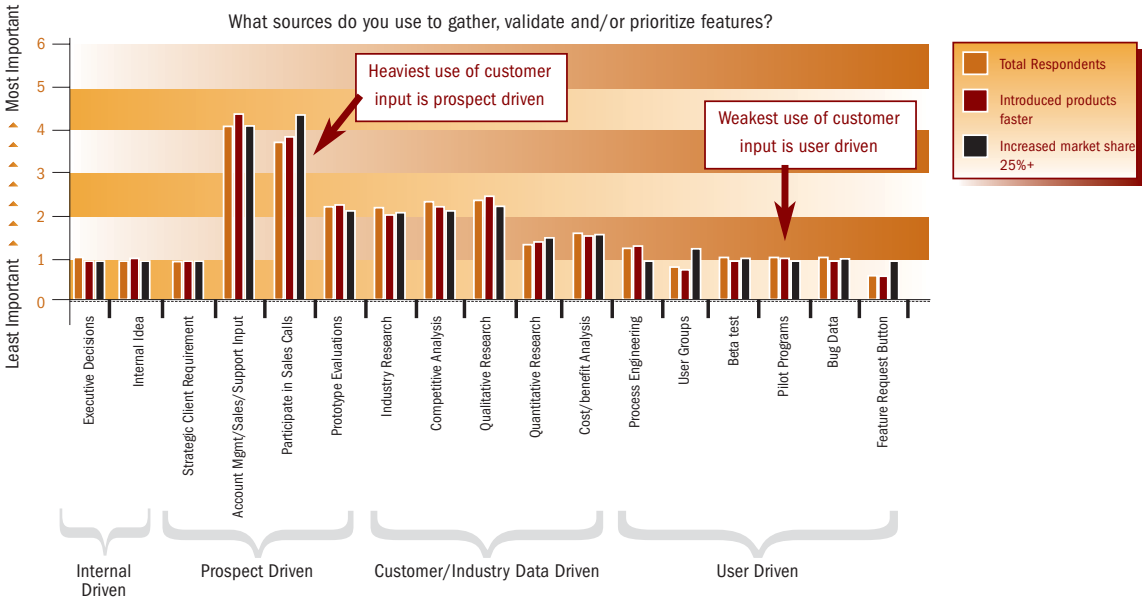
The Role of Process in Product Development

Internet Time Belief #5

Innovation comes from within, not from customers.

Many founders of young companies believe their product category is so new that customers can't understand it, let alone identify innovations for their product. Engineering-driven companies, both small and large, believe that it is only as a result of a deep understanding of a particular technology that break-through ideas can occur. This belief may be driving the limited application and use of customer input that we discovered in our research.

Earlier we noted that 28% of study participants were "more customer focused" than they were 18 months ago.



Interestingly enough, participants are only marginally more likely to use traditional market research, especially focus groups, today than they were 18 months ago. It's hard to tap customers for breakthrough ideas if you don't talk to them.

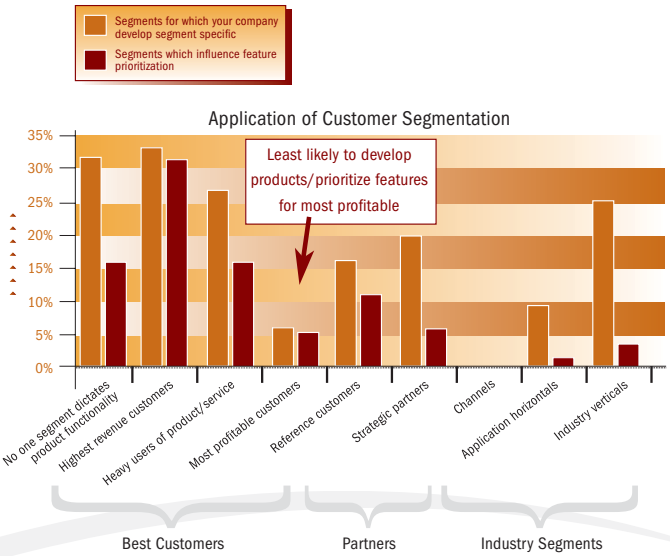
Yet the companies that talked to their customers showed a rather attractive success rate. The techniques used by the companies that were the most successful – as measured by increased market share and faster time to market – include participating in sales calls, mining customer wants and needs from customer-facing employees, employing focus groups and other qualitative research, and performing competitive analysis.

Gathering customer wants and needs through the sales process contributed significantly to increased market share. The most highly rated method of acquiring customer input was from talking to customer-facing employees. That is a good low-cost proxy for the customer, but not the customer. Interestingly, larger companies use this method most heavily, whereas earlier stage companies were more likely to use qualitative research.

What is notable from this research is how little validation of the product requirements is done by paying customers. We observed low usage of any sort of trial mechanism by the respondents; the use of pilot programs, beta tests, product bug data, and feature request buttons to collect feedback from paying customers was extremely limited. Asking people to evaluate products early in the sales process is clearly useful, but misses important insights that only come from talking to paying customers or those who are about to pay. Companies still need to validate their execution during, or after, the "buy" decision.

Customer segmentation has little influence over the product development process. Over 80% of companies do not let a customer segment dictate product functionality and almost 70% do not develop segment-specific products. Yet for the companies who achieved 50-100% revenue growth, over 60% developed segment-specific products. Nearly 85% used a customer segment to help prioritize feature development. Clearly customer segmentation positively affects top line revenue growth.

The following segments are untapped areas for product line extensions. The table below shows the percentage of companies that use these segments to drive their requirements process.



Overall, our research shows a rather amazing under-utilization of techniques to acquire customer input. Some of this lack may be driven by tighter budgets during the recession. Previously, it was mostly likely driven by a belief that product development cycle time had to be reduced at the expense of gathering customer input. The results of this research suggest there is not a big payoff in going so fast that you don't invest the time to capture customer wants and needs.

New Reality #5

Customers can help drive innovation - all you have to do is ask, listen and interpret. More importantly, listening to what customers want, gives you the most profitable ideas.

Summarizing the New Philosophy for Product Development

New Reality #1

If we build something people will buy, we'll make money.

New Reality #2

Success is dependent on a business model with well-designed, stable corporate and product strategies.

New Reality #3

The "be first to market" strategy ***does not*** drive success. Having a clear strategy for how to introduce products faster, given your competitive environment, ***does***.

New Reality #4

Rapid iteration and formal product development processes are equally viable methodologies.

New Reality #5

Customers can help drive innovation - all you have to do is ask, listen and interpret. More importantly, listening to what customers want, gives you the most profitable ideas.

Shortcuts that make sense

What shortcuts did companies take to get to market faster? The shortcut used most frequently - 43% of respondents - was reducing the feature set to lesson development efforts. Only one third of those respondents, however, gained incremental market share and met or exceeded their revenue projections for more than half of their products. Reducing the feature set was used most successfully by companies who had little or no competition.

Shortcuts used by companies that introduced products faster and gained incremental market share were, in order of frequency:

- Increased engineering resources to meet major milestones
- Implemented use of product development life cycle software tools
- Increased marketing research efforts
- Acquired companies or product lines
- Improved internal processes
- Used off-the-shelf software
- Out-sourced development

Interestingly, some of the "shortcuts" used to introduce products faster actually require more time. By putting more process or tools into place, companies ultimately reduced their time to market.

What's Old is New Again, Almost

The "New Realities" seem quite familiar, as does the latest mantra we hear in the press about "back to basics." What comes after "Internet Time" is the recognition that the window of opportunity to gain market share is wider for companies that plan well and execute effectively. Yet pressure to further compress the product development cycle shows no sign of abating.

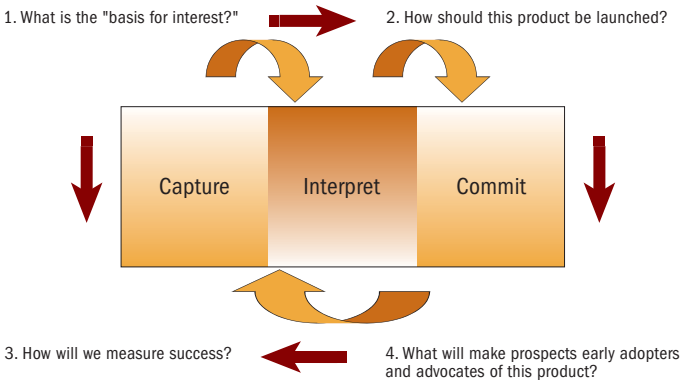
Vision & Execution offers a prescription for compressing the product development process without compromising the opportunity to capture important customer input and other relevant decision-making data. In other words, we offer a "formal" Rapid Iteration process.

The traditional formal product development process was created by Dr. Robert G. Cooper. His classic Stage Gate™ process is comprised of five stages or decision points. Each stage requires a "go/no go" decision by key stakeholders with responsibility for portfolio management.

1. Idea Screen - Preliminary Investigation
2. Second Screen - Detailed Investigation
3. Development
4. Testing & Validation
5. Launch

The Stage Gate process is a consensus driven formal process designed to funnel down the number of projects to which a company devotes it resources.

Vision & Execution has designed a simpler process tailored to meet the needs of smaller companies with one or few products in the pipeline. Rather than steering committee driven "go/no go" decision points, Vision & Execution offers pragmatic decision trees that can be used by management and/or small teams to evaluate their progress. Vision & Execution's approach compresses many of the customer data gathering events of the first three phases of a classic Stage Gate process into two phases.



Vision & Execution uses both "top-down" and "bottoms-up" analysis to help drive the product development process. Both approaches provide an effective analysis structure to better understand the sensitivity of the market opportunity including assumptions such as:

- Market size (rollout and market penetration assumptions)
- Product usage
- Potential
- Operating costs
- Pricing strategies

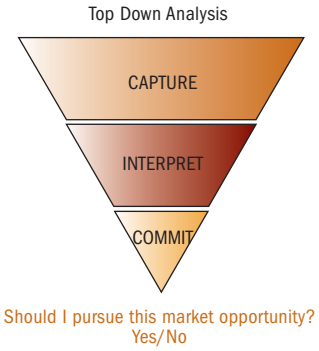
Vision & Execution uses "top-down" analysis to answer the first question, is there a "basis for interest?" "Top-Down" analysis quickly creates an expected financial picture from a high-level set of assumptions about the product category enabling a powerful understanding of generic economic sensitivities in a very short timeframe. Vision & Execution then places an emphasis on "bottoms-up" analysis using an extensive array of customer and industry data to inform the decision-making process for the remainder of the steps. "Bottoms-Up" analysis helps develop a much deeper understanding of the business as a whole. An extremely detailed assumption set makes it a valuable process for discovering where the greatest leverage resides in a particular business model.

Within each phase of the process there are three important steps: Capture, Interpret and Commit. The first step speaks to the need to capture relevant data and/or perform analysis to inform the decision-making process. The second step involves interpreting the data to identify new insights about the opportunity and advance the company's position. Implications from the current round of data capture and interpretation should be used to drive what is tested in the next phase. Last, is the step to commit resources to the next round of testing the new business or product opportunity. After completing all four phases of this process, the process begins anew, reevaluating the basis for interest.

1. What is the basis for interest?

Capture

- Industry research
- Qualitative research
- Competitive research
- Financial analysis
- Risk assessment



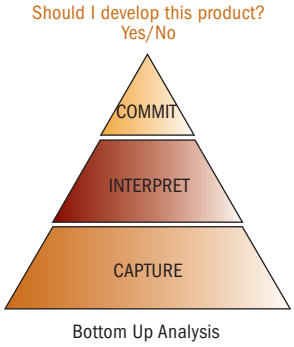
Interpret

- What is the ***basis for interest?***
  - How big is this market?
  - Who will buy this product?
  - Why will they buy my product?
- Implications for what to develop and how to launch this product.

2. How should this product be developed and launched?

Capture

- Sales calls
- Prototype reviews
- Technical feasibility
- Cost/benefit analysis



Interpret

- How should this product be developed and launched?
  - What is the USP and product positioning?
  - What features/benefits will drive trial?
  - How do customers want to learn about this product?
  - How do customers want to buy this product?
- Implications for how to attract early adopters and advocates for this product

Commit

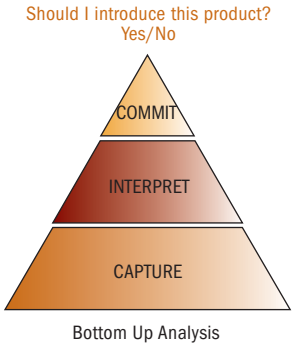
3. What will create early adopters & advocates?

Capture

- QA/Bug tracking
- Beta Test/Pilot Programs

Interpret

- What will make customers buy and promote this product?
  - Do the features perform as promised?
  - Does the product build trust/credibility?
  - Does the product deliver on the value proposition?
- Implications for how to measure the success of this product

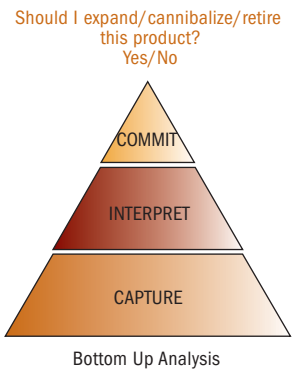


Commit

4. How will we measure success?

Capture

- Feature request button
- Quantitative research/ Customer Sat.
- User groups
- ROI/other financial analysis



Interpret

- How will we measure success?
  - Profitability
  - Customer Satisfaction
  - Brand equity
- Implications for new features or product line extensions or new markets

Commit

Appendix: Research Background

Vision & Execution created a web-based survey to gather input from product development professionals at both staff and executive levels.

We sent invitations to 879 people.

- 232 people (all currently on the NorCal Product Development & Management Association (PDMA) e-mail list)
- 319 people (all currently on the Silicon Valley Product Marketing Association (SVPMA) e-mail list)
- 328 people from start-up companies that each received $20 million or more in funding within the last 12 months

The survey was fielded from December 6, 2001 to January 14, 2002. We sent reminders on December 12, 2001 and on January 2, 2002.

We had a response rate of 90 respondents (10%).

- 24 respondents from SVPMA
- 24 respondents from NorCal PDMA
- 42 respondents from companies that each received $20M or more in funding in last 12 months

Contact

For a free consultation about how you can improve your product development process while reducing your time to market, please contact Patrina Mack, Managing Director of Vision & Execution at 650 233 0256.

This industry survey was sponsored by

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Vision & Execution is a marketing consulting firm that specializes in helping launch new companies and products. We are experts in identifying the optimal target markets for maximum revenue opportunity and prioritizing feature sets for rapid product launch. We frequently identify design partners, beta sites and/or reference customers to facilitate product design and roll-out. Vision & Execution through its partners can put together virtual marketing teams to take you all the way through product roll-out - from PR to trade show launches.

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