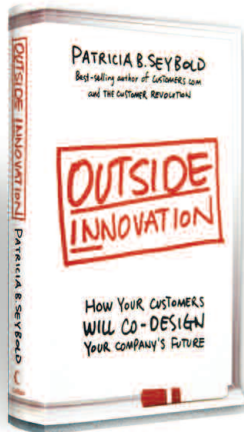




Executive Book Summaries®



By Patricia B. Seybold

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OUTSIDE INNOVATION

THE SUMMARY IN BRIEF

The Customer Revolution is in full swing. Customers have taken control. Their rampant comparison shopping is eroding your margins. Their renegade behavior is challenging your business models and endangering your intellectual property. Their demanding expectations for customized products, wonderful experiences and high service levels are draining your resources. Customers' insistence on open access is exposing your industry's policies and challenging your inflexible business processes.

Innovation is a form of creation. Like any creative endeavor, innovation emerges from the structural tension between current reality — the way things are — and a vision of what we'd like to achieve. The discrepancy between what customers can do today and what they ideally want to be able to do is the structural tension that spawns innovation.

Outside innovation is a process of engaging directly with lead users and passionate customers to harness and commercialize their ideas and to co-design solutions that will better meet their needs. Many companies already do this. What's new is the exponential growth in the ratio of outside innovation to inside innovation in many industries.

What can you do to channel this customer energy into a positive direction — one that will power your business rather than sink it? Here's the answer: Engage your customers in more ways to help you redesign your business, your products, your processes and your business models.

This summary will discuss the essential outlook that an organization must hold if it wants to be successful in fostering customer-led innovation. In addition, you will learn:

- ✓ *The keys to unleashing customer innovation.*
- ✓ *The roles that you should enlist your customers to play in your organization.*
- ✓ *How to begin building a customer-centric culture in your organization.*
- ✓ *The benefits of promoting and leveraging open source development.*

OUTSIDE INNOVATION

by Patricia B. Seybold

— THE COMPLETE SUMMARY

Outside Innovation Versus Traditional Innovation

There's an underlying assumption that drives traditional innovation: "Our experts are smarter than our customers." While it is certainly true that your company probably has deep subject-matter expertise in a certain domain, it's also true that your customers are subject-matter experts in their own right.

Traditional *inside out* approaches to innovation assume that subject-matter experts invent and design innovative new products to meet needs that customers may not realize they have. Then marketing and advertising departments make prospective customers aware of those needs, wrap a brand experience around the products, package and price those offerings and bring them to the market.

The *outside in* approach is to flip the innovation process around and assume that customers have outcomes they want to achieve, they have a deep knowledge about their own circumstances and contexts, and they are not happy with the way they have to do things today.

Customers will innovate — with or without your help — to create better ways to do things or to design products and services that meet their specific needs. If you want to harness the power of customers' organic creativity, you need to support their creative processes with tools, resources and imagination. ■

How to Harness Customer Innovation

How do you figure out what customers really want, need and will pay for? This is the fundamental question for any business. You must design solutions to help customers accomplish their desired outcomes or *Customer Scenarios*®. When designing these solutions, you must take into consideration the customers' context, the "job" they need to do (the Customer Scenario), their desired outcomes and their constraints or "conditions of satisfaction."

This concept of the Customer Scenario is subtly different from traditional customer segmentation and needs analysis. It's not enough to identify a group of customers who have certain things in common; you also need to know what

scenarios these customers actually care about accomplishing. *What outcomes are they trying to achieve?*

The Relationship Between Customer Scenarios and Innovation

Innovation occurs naturally as a result of the structural or creative tension between what you ideally want and what you currently have.

The keys to unleashing customer innovation are:

1. Find and commercialize the innovations of lead users who are already closing the gap between how they do things today and what they'd ideally like to be able to do.
2. Engage with your most creative yet grounded customers — your lead customers — and work with them to achieve their ideal outcomes.
3. Empower your lead customers with co-design tools and innovation toolkits so they can design their own solutions, innovating as they go.

In all three approaches, the discrepancy between what customers can do today and what they ideally want to be able to do is the structural tension that spawns innovation.

Adopting a Customer Outcome-Focused Approach to Business Design

When you take the outside innovation approach to business, you start by developing a deep understanding of your

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How to Harness Customer Innovation

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customers: the particular audience you are serving. At the core of that understanding is an appreciation of what they want and need to accomplish — their *ideal scenarios*.

As you and your customers work together to close the gap between their ideal scenarios and their current ways of doing things, you'll be co-designing new products, new business processes and new business models. That engine of customer-driven innovation powers your business, generating organic growth.

The ideal experience that customers want to have during their scenarios becomes your *brand experience*. The desired brand experience may be different for different customer audience/customer scenario combinations. Whether your firm takes a single brand or multi-brand approach, the brand experience should be optimized for each customer audience and scenario combination.

Products should not be the focal point of your company. They aren't your customers' focal point. Customers care about the "jobs" they need to get done. They are happy to use tools and to buy and consume services that help them accomplish their scenarios. The solutions that customers need and value will change over time.

Natural Behaviors You Can Tap to Unleash Customer Innovation

You'll find that customers and users play many roles in and around your business. Your goal should be to empower your most thoughtful customers to play as many of these roles as they can and as are appropriate for them. That way, passionate customers will intersect with people in many different parts of your business.

You can measure how well you're doing in harnessing customer innovation by counting the number of roles customers are playing in co-designing your business. You can gauge your process in cultural transformation by noting how many of your employees and how many departments are engaging with customers in these various roles.

The five distinct customer roles are as follows:

1. Lead Customers innovate without being asked. Often, they aren't paying customers — yet. But whether these people pay for your products, or whether they are even using your products to create something new and amazing, they are thoughtful and passionate about the outcomes they want to achieve.

Lead users and lead customers are the people who will design your next-generation products or business model. Watch them, support them and commercialize their inventions. Engage them in co-design activities. Give them innovation toolkits that enable them to extend, modify and/or redesign your products and

services. Then watch what they do and profit from it.

2. Contributors are happy to donate their work for the benefit of others. They innovate within your company's guidelines and provide value to your company by doing so. For example, contributors may create software or music or designs and offer their creations freely to others. They contribute their time as debuggers and testers of new products and concepts. They enjoy seeing their contributions and ideas used.

3. Consultants provide deep subject-matter expertise and offer valuable guidance and insights. Customer consultants serve on committees and design teams, validate marketing strategies and become advisory board members — all the time working with your employees on new ideas. Invite them to become part of your company. They'll analyze trade-offs, help you prioritize goals and recommend winning approaches.

4. Guides act as advisors to other customers, solving problems, offering insights and, most importantly, often creating "maps" that will help customers navigate complicated product lines or will explain relationships between complex concepts. Guides classify, filter, organize and review alternatives. They help others make sense out of confusion and add value by creating new knowledge.

5. Promoters are enthusiastic about your brand and your products. They are happy to spread the word and come up with innovative ideas about how to attract and delight other customers. They can help shorten time to adoption and may sell and/or promote your wares. ■

For additional information on lead users/lead customers, go to: <http://my.summary.com>

Powered by Customers' Inventiveness

The Lego Group is one of the world's largest toy manufacturers and is the largest in construction toys. It is estimated that the world's children spend five billion hours a year playing with Lego bricks.

Lego is making a comeback after some missteps. Engaging customers as co-designers and consultants has been part of the secret of Lego's success, in particular with regard to the development and implementation of its Mindstorms® product line, which enables families (children and parents), educators and hackers/hobbyists to build and manipulate robots.

Lego Mindstorms has been the company's most popular product for more than eight years. The new version, Mindstorms NXT, is forecast to be a best seller.

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Powered By Customers' Inventiveness

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How Lego Harnessed Customer Innovation

The Lego Mindstorms story provides a classic “how-to” for harnessing customer innovation. The company identified and sponsored lead users who were inventing new capabilities such as intelligent bricks and robotics software for kids, and later commercialized their inventions. Then, Lego commissioned one of these lead users/customers to develop the robotics software needed for the educational market.

The next step for the toymaker was to continue working closely with these lead users and end customers — teachers and students — as they took the commercial product (Lego Mindstorms) into the market. Lego also quickly identified an emerging and unexpected audience in adult hobbyists, who also enjoyed the product.

Lego executives tracked Internet Usenet groups and online discussions to monitor what lead customers cared about, then made the move to sponsor Lego's own online community, luring lead customers to join the

Lego-sponsored community. The company's executives watched lead customers hack its products, and embraced and encouraged their creativity.

Following these steps, Lego sponsored competitions for innovative use of its products by customers — kids, teachers and hobbyists — to identify new product possibilities, generate excitement among the community and create awareness in the market.

The company also listened to its lead customer and decided to partner with a like-minded technology provider — National Instruments — for the software needed to drive its next-generation product, eliminating the “not invented here” mindset.

Lego recruited lead customers as consultants to co-design its next-generation product, selecting beta testers who would both promote and enhance the new products from among its lead customer base. Lego then provided customers with an open toolkit to extend the product's capabilities. ■

Lessons From Lego

Lego has thrived because the company embraced the ongoing customer community that sprang up independently around it. Now, customers are collaborating with Lego in its product design. Here are some best practices that may apply to your business:

- Watch lead users carefully. Sponsor their research with your products. Be ready to commercialize their great ideas.
- Listen carefully to what customers are trying to do with your products, and let them know you're listening.
- Identify and appreciate your different customer audiences. Gain a deep understanding of what those customers are trying to accomplish and make sure that you are supporting them in achieving their desired outcomes.
- Establish and nurture customer communities.
- Give users the tools, information and capabilities they need to extend your products.
- Be willing to relinquish control and follow where customers lead.
- Engage lead customers to co-design your products.
- Sponsor activities that enable customers to gain recognition and respect from their peers.
- Encourage your customers to be your voice in the market.

Help Customers Reach Their Goals

Whether you're launching a start-up company or redesigning your business to be more customer-centric, the basic principles are the same. No matter how far along you think your organization is “outside in,” the following six design principles are essential for success.

Engage in Customer Research and Ethnography

Customer-centric businesses are not content to simply survey customers or run focus groups. Instead, they study how target customers do things *in situ*. They engage with customers in deep dialog and listening. They run discovery sessions with groups of customers, in which customers reveal their deep feelings — both negative and positive. They observe what customers are doing. They don't ask customers, “What do you want from us?” They ask, “What are you trying to do?”

Bathe Your Organization in Customer Knowledge

Customer-centric firms do not confine customer research to their market research organizations. Instead, lots of people from many different departments participate in these “deep dives” into customer context. One trend that makes this dissemination of customer knowledge easier is online customer communities.

Customer communities form the heart and soul of the company. Many customer-centric companies establish and maintain private online user communities. The customers in these communities become virtual members of the company's own cross-functional product development and marketing organizations. People from all over the

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Help Customers Reach Their Goals

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company “listen in” on these customers’ dialogues and ask questions.

Discover What Customers Care About Most

The purpose of ethnography and deep customer research is, of course, to understand what customers care about deeply. What outcomes are they trying to accomplish? This is completely different from asking customers what they like or don’t like about your current products and services.

You’re trying to understand what things in their own lives are hard for them to do. You’re seeking to learn which of these things they actually care about. In fact, the depth of passion (positive or negative) can be a good criterion in screening and recruiting lead customers to involve as customer consultants in your co-design activities.

Identify and Streamline Customer-Critical Scenarios

If you can identify what “job” customers are trying to do from their points of view, and clearly define (with the customers’ help) their desired outcome, their conditions of satisfaction and how they’d ideally like to achieve their goals, you now have a framework for customer-led innovation. By contrasting how customers do something today with how they’d ideally like to accomplish their desired outcomes, you’ll unleash many more creative ideas.

Engage Customers in Co-Designing

If you engage passionate customers in design activities, they’ll work with you to co-design their own ideal solutions. Customers can play a variety of roles, such as acting as guides, creating new product ideas and helping to create a market for a product or service.

Build Brand Identity and Customer Experience

Your brand is your customer experience. A customer-centric company’s brand-promises — and the customer experiences that are wrapped around those brand-promises — address the Customer Scenarios that its customers care about the most. ■

Let Customers Strut Their Stuff

Most people like to show off — to exhibit how smart and creative they are. A variety of organizations, from the venerable and staid American Institute of Physics to the new and sexy Flickr, have created thriving businesses out of content created completely by customers. Other companies, like Amazon and IgoUgo, complement and enhance their primary products with cus-

tomers-supplied reviews and ratings. The following are important design principles for customers creating content and acting as guides for others.

Give Customers a Role in Creating and Contributing Content

Many companies make their money by providing a place for “publishing” customers’ content. In fact, customers pay the American Institute of Physics for the privilege of having their articles published. Other companies, like IgoUgo and Amazon, enhance the value of their offerings with freely donated product reviews and recommendations. The people who contribute their opinions enjoy having this forum, and customers benefit greatly from this customer-supplied information.

Find Tools to Make It Easy and Safe to Create and Share Content

Almost a decade ago, Tripod recognized that not only do customers want to create and share content, they also need effective and easy-to-use tools to do so. The company, now owned by Lycos, offered the first tool for designing your own Web page.

Today, companies like Flickr (part of Yahoo!) have made it easy for photographers not only to post their pictures, but also to make their photos available to others. This involves tools to specify digital rights and categories, and to comment about their photos and others’. The result is an addictive Web site that has generated a creative community of contributors and fans.

Help Customers Find the Recognition They Crave

Humans are ego-driven, craving approval and accolades. Amazon recognizes this not only by giving people a mechanism for publishing product reviews, but also by encouraging feedback from those who rank the reviews. The American Institute of Physics has made it an honor for customers to be accepted for publication and makes it clear to the scientific community that the published articles are *the* authoritative research on the subjects.

Recruit Subject-Matter Experts to Build Expertise

The American Institute of Physics has created an editorial board that acts as a referee for the journal, vetting all submissions and thereby lending credence to their claim that published articles are the definitive research on the subject. Snap-on, a supplier of auto-repair tools and diagnostic systems, also relies on industry experts to vet its content.

Encourage Customers to Add Value to Your Content

Customer-provided reviews significantly add value to the customer experience on Web sites. Equally valuable is having customers categorize and “tag” content to

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Let Customers Strut Their Stuff

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make it easy to find and to ensure that the results are actually what other customers are looking for. Flickr allows customers to group and organize their photos in many different ways by allowing multiple tags to be assigned to each photo and adds even more value — and creativity — by allowing others to assign tags to one another's photos.

Pay Attention to New Trends in Customer-Provided Content

You never know where that next great idea for a business will come from. But a great way to start is by observing new or growing trends in people's behavior. The exploding growth of the blogosphere, and the human need to share ideas and get feedback on those ideas, proves that people want to strut their stuff and be recognized for their ideas and creativity. This free network of personalized viewpoints is impacting the world of journalism by offering new insights into world events, but also by potentially promulgating misinformation about the same events. For good or ill, this massive trend is something to watch to see how it might impact your company and your business model. ■

Promote and Leverage Open Source Development

The open source software development phenomenon has important lessons to offer anyone interested in harnessing the power of user-led innovation.

The Open Source Model Is a Creation-by-Customer-Community Model

Although the open source model can be said to have its roots in the hacker community and in the “free software” movement, it is really more about a group of people who care about creating an outcome that will benefit them and others than it is about who profits from the collaborative design and development efforts.

Unfortunately, the two concepts — open, as in open to inspect and extend, and free, as in cost-free to read, redistribute, modify and use — tend to overshadow the more profound breakthrough represented by the open source model: complex products that are co-created and evolved by a community of practitioners.

There are many people in many industries who are attempting to replicate the “success” of the open source software movement and/or to prevent a similar phenomenon from taking effect in their industries. The open source model is now spilling out into industries in which the final products are not digital in nature yet the

instructions or programs that describe the intellectual property are in digital form. For example, there are open source car design projects, open source biotechnology projects and open source industrial design projects, and there are bound to be many more.

There are useful lessons to be learned by watching the practices of open source development communities: These communities are structured, organized and sustained in order to create and maintain complex toolsets and products. These communities become the ecosystems of participating players. The toolsets and products that are created by each community tend to be used, in turn, to create additional products or specialized solutions. There is no question that these co-production communities generate value. How that value is monetized is a fascinating and complex topic, and the answers are likely to vary by industry.

Fundamental Design Principles for Open Source Projects

There are a number of repeating themes and principles that have arisen in the open source software world. Many of these principles may hold true as commons-based peer production models hit additional industries. Essentially, any product category that can be digitally designed — which includes most manufactured products and many bioengineered products — is a candidate for open source. The main design principles are as follows:

1. End users usually participate in open source projects because they intend to use the resulting product; sometimes they do it for the sheer pleasure or challenge.
2. Contributors believe in symmetry: They contribute and they benefit.
3. Clear governance (who makes the decisions?) and structure (what processes do we follow?) are critical for success.
4. Meritocracy prevails: Those who produce the best work gain the most status and clout.
5. Visibility — of the source code, of the work in process, and into the decision-making process — is critical to success.
6. Few people actually design and build; many people improve, debug and test; many more provide support, offer suggestions and promote.
7. Intellectual property “belongs” to the community, with various licensing and business models available for creating open or closed derivative works.
8. Open software does not have to be free to procure. It does have to be visible to examine and extend. It must be able to be redistributed to others.
9. Successful open source projects generate surround-

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Promote and Leverage Open Source Development

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ing ecosystems. They are magnets for continuing innovation. ■

For additional information on open source development and commons-based peer production, go to: <http://my.summary.com>

Enabling Customer Co-Design

There are a number of different kinds of customer co-design tools that you may find of value in working with lead users (advanced users who aren't yet customers) and lead customers.

The purpose of offering co-design tools is to make it easy for customers to design their own ideal solutions by leveraging your domain knowledge, and to learn what's possible as they do so. By giving customers design tools, you shortcut the laborious and lengthy hand-offs between the customers and the producer.

Empower Your Customers

By empowering your customers to create their own solutions through the use of co-design tools, you transfer to your customers the hard part of the problem — specifying exactly what it is they want and need. Design tools allow customers to iterate many times before they hand their design to you to produce for them (often with the click of a button).

In the case of an electronic or digital solution, the final assembly and delivery may be virtually instantaneous. If the product is a physical one, the lag time from design to production typically varies from hours to days or weeks. The co-design tools you offer your customers provide a mechanism to “open up” your proprietary expertise without exposing your intellectual property or compromising the deep domain knowledge on which your business is based.

There's a wide range of end-user toolkits — software tools, manual tools and tools for the mind — and they all have one purpose: to empower the end user or customer to envision and create their own ideal solution. Some of these tools are fairly constrained. They empower customers to customize or configure a solution to meet their needs. Others are more open-ended — they provide a springboard for true creativity and innovation.

Customer Scenario Mapping — A Tool to Enable Customer Innovation

The Customer Scenario approach is designed to identify your customers' ideal scenarios and to help you engage directly with those customers. Customer

Customization, Configuration and Build-to-Order Tools

Tools that enable customers to configure or customize their own solutions include:

- **Configurators:** Configurators are usually interactive software programs that enable the user to custom design a solution. Customers can try out different combinations and permutations until they find the optimal solution based on the constraints.

- **DIY Construction Kits:** You can provide customers with a set of parts and steps they can use for do-it-yourself projects. Customers' options are constrained based on the components/ingredients that they have selected and/or that the supplier provides. Either the customer performs both the customization and production of the final solution or the customer uses the kit to produce a prototype or mock-up that is then sent back for actual testing and production. In addition, DIY kits do not have to be collections of physical ingredients; also, they may include customer-created components.

- **DIY Workshops:** There are businesses built to support the do-it-yourself urge found in people of all ages. Build-A-Bear Workshop is a great example of a retailer that built a healthy business providing DIY workshops: Customers come to the stores to custom-build their own stuffed animals.

Scenario Mapping will enable your customers to co-design new ways that your firm and your partners can support them in achieving their goals in the way that works best for them, makes you money and streamlines your operations.

When you're willing to design or redesign your business around your customers' ideal scenarios — the outcomes they care about — you discover loads of opportunities for innovation.

Customer Co-Design Using Customer Scenarios

Typical customer co-design sessions involve up to 24 lead customers who break into four teams and, working together with your employees, map out four ideal scenarios — how they would ideally like to accomplish their goals and all the ways you could support them in doing so.

The core design elements of customer scenario design and mapping are:

- Design from the end customers' point of view.
- Recruit your lead customers to co-design with you.
- Involve multiple stakeholders from your organization to provide subject matter-expertise and to build a

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Enabling Customer Co-Design

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shared mental model.

- Map out the *ideal* state. Don't get bogged down in current reality.
- Capture customers' hot buttons and prioritized requirements for information resources, tools, services and technology enablers in a single session (all in the context of the things they care about the most).
- Identify the metrics that are crucial to your customers — what are their conditions of satisfaction, their moments of truth, and how do they measure them? Identify your business metrics — how will you increase profits, lower costs, reduce steps, shorten time and build customer retention and organic growth?
- Convey the results by telling the story of the map. The power of storytelling will “sell” the customers' vision to all who hear it. ■

Let Customers Co-Design and Promote Your Products

The number of businesses that are encouraging customers to play an active role in developing products, in co-designing their offerings and in actively promoting and building referral networks and ecosystems is increasing exponentially. Most (but not all) of them are young companies or newer companies.

Threadless: Selling Customers' Designs to Other Customers

What about letting customers compete to create the designs for the products you manufacture and sell? That formula has proven to be an extremely profitable one for Jake Nickell and Jacob deHart, founders of Threadless.com, a design-your-own T-shirt competition and retail Web site.

While there are many Web sites that let customers submit their designs for printing on T-shirts, mugs and posters, Threadless was one of the first to presume that customers wanted to strut their stuff by having their designs produced as commercial products that other customers could buy. Threadless was also one of the first design-your-own T-shirt sites to involve its customers in a design community, by having them vote on and comment upon each other's submissions.

What works so well about Threadless is that its customers, who are design-conscious people of all ages and from all over the world, value one-of-a-kind clothing designs. They don't want to be seen wearing mass-produced apparel. T-shirts have become a fashion statement. The cooler the shirt, the cooler the person.

So the Threadless business concept is to have a constant supply of unique, fresh designs and to produce a limited quantity of the designs that customers like the most. New designs keep these style-conscious consumers coming back for more.

In creating a T-shirt business where customers submit their own designs, which are then rated by other customers, Threadless' founders have perfected a customers-as-creators community business model. Customers' creations are acknowledged and rewarded. Customers maintain their own intellectual property and copyright, but Threadless produces and sells the designs.

Customers promote their wares, luring others to the community. The cost of goods sold is low. The profit margins are high. The overhead is in tending the community. ■

A Blueprint for Harnessing Customer-Led Innovation

Organizations that are successful in fostering and harnessing the results of customer innovation all have one thing in common: A large percentage of their employees at every level of the organization are deeply curious about what problems and issues their customers are trying to solve and what those customers' aspirations are.

The people in these organizations aren't just focused on developing, producing and delivering great products and great service. What they really love is to get into their customers' shoes, to view the world from their customers' perspectives and to appreciate what it is that each group of customers ideally wants to accomplish.

Customer-led innovation happens almost organically in organizations with this kind of culture. If everyone is focused on what their customers are trying to accomplish rather than their own internal business processes, it becomes natural to empower customers to invent new ways of achieving their outcomes. ■



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