Publication: The Business Times, p 11
Date: 20 May 2015
Headline: Incentives for motivating radical innovation - how to make it work?

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Incentives for motivating radical innovation – how to make it work?

While rewards and recognition are critical in encouraging a robust innovation culture, they can also backfire. Designing an optimal and strategic incentives system is key, says SMU Professor Thomas Menkhoff

AN important question for academics and business leaders is how best to motivate innovative behaviour in organisations. In one of my research studies on knowledge sharing behaviour in knowledge-intensive contexts, rewards and recognition turned out to be critical management tools to encourage employees to innovate.

But top management does not always see the need to incentivise to introduce actionable new ideas for many reasons, such as the belief that too many positive, tangible incentives might backfire.

And then there are corporates who go all out: tech firms empower their employees to award peer cash bonuses to innovative colleagues without approval (one's own team members excluded); banks motivate with special bonuses and long-term incentive awards, such as profit-sharing plans which sometimes outweigh their fixed remuneration components.

To avoid frustration among those who got too little or nothing, it is important to check whether the chosen approach leads to a robust innovation culture or the opposite: envy and disengagement.

Even the best intended practices can provide disincentives for the right (innovative) behaviour. The promise of tangible monetary rewards can erode one's intrinsic motivation which is critical for breakthrough innovations. The rise and fall of the dotcom bubble has been partly attributed to too much focus on downstream financial rewards.

Limiting the risks of failure inherent in innovation efforts requires specific skills to enable "those who did not deliver" to quickly bounce back without career setbacks.

Competitive innovation tournaments are no panacea for greater innovativeness if risk-averse leaders fail to implement newly proposed ideas.

Firms may forgo the chance to achieve great(er) performance outcomes unless people relentlessly innovate, driven by passion alone. Psychologists describe this as "a strong inclination towards a self-defining activity that one likes or loves, and in which one invests time and energy". The story of Steve Jobs suggests that such behaviour can be so self-defining that it represents a central feature of one's identity.

Most of us are not extremely self-motivated co-founders of multinational tech firms. Despite being dutiful and conscientious, we do need some carrots. If there is no outlet for our passion, or worse, if compensation is below market price, and driving new ideas is not recognised in one way or another, some people might look for better prospects elsewhere.

What does it take to create an organisational incentive framework that supports radical innovative behaviour? This is a key competency which we impart to our innovators enrolled in SMU's Master of Science in Innovation programme.

First, when designing an incentive framework to support innovativeness, managers need to appreciate the temporal distinction between two motivational tools:

- Incentives, such as funding or financial compensation, which kick in before an innovation project starts;
- Rewards, such as recognition in the form of publicly showcasing innovative employees, which are doled out after the interim results of the innovation effort have been achieved. This might then encourage people to continue to innovate, provided the right carrots are in place.

Second, incentive systems must specify and reinforce strategic and long-term innovation goals in order to achieve the desired corporate results. For instance, in contrast to incremental innovation, the goal posts of radical innovation projects such as SpaceX (founded in 2002 with the ultimate goal of enabling humans to live on Mars) are distinct but much less specific. This requires a unique reward management approach based on subjective metrics, such as attaining intermediate roadmap targets, rather than objective measures, such as speed to market or percentage of sales derived from "new" products.

> **'Innovation KPIs incorporated into a balanced innovation scorecard must leave enough room for trial and error, experimentation, exchange of ideas and learning.'**
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> **– Thomas Menkhoff, Professor of Organisational Behaviour and Human Resources at SMU Lee Kong Chian School of Business, and Academic Director of SMU's Master of Science in Innovation programme**

Initially, radical innovation projects have a very high level of uncertainty associated with high costs. CEOs keen to achieve greater product innovation are advised not to stifle risky new development initiatives and flexibility by prescribing narrow, specific business goals. The development of Logitech's IO Digital Pen, for example, has been attributed to broad goals set by former CEO Guerrino de Luca aimed at creating new last-inch products at the interface between human and technology.

Third, once formulated, innovation goals and exploration activities need to be integrated into the corporate performance measurement system. Innovation experts suggest coming up with stretch goals which inspire employees beyond a narrow project mentality in contrast to (potentially demotivating) measurable goals. Bill Gates' "a PC in every home" and Netflix CEO Reed Hastings' vision "to reach out to the five billion people on mobile" fall into this category.

Innovation KPIs incorporated into a balanced innovation scorecard must leave enough room for trial and error, experimentation, exchange of ideas and learning. If individual innovation efforts can be pinpointed and measured but remain unrecognised, personal effort will decrease.

Likewise, it is essential to reward collaborative value creation because the success of breakthrough products or services newly developed by one team often depends on other units. To ensure equity and to prevent social loafing, team-based performance measures, such as on time project completion, can be combined with individual performance evaluations, such as 360-degree feedback based on a holistic portfolio approach across several innovation projects, to measure efforts and outcomes over time.

According to Kenny Yap, executive chairman and managing director of Qian Hu Corporation Ltd, it is of utmost importance to prevent office politics in order to maintain a work environment conducive for innovative behaviour.

Team efforts can be rewarded through gain-sharing which links actual team-based rewards with the long-term value of innovation outcomes throughout a particular gain-sharing period. Sharing monetary savings (gains) from improved performance with employees, for example in the form of deferred bonuses, can potentially increase a sense of ownership.

Finally, the determinants of innovation measures and rewards are all contingent upon business model, profitability, and organisational culture. For CEOs and corporates, the challenge is to measure what is important for their businesses.

Rewards can take the form of "failure rewards" (for teams whose failures taught valuable lessons), "gamification-linked point systems" (aimed at incentivising great new ideas) or "long-term stock-based incentive systems" (deemed suitable by experts to drive radical innovation).

One interesting takeaway of recent strategic management research on rewarding innovation is this: rather than providing highly incentive-intensive rewards, such as financial compensation which is tied closely to the value that very few outstanding people have created (which leads to rivalry and potentially corrodes innovative behaviour), a better option might be to stimulate the process of value-creating ideation through a robust culture of innovative intrapreneurship, in conjunction with a weaker incentive intensity. This might then lead to many incremental innovations – and a few (albeit very valuable) radical ones as fresh drivers of more innovation breakthroughs.

This is a monthly series by the Singapore Management University. Next month's feature will discuss various challenges in mobile computing security.