

Value innovation and how to successfully incubate “blue ocean” initiatives

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“The creators of blue oceans, surprisingly, didn’t use the competition as their benchmark. Instead, they followed a different strategic logic that we call *value innovation*. . . instead of focusing on beating the competition, you focus on making the competition irrelevant by creating a leap in value for buyers and your company, thereby opening up new and uncontested market space.” – Kim and Mauborgne (2005)[1]

“In *Blue Ocean Shift*, people and our human spirit are put on an equal plane with a tested process and market-creating tools to move you, your team and your organization from red oceans in a way that people own and drive the process to succeed.” – Kim and Mauborgne (2017)[2]

The publication of Michael Porter’s *Competitive Strategy* in 1980 marked a watershed in the history of the strategy field, and the period since has been marked by the flowering of three major perspectives, each with its own set of tools and frameworks, which taken together have greatly advanced our capacity for strategic analysis and strategy development. Two of the three are “strategic positioning” (Porter) and “core competency” (C.K. Prahalad and Gary Hamel).[3] Both were primarily concerned with sustainable competitive advantage and how to develop it.[4]

Value innovation and its three main variants

The emergence of the third perspective, “value innovation,” is arguably the most exciting development in the strategy field in the last two decades. There have been at least three major variations on this theme to date: “blue ocean strategy” (Chan Kim and Renee Mauborgne), “disruptive innovation” (Clayton Christensen) and “value co-creation” (C.K. Prahalad and Venkat Ramaswamy).[5] The three share some common characteristics that distinguish the value innovation perspective from an approach that seeks to sustain an established position. These are:

- Viewing the basic strategy challenge as how to create and capture new demand.
- Shifting the primary emphasis in strategy development back onto the customer rather than the competition.
- Recognizing major new demand potential in current “non-consumption” and ways to overcome it.

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- Aiming for a “value breakthrough” (or leap in value), usually through business model innovation – changing the game.

Where:

$$\text{Value} = \frac{\text{Customer benefits}}{\text{Cost}}$$

The three approaches highlight somewhat different types of new market space opportunities. Blue ocean strategy tends to focus on value innovation that uncovers new aggregations of demand by redefining the category, like Cirque de Soleil – entertainment that merges circus and theater – while disruptive innovation tends to concentrate on new demand-creation that expands the current served market, like Southwest and Ryanair in low-price air travel. The third variation, value co-creation (or “experience innovation”) is aimed at creating new demand through transforming the user experience, offering “scalable personalization” through using ubiquitous, smart-connected technologies to convert traditional products into interactive, information-rich, engagement platforms, as Nike has done with its Nike+ smart wearables and LEGO with its robotic toys.

This masterclass examines the blue ocean variation, how it works in practice and how it has evolved since the publication of *Blue Ocean Strategy* (2005) by W. Chan Kim and Renee Mauborgne just over a decade ago.[6] The main resource will be their new book *Blue Ocean Shift* (2017).[7]

Blue and red oceans and the strategic logic of value innovation

In *Blue Ocean Strategy* (2005), Professors Kim and Mauborgne offered their concept of value innovation, an idea they were developing in the late 1990s. They contrasted it with the goal of sustainable competitive advantage, the prevailing “red ocean” model.

Red oceans are market spaces where competition is already well established and becoming increasingly “bloody” as competitors strategize for a greater share of existing demand. Industry boundaries are well defined and accepted and the competitive rules of the game are known. Competition revolves around a relatively narrow set of core product or service features, and competitors typically face a differentiation-cost trade-off.

In contrast, blue oceans are markets yet to be created, where significant new, uncontested demand can be unlocked by companies willing and able to pursue breakout “strategic moves.” In their original study, Kim and Mauborgne found that such moves had a number of common characteristics. They “didn’t use the competition as their benchmark,” but followed a “different strategy logic,” one that Kim and Mauborgne came to define as “value innovation.” Blue ocean strategy sets out to reconfigure value propositions in compelling new ways that can deliver a quantum leap beyond the current red ocean value-cost frontier through raising buyer value and lowering company costs simultaneously.[8] The emphasis on both value and innovation is essential to the creation of new “blue ocean” market spaces.[9]

Blue Ocean Strategy “laid out the conceptual differences and underlying patterns” that separate market-competing “red ocean” moves from market-creating “blue ocean” moves. Kim and Mauborgne also provided the main “analytical tools to create blue oceans.” These include:

- The Strategy Canvas and Value Curve
- The Four Actions Framework and ERRC Grid
- The Six Pathways to Reconstructing Market Boundaries
- The Pioneer-Migrator-Settler Map
- The Three Tiers of Noncustomers
- The Buyer-Utility Map
- The Three Characteristics of a Good Blue Ocean Strategy

Making a successful blue ocean shift

In the period since the publication of their classic, Kim and Mauborgne found the interest increasingly changing from “What is blue ocean strategy?” to “How do we actually apply its theory and tools to shift from red to blue oceans?” In their new book, *Blue Ocean Shift*, they crystallize the recipe into three main components:

- Adopting a blue ocean perspective – a major shift in mindset from “red ocean” to “blue ocean” strategic thinking, carefully avoiding the most common red ocean cognitive “traps.”^[10]
- A set of market-creating tools – essentially the tools introduced in *Blue Ocean Strategy* with further guidance on how to apply them as an integral part of a blue ocean “transformation journey.”
- Having a “humanistic process.”^[11]

The first two components are fairly self-evident, but the third merits further expansion. Kim and Mauborgne came to see that successful blue ocean shifts were also marked by a process that inherently “recognized people, acknowledging their fears, their insecurities, their need to be treated with dignity, their desire to matter.” Building such a humanistic dimension into the blue ocean transformation process can help the organization “to shift its team’s psychology and create an emotional landscape for change,” by “weaving” three humanistic elements “into the entire journey” – atomization, first hand discovery and fair process (See [Box 1](#) “The three humanistic elements”).

“Blue ocean strategy tends to focus on value innovation that uncovers new aggregations of demand by redefining the category . . . while disruptive innovation tends to concentrate on new demand-creation that expands the current served market.”

Box 1. The Three Humanistic Elements

Fair process. Its three major elements are:

- Engagement – “actively involving people in the strategic decisions that affect them.”
- Explanation – “providing people with a clear account of the thinking that underlies the process.”
- Reassuring people “that their opinions have been considered,” even if not finally adopted) and clear expectations – “stating clearly what people can expect, and what their roles and responsibilities are.”

Fair process helps foster mutual respect and trust, essential in building a collective willingness and capacity to take blue ocean risks. The touchstone of fair process is transparency.

First hand discovery. This is a process of enabling people to discover for themselves the need for change. It is intended to challenge team members’ understanding of what they believe to be true by bringing them “face-to-face with the market,” exposing them to “patterns that might have escaped them,” collecting “visceral insights” from the close study of customers and noncustomers alike, and building collective confidence, optimism and creativity within the blue ocean shift process.

Atomization. This practice breaks a seemingly big blue ocean shift challenge “down into small concrete steps,” where “each step pushes the boundaries of our thinking, but no one step overwhelms us,” and where “tangible evidence that creating new market space is possible” begins to accumulate, and people “feel their creative competence” progressively increase.

A systematic five-step process

In *Blue Ocean Shift* Kim and Mauborgne weave these three essential components into a systematic five-step process to help organizations to develop and execute successful new market-creation strategies. The five steps are:

- Getting started.
- Understanding where you are now.
- Imagining where you could be.
- Finding how to get there.
- Making your move (see [Figure 4-2](#)).

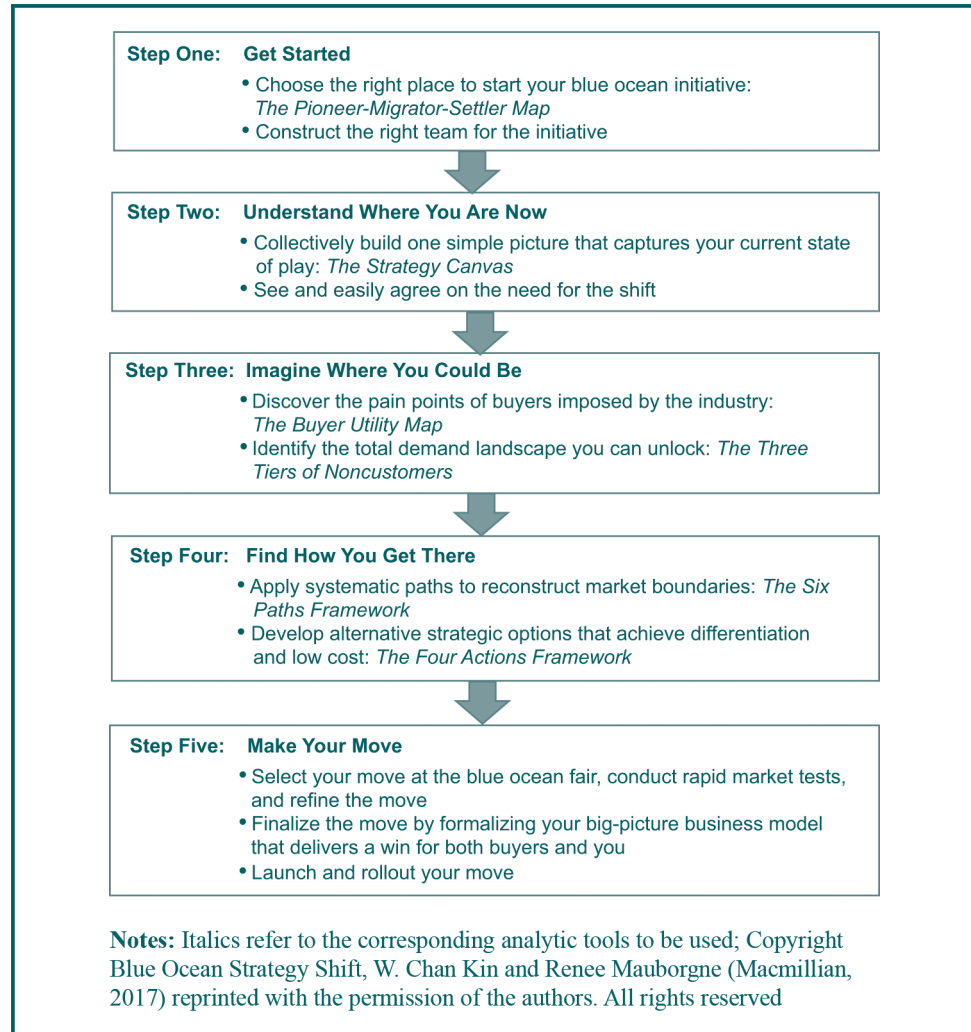
Step 1: Getting started

The two main tasks in Step 1 are:

- Choosing the right offering for your initial market-creating initiative.
- Forming the right blue ocean team to drive it.

The main tool to be used in this step is the “pioneer-migrator-settler map.”

Figure 4-2 Overview of the Blue Ocean shift process



The map is a visual tool designed to help companies profile their “current value innovation pipeline” and the potential for growth “inherent” in their existing portfolio. Pioneers are “value innovators,” migrators are “value improvers” and settlers are “value imitators.” In the case of settlers, changes to the appeal of their offerings are incremental, their strategy “converges with the rest of the industry” and their prospects are limited to the growth rate of the market. Pioneers offer “unprecedented value that opens up a new value-cost frontier” and are poised for “strong, profitable growth,” while migrators try to offer some value improvement, but it is not compelling and game-changing. In using the tool it is “crucial” to label each given offering from the point of view of the buyers, and how they would be likely to rate them “compared to the other offerings available to them in the market.”

The ultimate aim is not to move towards “a portfolio dominated by pioneers,” but to “create a healthy balance between today’s businesses – your settlers that provide cash and a measure of earnings stability – and the pioneers that are the growth engines for tomorrow.” A completed map shows “how strategically vulnerable or healthy” your portfolio really is, highlights the urgency with which a blue ocean pioneering move is needed and indicates which offerings to prioritize for blue ocean reinvention.

“If pain point identification is a bit slow in coming, Kim and Mauborgne suggest getting the team out to observe ‘what it means to experience your industry’s offering across the entire buyer experience cycle in the same way that ordinary people do.’”

In addition to targeting a particular offering for the organization’s initial blue ocean move, it is also crucial to choose the right team to drive the initiative. Experience suggests that a cross-functional team of the 10-15 members works best and that all of them should “be directly involved in the division or product/service offering you are aiming to shift.”^[12] The team should also have a proven leader capable of mobilizing wide organizational support for the initiative and navigating the team successfully through the organization’s decision-making structures and processes.

Step 2: Understand where you are now

The primary task in this step to help the organization achieve sufficient clarity “about the current state of play,” and the most useful tool supporting this task is an “as-is strategy canvas.” Editor’s note: Graphic representations of the *Blue Ocean Strategy Shift* models can be viewed at the authors’ website.

The strategy canvas is an analytical tool that will be useful “throughout the blue ocean shift journey.” It is a visual analytic that is designed to communicate a one-page visual of “the four key elements of strategy: the factors of competition, the offering level that buyers currently receive across these factors, and your own and your competitors’ strategic profiles and cost structures.”

Drawing up the “as-is” strategy canvas requires the team to specify on the horizontal axis the key factors that the industry’s players currently compete on and invest in. While managers “typically have a strong sense of how they and their rivals compete on one or two strategic dimensions,” they rarely have a “strong grasp of the full picture.” The vertical axis “captures the offering level buyers receive or experience” for each of an industry’s key competing factors.

To help them in assessing the current state of play, the blue ocean team should aim to identify between 5 and 12 factors in their development of the as-is strategy canvas.^[13] The as-is canvas should include the strategy profiles of the firm and its strongest competitor and no more than one or two others.

Completing the as-is strategy canvas provides the team with a “one-page picture” that captures “the current state of play, the assumptions the industry acts on and the degree of competitive convergence across existing players” and serves to build a “compelling objective case” for why, or why not, a blue ocean shift may be in order.” It also provides “a good baseline against which to evaluate new ideas.”

Step 3: Imagining where you could be

The two main tasks involved in this step are:

- Uncovering “the hidden pain points” that limit the size of your industry.
- Discovering “an ocean of noncustomers.”

The main blue ocean tools for helping with these two tasks are the “buyer utility map,” and the “three tiers of noncustomers.”

Most existing industries have hidden pain points, compromises or blocks to full utility for many existing and potential buyers that have long since become industry “blind spots” limiting the market from reaching its full potential. These often hold the key to releasing “trapped value” in the industry’s current value chain and unleashing new demand. Restricted retail or banking hours before the arrival of online shopping and banking is one of the most familiar examples.

The generic buyer utility map is a matrix with the “six stages of the buyer experience cycle” on the horizontal axis and the “six utility levers” on the vertical axis. The six stages of the buyer experience cycle are purchase, delivery, use, supplements, maintenance and disposal; and the six major utility levers are customer productivity, simplicity, convenience, risk reduction, fun & image and environmental friendliness. The standard version of the matrix “highlights 36 potential utility spaces” and companies in “commoditized red oceans” typically concentrate “on only a few, leaving the rest virtually wide-open for blue ocean possibilities where today only inadvertent pain points reside.” This is how French-based Groupe SEB found a new blue ocean opportunity in the commoditized market for domestic electric French fry appliances.[14]

Drawing and filling in this matrix is often when the team first comes to see “the real possibility of creating blue oceans.” If pain point identification is a bit slow in coming, Kim and Mauborgne suggest getting the team out to observe “what it means to experience your industry’s offering across the entire buyer experience cycle in the same way that ordinary people do.”[15]

When it comes to the second task, where the traditional view of the market might be “customer first,” the “blue ocean strategist’s mantra is noncustomers first,” and the blue ocean toolkit highlights three tiers of noncustomer each offering potential opportunity for creating significant new demand. The three tiers tool complements buyer utility mapping by helping to give the team more insight into the “the total demand landscape.”

The first tier is the “soon-to-be noncustomers,” customers currently “on the edge” of your industry that are most ready “to jump ship” once a “superior alternative” comes their way.[16] The second tier is the “refusing noncustomers,” potential customers that have “consciously thought about using your industry’s offering, but then rejected it” in favor of another industry offering that better meets their needs.[17] The third tier is the “unexplored noncustomers,” whose needs have always been assumed to belong to

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other industries or categories. For example many travelers chose intercity buses or trains before SouthWest Airlines offered competing routes. This third tier typically presents the biggest opportunity to create new demand.[18]

The overall aim of this analysis is to “get a rough sense” of how significant each of these tiers could be, if “unlocked,” and teams usually end up surprising themselves “by how much they agree on who the key groups of noncustomers are in each tier and the relative demand potential for each.”

Step 4: Finding how you get there

With the overall demand landscape more fully identified, Step 4 now shifts the process to “generating practical, real world, blue ocean options.” The two main tasks involved in this step are:

- Systematically reconstructing market boundaries.
- Developing alternative blue ocean opportunities.

The challenge in reconstructing market boundaries is the opposite of finer segmentation. It is looking for potential new aggregations of demand spanning traditional industry boundaries, strategic groupings or product/service categories that can open up new value-cost frontiers. Kim and Mauborgne developed their six paths framework “to demystify and structure the work of seeing opportunities where others see only red oceans of competition.”

The six paths are:

Path One: Look across alternative industries.

Path Two: Look across strategic groups within your industry.

Path Three: Look across the chain of buyers.

Path Four: Look across complementary product and services.

Path Five: Rethink the functional-emotional orientation of your industry.

Path Six: Participate in shaping external trends over time.

Two paths usually offer the biggest potential payoffs. Path One encourages the team to identify the needs its current offering solves, and then “to generate a list of other solutions or industries noncustomers use to address the same problems and satisfy the same needs.” The ultimate aim of this exercise is to “drill down to the factors” that cause buyers to choose other industries’ offerings over theirs, find a way “to combine these decisive factors and then reduce or eliminate everything else.”

Path Two seeks to identify similar opportunities by looking across strategic groups within the same industry, for example the five star and three star groupings within the hospitality industry. The aim here is to try to identify and examine more closely “what factors determine buyers’ decisions to trade up or down from one strategic group to another” thinking about ways the trade-offs involved might be broken. More clearly understanding “the factors that are decisive for noncustomers as well as customers” allows the team to “emphasize those factors while eliminating and reducing everything else.”[19]

The other four pathways are also aimed at helping a team to see the taken-for-granted world with new eyes. As this exercise is “the most time-consuming part of the blue ocean shift journey,” Kim and Mauborgne advise splitting the team into two sub-teams and giving them three pathways each to explore. They emphasize the importance of fieldwork.[20]

The second task in this step involves turning all of the “market exploration” insights that the team has gathered so far into “well-formulated blue ocean strategic options.” The main blue ocean tools to help with this task are the Four Actions Framework and associated ERRC grid, and the “to-be” strategy canvas.

The four actions framework is built around a set of four questions that help create a new value proposition aimed at opening up a new value-cost frontier through the “simultaneous pursuit of differentiation and low cost.” The four questions are:

- Which factors that the industry takes for granted should be eliminated?
- Which factors should be reduced well below the industry standard?
- Which factors should be raised well above the industry standard?
- Which factors that the industry has never offered should be created?

The first two questions are aimed at lowering costs. The second two are aimed at increasing differentiation. Emphasizing all four is essential to unlocking new sources of profitable growth.^[21] Identifying the most promising factors to feature in this way, and displaying them on the associated ERRC (Eliminate/Reduce/Raise/Create) grid provides the basis for developing the “to-be” strategy canvas.

Step 5: Making your move

By the end of Step 4 the blue ocean team will have developed “up to six potentially viable blue ocean opportunities,” one for each of the six pathways, complete with an ERRC grid and a “to-be” strategy canvas for each. In the final step of the process, “making your move,” the three main tasks involved are:

- Selecting from among the viable blue ocean alternatives.
- Formalizing the business model for the move.
- Launching the initiative and rolling it out.

In choosing which of the value pioneering options to pursue, Kim and Mauborgne recommend setting up a “blue ocean fair,” bringing together the organization’s senior leadership and all the members of the blue ocean team, along with representatives of the major functions likely to be crucial to the success of the initiative. Using such an approach not only helps to foster transparency and widen engagement, but also creates a mini-marketplace for the ideas, letting them compete on their own merits. Following the fair, the team should be encouraged to develop a prototype for the chosen blue ocean offering and conduct a rapid market test to get an early, inexpensive, indicator of its likely customer appeal.

Once the blue ocean strategic move has been selected and its market potential reconfirmed, the final tasks are to fill out more fully and formally the “big-picture business model” and launch the offering. Many main elements of the big-picture business model have already been identified in the four actions framework/ERRC grid exercises. What remains is to map out how these cost-reducing and value-raising elements are likely to operate together as a coherent and optimized activity system to deliver the target profit margin.^[22]

Finally, the “wisest rollout strategy is to start small” to further test and refine the viability of the new blue ocean move, and then “go fast and wide.” Scaling up quickly will then help to unlock the new demand and secure its capture with an innovative business model and the investments that support it. These can create significant barriers to imitation and considerable first mover advantage.

Notes

1. Kim, W.C. and Mauborgne, R. (2005), *Blue Ocean Strategy: How to Create Uncontested Market Space and Make the Competition Irrelevant*, Boston, Harvard Business Review Press.
2. Kim, W.C. and Mauborgne, R. (2017), *Blue Ocean Shift – Beyond Competing: Proven Steps to Inspire Confidence and Seize New Growth*, New York, Hachette Books.
3. For more on the positioning perspective see Porter, M.E. (1980), *Competitive Strategy: Techniques for Analyzing Industries and Competitors*, New York, Free Press. See also, Porter, M.E. (1996), "What is strategy?," *Harvard Business Review*, November-December, 61-78. For more on the core competency perspective see Hamel, G. and Prahalad, C.K. (1994), *Competing for the Future: Breakthrough Strategies for Seizing Control of Your Industry and Creating the Markets of Tomorrow*, Boston, Harvard Business School Press.
4. For a comparison of these two perspectives, see Leavy, B. (2003), "Assessing your strategic alternatives from both a market positioning and a core competence perspective," *Strategy & Leadership*, Vol. 31 No. 6, pp. 29-35.
5. Christensen, C.M. and Raynor, M.E. (2003), *The Innovator's Solution: Creating and Sustaining Successful Growth*, Boston, Harvard Business School Press. See also, Prahalad, C.K. and Ramaswamy, V. (2004), *The Future of Competition: Co-Creating Unique Value with Customers*, Boston, Harvard Business School Press.
6. Kim, W.C. and Mauborgne, R. (2005), *Blue Ocean Strategy*, already cited.
7. Kim, W.C. and Mauborgne, R. (2017), *Blue Ocean Shift*, already cited.
8. For more on the value-cost or productivity frontier see Porter, M.E. (1996), "What is strategy," already cited.
9. Value without innovation tends to lead to incremental value creation, while innovation without sufficient emphasis on value tends to lead to ineffectual technology pioneering where ultimately others, with a greater focus on real buyer utility, come to reap the main rewards.
10. The most prevalent of these red ocean cognitive traps are:
 - Seeing market-creating strategies as customer-led approaches. Rather they are "noncustomer-led."
 - Confusing technology pioneering with value innovation. In fact value innovation may, or may not, involve technology pioneering. Technology pioneering may, or may not, result in value innovation.
 - Equating market-creating strategies with differentiation or low cost strategies. To the contrary, they aim at breaking the differentiation-cost trade-off.
 - Treating market-creating strategies as niche strategies. Instead they aim at creating new aggregations of demand not finer segmentation.
 - Equating creative destruction with market creation. Creative destruction involves demand displacement. Blue ocean strategies aim mainly to unlock new demand in current noncustomers.
For more, see Kim, W.C. and Mauborgne, R. (2015), "Red ocean traps," *Harvard Business Review*, March, pp. 68-73.
11. All quotes in this and the following sections are taken from Kim, W.C. and Mauborgne, R. (2017), *Blue Ocean Shift*. Graphic representations of the *Blue Ocean Strategy Shift* models can be viewed at the authors' website.
12. Ideally, in terms of personal qualities, you want team members who are "good listeners," willing to "raise questions when others don't," "noted for their commitment to getting things done" and can "dream big." You also want to include one or two skeptics capable of functioning as genuine devil's advocates while remaining open to contrary evidence and analysis.
13. A minimum of five "pushes" teams "to challenge their assumptions and to uncover factors that may have become so familiar they no longer register," while a maximum of 12 forces them to identify only the most strategically relevant.
14. Buyer utility mapping revealed several major pain points for customers spread across the matrix, many relating to the role of the cooking oil. This was a major stepping stone in Groupe SEB's successful blue ocean journey that led to the introduction of its ActiFry line, a breakaway electric French fry maker that "requires no frying, and uses only one tablespoon of oil to make two pounds of fries," and is "easy to clean and has no safety or oil disposal issues."

15. "We have rarely seen a team that wasn't initially somewhat reluctant to go out in the field" but "we have also never observed a team that didn't come back glad to have done it" and with a more "visceral, grounded understanding of what buyers experience and the blocks to utility they face."
16. These are the customers that currently "patronize your industry, not because they want to but because they have to." These are the taken-for-granted customers that regular taxi services have since lost to Uber or the hospitality industry lost to Airbnb.
17. Tier two noncustomers are more prevalent than most executives might think. For example, they include the people who decided to paint a room rather than wallpaper it. "The fact that they contemplated and weighed the pros and cons" indicates that "the industry they rejected is far closer to capturing their wallets than most of its players realize."
18. Kim and Mauborgne warn: "Do not be tricked into thinking that third tier noncustomers are 'everyone else.'" Rather, these are "the people or organizations that would ideally like to use, or who could benefit from, what your industry fundamentally offers, but who have never seriously considered doing so because your industry has made this somehow unfeasible, unattractive or unimaginable."
19. In following this second pathway, Kim and Mauborgne advise the team to "concentrate on the largest two strategic groups," including "the one with the largest share of customers, and the one that has the largest share of profitable growth, if they are different." In addition, if there is a "small but very fast-growing strategic group," the team should "zoom in on that one as well."
20. The sub-teams should each try to target at least 10-12 interviews per path with customers and noncustomers. After completing these "live-action market explorations," they "will be armed with a wealth of new insights into how value can be unlocked in innovative ways."
21. The "eliminate" and "create" questions are particularly important, because "reducing" and "raising" activities on their own "don't change the key factors on which everyone else is competing." To make the existing competition irrelevant "new kinds of buyer value need to be offered through the elimination of existing factors and the creation of new ones." Likewise, groups "tasked with creating something new" are often tempted to give too much attention to the "raising" and "creating" activities, and risk ending up "conceiving of potentially costly offerings" that "reflect red ocean differentiation" rather than true "blue ocean strategic moves."
22. The target margin for a blue ocean offering requires setting the price first, at a level which will be compelling enough in terms of the features on offer, to represent a clear leap in value for the buyer. This typically still leaves a "challenging cost target" to be met which can also deliver a leap in profitability for the company. To meet this target, the team will need to reexamine the major elements in the new business model to see where costs can be further reduced in areas that don't compromise customer value.

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