

# DIRECTING DIGITAL INNOVATION AT PEPSICO

by Peter Reynolds, Anne Quaadgras, David Ritter, Stuart Scantlebury, and Benjamin Rehberg

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**I**S DIGITAL INNOVATION DELIVERING real bottom-line business impact to your business? Too often, we see companies generate an abundance of innovation activity, experiments, prototypes, and spin-outs—only to struggle with having these ideas sponsored, integrated, and scaled. In this article, we share lessons on how to direct digital innovation to maximize business impact.

The stakes are high. We examined the financial results of more than 70 large companies recognized as the world's most innovative.<sup>1</sup> Compared with their industries' averages, top performers had higher net margins (11.8 percent), better ROI (5.7 percent), and increased revenue growth (17.1 percent). It's no wonder that CEOs are rating innovation as one of their top priorities.<sup>2</sup> The pressure is on at all companies to be more innovative—and one of the hottest areas of innovation is digital innovation.

A lot has been written on what it takes to get digital innovation right. Aspects for consideration include process, culture, teams, partnering, and technology.<sup>3</sup> In our research, which included case studies of 15 digitally innovative companies, we identified one other char-

acteristic. Rather than just collecting ideas across the organization and “letting a thousand flowers bloom,” these top-performing companies direct their innovation efforts to the areas of greatest impact and business priority. They then lift and scale the resulting innovations across the business.

## PepsiCo—A Digitally Innovative Company

Take PepsiCo, a global food and beverage leader with \$65 billion in revenues and more than 22 billion-dollar brands, such as Frito-Lay, Tropicana, and Gatorade. PepsiCo is regularly recognized among the top innovative companies in the world and has a spectacular five-year growth rate—10.7 percent, compared with the industry average of 2.3 percent.<sup>4</sup>

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We consider PepsiCo to be a digitally innovative company because it applies digitization to every part of the business, including the following:

- *Products and Services.* While PepsiCo is primarily a physical-products company, it also wraps digital services around its products. For example, PepsiCo’s Touch Tower, a digital fountain, can dispense more than 100 flavors of drinks from a benchtop unit with a touch screen. Digital services allow PepsiCo to advertise, run loyalty programs, collect and analyze real-time data, and conduct A/B testing of new products.
- *Processes.* PepsiCo relies on efficient core processes, including merchandizing and distribution, which are supported by traditional enabling processes such as finance and sales. One digital process innovation is an iPad app—Facts on Demand—that shows store-sales performance of PepsiCo products at any time. The app is location based so that, during a visit, a salesperson can compare a store’s sales with those of others nearby and show the results to the store manager.
- *Customer Experience.* PepsiCo is also changing the way it interacts with customers via its interactive social vending machine. Customers can buy products, collect loyalty points, and even send gifts by e-mail or their social-media profiles, while PepsiCo learns about its customers, their locations, and their connections.
- *Strategy.* PepsiCo is continually exploring new business models and ecosystems, in particular in technology, media, and communications. For example, the company was an official launch partner for iTunes Radio.

These examples show that for PepsiCo, digital innovation is not about a standalone digital product or a separate digital business. Digital

*PepsiCo has consistently leveraged music as a growth driver for our brands. We believe that today’s music ecosystem allows our brands to play a more active role in supporting artists and engaging music fans.*

—Frank Cooper, Chief Marketing Officer, Global Consumer Engagement, PepsiCo

innovation is practiced in every part of the business, and it is impacting the bottom line.

## Directing IT Innovation at PepsiCo

To achieve this kind of innovation, PepsiCo has many R&D centers and centers of excellence around the world. Within the IT function, the Business and Information Solution (BIS) innovation team, led by David Bernard, leader of Global Innovation Strategy & Services, is responsible for identifying breakthrough and emerging opportunities that could have a significant impact on PepsiCo’s growth.

At the start of each annual business-planning process, the team partners with business unit CIOs and line managers to identify strategic business capabilities—high-impact, long-term opportunities with potential to create competitive advantage for PepsiCo. These opportunities are referred to as “leverage points.” In 2013, they included product and life cycle management, insights and advanced-analytics solutions, and merchandizing.

Next, the innovation team evaluates points of opportunity in each unit to identify two to three “sticky business challenges,” or challenges that it has not overcome on its own by traditional means. Then the team looks at emerging technology (such as social media, sensors, advanced analytics, security, cloud, and customer-centric design) to facilitate the selection of a small number of challenges it can help solve.

One challenge was to ensure optimized merchandizing solutions for stores with varying layouts in different locations; the solution was an enhancement to PepsiCo’s Facts on Demand iPad app that adds augmented reality to assist in merchandizing PepsiCo products. With this innovation, the iPad provides a 360-degree panoramic visualization of what proven PepsiCo merchandizing solutions would look like in a specific store. The iPad app enhancement is now being employed in various markets to help salespeople serve merchants with the right products displayed in the most effective ways.

In short, the BIS innovation team applies significant effort to find high-priority problems,

*The biggest challenge is getting to the right problem to solve. We have found that this is a significant effort in itself.*

—David Bernard, Leader, Global Innovation Strategy & Services, PepsiCo

directing innovation to where it can deliver the greatest impact, now and in the long term.

To implement innovations, PepsiCo operates a portfolio of initiatives spanning three “horizons.” Horizon 1 is for initiatives in which the company understands both the problem and the solution, such as the augmented reality example above. The team runs the full process through into business case and implementation. Horizon 2 is for initiatives in which the problem is understood but the solution is not known. In these cases, the team creates experiments and prototypes, often involving partners to pitch ideas around the specific problem. Horizon 3 is for areas where PepsiCo doesn’t yet understand either the problem or the opportunity, around which the team may do some preliminary research and evaluation of new technologies. Initiatives flow between horizons over time.

PepsiCo continues to evolve and mature its innovation capability as it looks to new op-

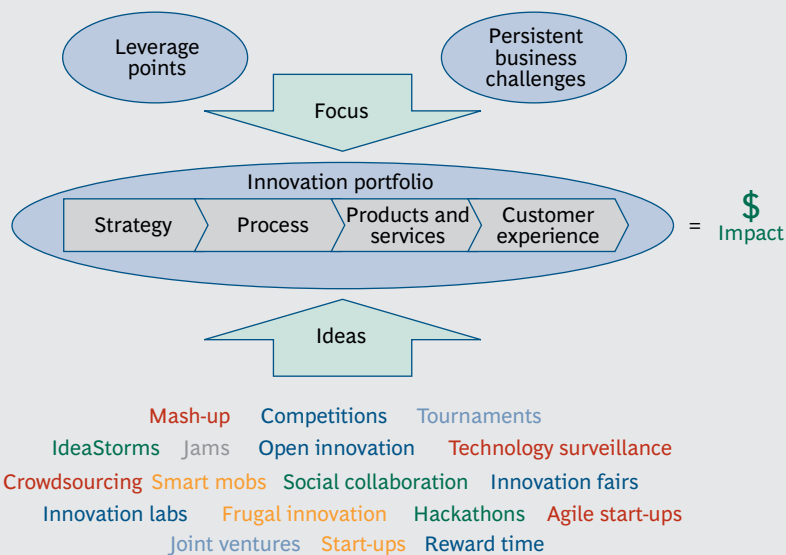
portunities and partnerships to help scale its efforts. Key objectives of the innovation center are stronger engagement and collaboration and active sharing of knowledge, ideas, and processes across PepsiCo. By directing innovation to key areas of high priority and impact, it is increasingly being built into business strategy and plans across the organization.

## Flipping the Switch on Innovation

Too often, in their rush to be innovative, companies end up generating hundreds of ideas across the business—by means of innovation platforms or competitions, for example. This then requires a mammoth ongoing process to select, prioritize, fund, stage gate, and evaluate the ideas. Even when an idea is selected, there are few guarantees that the solution will significantly affect business strategy and fit within agreed-upon priorities.

But rather than starting with a bunch of ideas, PepsiCo and other innovative companies we have studied employ a different approach: they flip the innovation process to first define high-priority problems where innovative solutions could deliver maximum impact. While they still use many of the same processes to innovate, they start at a different point. (See the exhibit.)

### Focusing Innovation on the Areas of Highest Priority and Maximum Impact



Source: BCG analysis.

## Maximize Your Impact from Digital Innovation

There is a lot of pressure to be more innovative, particularly by exploiting digital opportunities. Directing digital innovation to target your company's areas of highest priority and impact is one way of focusing your efforts and delivering real bottom-line impact.

Not all companies are at the stage of PepsiCo. To maximize the business impact from your digital innovation efforts, consider the following questions:

- What are your highest-priority problems to which innovative solutions could deliver the greatest impact?
- Where should you initially focus innovation efforts across the business—strategy, processes, products and services, or customer experience?
- What is your process to lift and scale your successes across the company?

### NOTES

1. These 73 recognized innovative global companies with more than \$2 billion in annual revenues are based on InformationWeek, *2012 Information Week 500*, September 2012, <http://reports.informationweek.com/abstract/186/8993/InformationWeek+500/research-2012-informationweek-500-full-report.html>; Forbes, "World's Most Innovative Companies," 2012, <http://www.forbes.com/innovative-companies/list/>; Thomson Reuters, "Top 100 Global Innovators," 2012,

<http://top100innovators.com/>; and *Fast Company*, "The World's 50 Most Innovative Companies," 2012, <http://www.fastcompany.com/section/most-innovative-companies-2012>. Industry averages were retrieved using the primary North American Industry Classification System code for the company in Hoover's. Analysis conducted by Deepak Mohan, MIT Fellow, MIT System Design and Management 2013.

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3. G. Westerman and K. Gundersen, "Build Innovative Capability Through an Innovation Team," MIT Sloan CISR Research Briefing, Vol. IX, No. 6, June 2009, [http://cisr.mit.edu/blog/documents/2009/06/12/2009\\_0601\\_innovation\\_westermangundersen.pdf](http://cisr.mit.edu/blog/documents/2009/06/12/2009_0601_innovation_westermangundersen.pdf); G. Westerman, "Meeting the Challenge of Innovation," MIT Sloan CISR Research Briefing, Vol. VIII, No. 2D, June 2008, [http://cisr.mit.edu/blog/documents/2008/06/04/2008\\_07\\_2d\\_mtginnovationchallenge\\_westerman.pdf](http://cisr.mit.edu/blog/documents/2008/06/04/2008_07_2d_mtginnovationchallenge_westerman.pdf).

4. Reuters, Financials: PepsiCo Inc., <http://www.reuters.com/finance/stocks/financialHighlights?symbol=PEP>.

*Peter Reynolds and Anne Quaadgras are research scientists at the MIT Sloan School of Management's Center for Information Systems Research.*

*David Ritter is a director in the Boston office of The Boston Consulting Group. You may contact him by e-mail at [ritter.david@bcg.com](mailto:ritter.david@bcg.com).*

*Stuart Scantlebury is a senior advisor in the firm's Boston office. You may contact him by e-mail at [extscantlebury.stuart@bcg.com](mailto:extscantlebury.stuart@bcg.com).*

*Benjamin Rehberg is a principal in BCG's New York office. You may contact him by e-mail at [rehberg.benjamin@bcg.com](mailto:rehberg.benjamin@bcg.com).*