

# Innovating in a downturn

By Phil Kohler

In most industry sectors, R&D expenditure is undergoing urgent review, with medium and long term projects being shelved and funding slashed. The resulting cost savings are undoubtedly attractive, but are they false economies? Will those companies pulling back from longer term development find themselves without the products or services capable of generating the thrust to power out of a recession?

Companies that do more than incremental innovation during a downturn can reap considerable rewards. During the technology downturn of 2000, for example, IBM took a hard look at its innovation strategy, and moved (controversially) away from computer chips, instead focusing efforts on the newly emerging sectors of gaming processors and technology services. By the upturn, IBM was strongly positioned to dominate what turned out to be major growth areas, and quarterly profits continue to rise even in the current harsh economic climate. Sun Microsystems, however, is a more cautionary tale. A market leader of high-end servers before the same recession, Sun missed the growing challenge of the PC market, focused efforts on extensions to the existing portfolio, and has had difficulty recovering since.

A complication is that recessions impact not only the company, but also markets and customers. Considerable churn can take place in the market which is difficult for incumbents to see; those emerging strongly are those that can identify – and are ready to answer – the new needs that emerge, even shaping these needs in the process.

Based on our experience with leading technology innovators, as well as innovating ourselves, we believe companies should concentrate on three objectives in order to survive the downturn and position for the upturn:

- focus the R&D portfolio
- accelerate innovation
- reach outside for support

## Focus the portfolio

The first objective is to assess the existing R&D portfolio and focus efforts. Immediate impact can be found by 'spring cleaning' ongoing projects to free up R&D resources. One company we're working with is suffering from project overload. R&D staff are spread thin with multiple priorities, and management does not have the time to adequately review progress. Taking a hard look at what is consuming resources, ensuring alignment with the strategic direction, and maintaining a balance of short and long term investments will ensure innovation efforts are not being squandered.

We often see companies sacrifice long term projects as a result of portfolio analyses. This bias to the short term can be due to more certain payoffs, vocal customer demand or near term business unit targets. However such a portfolio won't position the company for upturn growth. An effective tool is to shape the portfolio by allocating funds top-down, ensuring balanced investment at the two ends of the portfolio; incremental projects with strong ROIs and a few protected 'long bets' to enable upturn growth.

The pruning zone is then the large platform projects which can be huge resource drains without clear returns.

IP reviews are another way to ensure a company only spends money where it counts. The costs of submitting new patents are high, not to mention the maintenance fees, so alignment with the core business is crucial. A thorough review of patent portfolios frees up cash and often reveals hidden value – IP that can be licensed out or sold on.

## Accelerate innovation

The second objective is to accelerate the pipeline for these short term projects. A more agile approach to innovation, empowering the project team and streamlining the process, makes R&D spend do more for less. Leaner and meaner, the resulting innovation organisation can more quickly deliver products and services.

Many companies in a downturn will focus just on cost reduction, with 10 to 15 per cent mandates across the board. However, this can slow innovation as requests are denied and resources become scarce. Our experience shows that issues with time to market and cost effectiveness can be traced to the same set of root causes. Focusing instead on increasing speed will by default deliver the cost benefits while also bringing forward the payoff from short term projects. The benefit of delivering a project that reduces one per cent of product cost is equal to taking 10 per cent out of the R&D budget (assuming five per cent R&D spend and 50 per cent product cost). Focusing on speed pays off more directly, energises the organisation to improve and does not hamstring existing capabilities.

### Reach outside

The final objective is to reach outside for complementary technologies and avoid building up non-core capabilities. It may seem counter-intuitive in a downturn for companies to increase reliance on external partners, but the objective again is to focus and simplify; focus the internal innovation organisation on differentiating core technologies and capabilities and simplify the remit to accelerate

developments. There will be many areas of development where the technology and/or capability required is not a core strength or is not valued by the market. It is to these areas that an external partner can bring expertise, speed or lower costs as a consequence of their specialisation or scale. An example is a product development we recently performed for a client who had identified a lucrative new market. By collaborating with external partners to leverage existing technologies the product was first to market and now has commanding market share. Similar to an IP review, a capability and technology assessment can also turn up new revenue streams by identifying areas of strength outside the core.

A downturn is a difficult time for innovation, but also one of great opportunity. It is during this period that the competitive order for the inevitable upturn is set. By focusing the portfolio, accelerating innovation and reaching outside for support innovation companies can not only survive the downturn but also position for the upturn.

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## Summary of recommendations

### Focus the portfolio

- reduce the number of projects
- ring-fence investment in new markets / technologies
- align the IP and innovation portfolios

### Accelerate innovation

- focus on speed not cost
- simplify roles and processes to accelerate the pipeline
- weed out weak projects at gate reviews to build a funnel, not a tunnel

### Reach outside

- identify differentiating technologies and capabilities
- leverage external resources for speed and cost
- allocate funds to overcome 'not invented here' bias