

Innovating to grow

By

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Six major innovations¹ account for 32% of global growth over the past decade. They account for 70% in Europe.

Innovation is obviously a critical driver of global growth (along with demographics), and is indeed the only one in mature countries. The mere improvement in productivity through cost reductions enables an economy to grow in volume, but not in value.

The same phenomenon occurs with every business which grows in the long term. The number of products, services, business models which did not exist five years ago can represent 50% to 100% of revenue at any time.

There is no long-term growth without disruptive innovation.

1. The great disruptions

Innovations correspond to six types of disruption (see table 1):

- *Pure inventions*, creating new features or combining old ones in an original way, and generating a new product or a new service: the iPhone (Apple), a new tool combining multiple traditional features; social networks (Facebook), a new way of communicating within a community; search engines (Google) giving instant access to massive layers of information or knowledge to as many people as possible.
- *Technological breakthroughs* (new technology or transposition of a technology developed in another *field*) not changing the existing features but radically transforming its scope, efficiency, or cost: the electric car (Tesla); the production of nuclear energy in the 70s (Westinghouse); the mRNA technology developed against cancer and used for the COVID-19 vaccine (Pfizer/BioNtech and Moderna).
- *The re-segmentation* of the market, changing the structure of the offers and compromises made to best meet the needs of different types of customers while consolidating costs; with a finer or different segmentation, or with a merger of segments: the specialized distribution of fresh products going between distribution of frozen food and the distribution of produce (Grand Frais); the development of low-cost payment methods for independent businesses (Square) with associated services (financing of instalment payments; reservation systems, payroll management systems, etc.).
- *The creation of significant new markets with new price positioning* capturing new consumer classes or needs:
 - *Very high*: the development of vacuum cleaners at prices three times higher than the market with a premium brand, increasing the size of the market by 50% in ten years

¹ E-commerce, mobile phones, online media, search engines and social networks with their online advertising, internet subscriptions, and cloud related software.

(Dyson vacuum cleaners); the iPhone (again) with the development of a premium brand and a unique design (Apple);

- Or conversely very *low*: the development of superstores in the 60s, 70s and 80s, resulted in the distribution of food products (and mass consumption) at low cost thanks to the industrialization of purchases and logistics and the reduction of costs in stores (Walmart); low-cost fast fashion (Zara) thanks to the control of the integrated value chain allowing the rapid renewal of collections and optimized inventory management; low-cost models developed in many industries (Ikea, Ryanair...).
- *The development of a new business model*: modification of the positioning in the value chain, aggregation or disaggregation of stages in the value chain, change in the mode of access to customers (e-commerce with Amazon, online distribution of movies and series with Netflix with modification of the business model: subscription versus renting).
- *The invention of a new design*, especially for everyday consumer products (cars, home equipment products, telephones, clothing...) favoring functionality, strongly differentiating, and allowing a strong identification with the brand (Jeep with the SUV² from the 80s).

These six types of disruption can be combined for some major innovations. The iPhone combined four at its launch: features, technology, price positioning, and design.

Market research, consumer preference research or detailed analyses of major statistical databases cannot predict them because they are the result of a discontinuity. The only relevant analyses to anticipate or *create them* are on the *potential dynamics* related to possible inconsistencies or imbalances between technological, behavioral, and economic factors.

Each new major innovation will itself create profound changes in consumer markets, behaviors, and economic trade-offs. Thus, it generates opportunities for innovation: the development of hypermarkets has made it possible in forty years to reduce the share of the household budget in France devoted to food from 31% in 1960 to 17% in 2000. Without this reduction, the explosion in spending on portable media and telecommunications would not have been possible. The iPhone (and its derivatives) as a structuring tool would not exist on its current scale without the development of the first superstore, Walmart in Arkansas in 1962.

For any team thinking about great potential innovations in its industry, there is a classic question: what are the consequences of the great recent innovations that have impacted my business? Do they generate different opportunities?

The innovation strategy of a company must be based on the search for these potential breakthroughs, on the selection of the most attractive in the short and the medium term and on the coherence of the means (technology, positioning, business model...) in relation to this disruption.

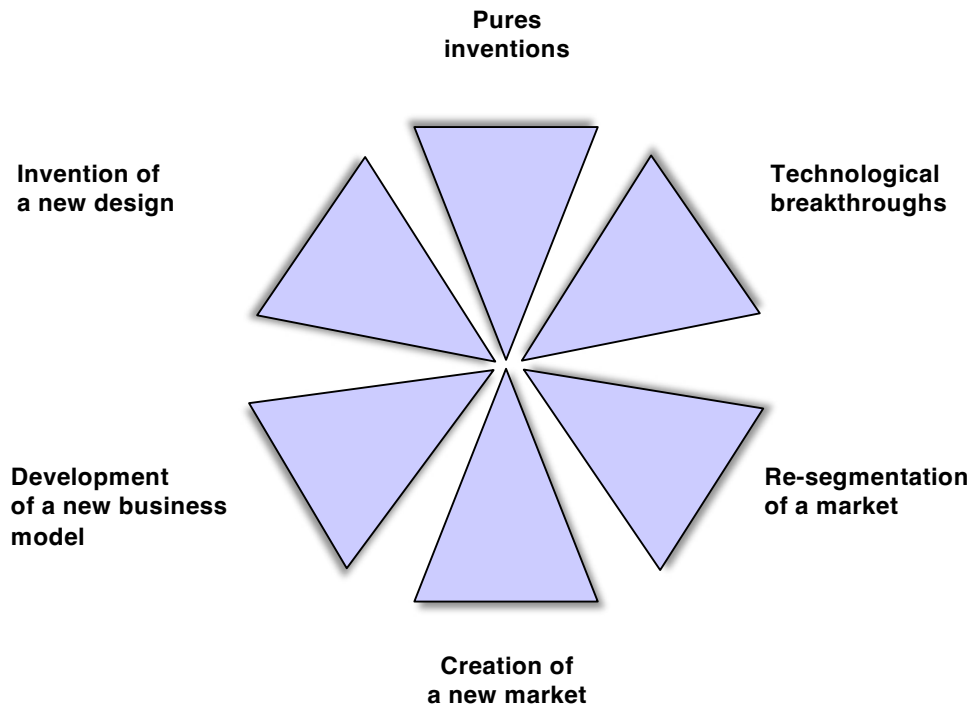
There is no point in pursuing a purely technological axis of disruption that does not correspond to a new trend of market evolution or whose economic structure is incompatible with this current axis (the Ford Edsel in the 60s, the “car of the future” at prices and with an “intermediate” brand, did not correspond to any possible consumer segment; the Blu-ray technology in the 2000s and 2010s was developed to substitute the DVD and was itself replaced by streaming).

² Sport Utility Vehicle (sport utility vehicle)

- Table 1 -

Major innovations

- How to break down and recompose a market? -



Search of discontinuities

- **Inconsistencies, insufficiencies and diseconomies in the offering**
- **Search of unrevealed market potentials**

2. The conditions for success

Beyond its initial design, the success of an innovation is based on three simultaneous levers:

- *The matching of a sufficiently high market potential* resulting from an acceptability or desirability of innovation and at an acceptable level of cost for the targeted consumers. If these two elements are not in sync, innovation does not find its market (the Apple Newton in the 90s introduced tablets *too early* compared to technological possibilities and consumer expectations, and at too high a price).
- *A massive and rapid development*, to reach the scale that makes it economically acceptable, but also ensures it becomes a structural reference in the market before competing copies. The ramping up of resources, commercial development, marketing, logistics, and the coherence of the whole are factors which are just as important as the conception of the innovation (the VHS was a “good enough” system which was quickly deployed and massively adopted by many players; it won against Betamax in the 80s despite having inferior technology). There is no point in developing many products that are technologically superior to the competition if the company cannot deploy them into the market quickly and at scale.
- *Competitive barriers strong enough and resilient enough* in the short and medium term (trademarks, patents, know-how, speed of deployment, economies of scale) to protect competitive positions, ensure full development over time and generate a cash flow greater than the investments made (development of Google and its PageRank algorithm with strong network effects, Intel's growth in microprocessors with strong economies of scale, etc.).

3. Use or bypass the organization?

Innovations go far beyond research & development. They create disruptions that change the perspectives of businesses from at least three standpoints: market structures, competitive structures and companies' internal organizations.

This is the reason why they often come from entrepreneurs and new entrants rather than large established players (it is not Walmart that invented e-commerce, nor Nokia the iPhone). Of the six major innovations presented in the first chapter of this article, only one comes from an established company.

For a large group, the biggest obstacle to innovation is often organizational and cultural, for its design as well as for its deployment.

Within the company, organizational units always produce results within the limits of their current perimeters and business models, therefore rarely breaching the limits of their existing one. This is why groups often outsource innovation to smaller, more agile companies (Pfizer and BioNTech), or even buy them out; or create internal entities transversal to the organization and reporting to the highest level in the organization, carefully separated from technological research or the mere renewal of product ranges (Parrot and its internal “start-ups” in drones); or create separate subsidiaries for the new activity (Google and its subsidiaries in the autonomous car, artificial intelligence, health spaces...).

The development of major innovations and their market deployment also require financial trade-offs and reallocation of resources across the group (growth priorities, human resources, financial resources, etc.) which cannot result from consensus decision-making and which lead to high risk-taking (the development of the iPhone cost Apple 8% of its revenue for two to three years). Strong leadership is needed to initiate and bring such developments to fruition.

Finally, the structure of resources deployed between innovation, R&D, sales, brands, and consumer access networks must allow rapid and massive deployment – if necessary, simultaneously on a global scale – *without bottlenecks* or organizational frictions. The allocation of budgets to the different stages of the market access chain, including the mix of growth investments, is key. Moreover, the organizational logic of innovation and R&D is different from the one needed for the systematic deployment of innovation on a large scale. Large groups often separate the two in different organizations and management methods.

The management method and organization of the company must allow the implementation of these levers. In particular, the organization must be *consistent* with the preferred innovation strategy (disruptive innovator, or agile and competitive follower, or developer of regularly renewed product and service ranges) and the resulting business model. Few companies manage to successfully implement two or three of these strategies concurrently within the same organization.

4. The role of the CEO

Great innovations are great breakthroughs. These can only be initiated by entrepreneurs or by CEOs of large groups who can and want to question their dynamics, their positioning in their businesses and their organizations.

The choice of the innovation model (breakthrough; copying; renewal), the identification of the relevant axes of disruption and investment beyond the comfort zone of the company (six main categories), the corresponding management mode and organization as well as the management of the deployment of innovations in the market are the four key factors to success.

For a large Western group, growth over the last ten years has been driven either by innovation or by China (and often by both). The main axes of innovation have been mostly around digitalization. What will they be, in each business, for the next ten years? How to anticipate them – or even create them?

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Estin & Co is an international strategy consulting firm based in Paris, London, Zurich, New York and Shanghai. The firm assists the senior management of major European, North American and Asian groups in their growth strategies, as well as private equity funds in the analysis and valuation of their investment

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