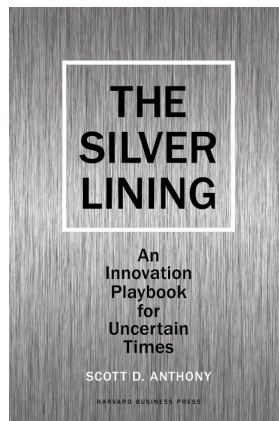


An excerpt from ***THE SILVER LINING: An Innovation Playbook for Uncertain Times***

By Scott Anthony



THE SILVER LINING: An Innovation Playbook for Uncertain Times by Scott Anthony was written specifically for today's downturn. The book is intended to be a guide for executives and innovators seeking to seize the silver lining in today's difficult times; for strategists and investors trying to spot industry winners and losers; and for individuals thinking about how to tighten their own belts or reinvent themselves. Scott D. Anthony is president of Innosight, an innovation consultancy, and lead author of *The Innovator's Guide*

to Growth: Putting Disruptive Innovation to Work. At Innosight, he has worked with clients ranging from national governments to leading consumer products, media, health care, telecommunications, and software companies.

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The Transformation Imperative

The challenge is steep. In the 1980s and 1990s, companies could grow bottom-line profits by focusing on operational excellence. Today, most well-run companies have very little fat left to cut. In the Great Disruption, that leaves companies with a choice: live with shrinking profits and increasing chances of extinction or follow a different approach. For many companies, the challenge is steeper than simply eking out incremental improvements or expanding into new markets. The challenge is reinvention, or transformation.

Simply doing what companies are doing better won't be enough. Companies have to fundamentally do something quite different from today. Perpetual transformation is the only way to thrive during the Great Disruption. Even in healthy economic times, standing still was becoming less of an option as competition intensified and industries collided.

Unfortunately, the brutal reality is that most efforts at transformation fail miserably. Just about every manager has lived through a transformation effort that starts brimming with unbridled hope and ends in crashing disappointment. A survey Innosight administered in late 2008 with Forbes illustrates the basic challenge. The survey found that close to 80 percent of respondents recognized the fundamental need for transformation. About two-thirds of respondents reported allocating resources toward transformation. But only 12 percent of respondents reported making excellent progress in their transformation efforts. Further, 80 percent of respondents reported that the current economic climate was increasing the need for transformation, even if toughening times held the amount of resources for transformation constant.

There are signs of hope. The company most widely cited in the Innosight survey as successfully transforming itself was Apple. Indeed, the period from 2003 to 2008 was absolutely remarkable for a company that limped along during most of the 1990s. Its market capitalization increased from roughly \$5 billion to roughly \$150 billion. While a nontrivial portion of that growth came because Apple dramatically improved the performance of its core computing operations, the lion's share of credit goes to the creation of new growth businesses. Apple launched its first iPod player in 2001, it opened the virtual door of its iTunes online music store in 2003, and it launched its iPhone smartphone in 2007.

Each of those launches became a platform for successive generations of innovations that drove Apple's phenomenal growth. IBM is another company often cited as having mastered perpetual transformation. The company frequently enters into new businesses and categories. Its latest widespread transformation traces back to challenging times in the late 1980s and early 1990s. The company faced intensifying competition in many of its core categories. While the old saying, "No one gets fired for hiring IBM" still held, many other competitors had reached the level of quality where they too were viable purchase options. IBM responded by accelerating its move into service businesses. Today, close to 60 percent of its revenue comes from services (aided by a 2002 purchase of PricewaterhouseCoopers). It also formed a group called Emerging Business Opportunities to enter into new markets. That group has helped IBM create substantial businesses around open-source software, wireless, life sciences, and grid computing.

Notice a connection? Transformation comes from entering new markets and leaving old ones. Companies rarely transform themselves through cost cutting or improved operational effectiveness. Operational effectiveness is necessary to compete, and world-class operators can create competitive advantage, but in almost all cases, operational effectiveness is insufficient to stave off disruption and drive long-term competitive advantage.

The pattern continues. Another company flagged in the Innosight survey was Procter & Gamble. Founded more than 170 years ago, the consumer packaged-goods titan is constantly launching new brands and evaluating which businesses it should exit. During the 2000s, it sold off consumer staples such as food shortening (Crisco), peanut butter (Jif), and coffee (Folgers), and accelerated investments in higher margin health and beauty products. It acquired Wella and its professional hair-care products in 2003 and Gillette men's grooming brands in 2005.

As of this writing, Pampers was P&G's biggest brand. P&G's biggest competitor in the diaper business is Kimberly-Clark (KC), which produces Huggies, Kleenex tissues, and Scott paper towels. If you go back to the 1980s, it wasn't obvious that KC was destined to be a critical P&G competitor. At the time, most of KC's business involved making commodity paper that served as an input for other consumer products companies. KC expanded its efforts into branded consumer products and grew substantially. One of KC's competitors in the paper business in the early 1980s was a Finnish conglomerate that primarily focused on making products derived from natural products, such as rubber boots. In one of the most unlikely transformations in business history, the company entered into the mobile phone market. That company—Nokia—is today one of the world's leading technology companies. While Nokia and KC successfully transformed themselves and reaped the rewards, a third paper company focused on operational effectiveness. International Paper has profit margins and other operating statistics that rival any paper player. But while Nokia and KC created billions of dollars of value, International Paper largely languished.

These examples are not meant to suggest that transformation is easy. It is not. More often than not companies fail when they try to go beyond their core business. But in the Great Disruption, companies don't really have a choice. Investing in transformational efforts in a brutal market appears difficult, but the alternative isn't stagnation, it is extinction.

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