

TAKING ADVANTAGE OF

Tumultuous Times

MONITOR



Claiming the Future

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The geometry of sustained advantage is changing—permanently, irreversibly, and with profound consequences for every organization that wishes to grow, endure and make a difference. This paper outlines the four key global discontinuities that are driving this change, identifies the most significant ways in which a new geometry of advantage is becoming manifest, and advocates several critical sets of actionable and immediate responses. While addressed primarily to leaders in the enterprise sector, the key messages are of equal significance to those leading organizations in the governmental and civic sector.



Taking Advantage of Tumultuous Times is a series from Monitor offering insights into critical issues organizations face during this unprecedented period of economic uncertainty, and how business leaders can use this time to seize opportunities for lasting change and growth.

Today, by most technical measures we appear set to emerge from the 2008/2009 recession, with increasingly positive data regarding global industrial production, growth in trade and a significant rise in most stock markets. However, the recovery remains **uneven, fragile and uncertain**. **Uneven**, because while high-growth economies in China and India demonstrate faster and stronger return to growth (projected by the IMF at 9 percent and 6.4 percent respectively for 2010), the emerging nations in Central and Eastern Europe remain weak. **Fragile**, because the highly developed western economies (including

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and especially the United States and the United Kingdom, with 2010 growth forecasts of only 1.5 percent and 0.9 percent) face continuing vulnerability in the financial sector, still rising unemployment, very sluggish rises in consumer confidence

and retail sales, and concerns regarding further downturns in commercial real estate. **Uncertain**, because there is a real possibility that these continuing weaknesses could result not only in very slow recovery in the west, but even a double-dip or “W-shaped” recession.

The global economic outlook over the next two to three years then, observed even through the most traditional of lenses, is volatile and unclear. However, three assumptions now appear to be quite reasonable:

- First, the entirely catastrophic meltdown of the global financial system and the economic models it supports, anticipated just months ago by some observers, has most probably been averted (for reasons of built-in resilience, good policy or sheer luck, depending on one’s political philosophy and ideology).
- Second, the period of recovery from the 2008-09 recession will be complex, spotty and different from any historic precedents.
- And third, this recession has both illuminated and served to accelerate key global discontinuities that will fundamentally reshape the economic, social, political and business environments in the years ahead.

A meaningful understanding of even the next most immediate stages of economic recovery—and therefore any strategy aimed at even the shortest term survival agenda—is dependent upon an understanding of the profound discontinuities now underway, their key implications for every organization committed to thriving, growing and prospering, and the range of responses that will be required.

As the past few decades have already amply demonstrated, every organization must evolve to remain relevant and effective amidst rapid change. Today, not only is change accelerating, but we are entering a period of discontinuity and uncertainty that defies easy description, much less prediction. However, even in the messiness, it is possible to identify four profound sources of global transformation: the rise of **Post-Western Globalization**, in which emerging economies

and nations have made the transition from followers to innovators, with major implications for the global economy; the **Convergence of Enterprise, Government and Civic Sectors**, which sees a rebalancing of influence among the three sectors driven by market, civic and public interest values; the rise of **Sustainability and Climate Change** as a force driving decisions by governments, enterprises and citizens to innovate for sustainable and less resource-intensive practices; and **Connective Technologies** opening opportunities for innovation and enabling new, valuable webs of co-creation with customers, suppliers, partners and competitors.

POST-WESTERN GLOBALIZATION: AN EMERGING ECONOMIC ORDER

For centuries, Western nations and enterprises have largely created and determined the shape, direction, and rules of the global economy while enjoying an outsized share of economic growth and prosperity. The West has established the terms of engagement in global trade and led the institutions that set and administer the rules. Western nations devised the capital markets and instruments that fuel the global economic engine. The same nations created the most mature product and service markets by addressing the preferences, aspirations, and budgets of Western consumers. While exporting their own cultural norms and values, Western nations accessed and consumed global resources on a per capita basis at levels far outstripping the rest of the world.

That era has now ended. Shanghai, Dubai and Mumbai are gaining prominence as centers of global finance. China boasts the world's larg-

est publicly traded company. Dubai hosts the world's largest shopping mall. Abu Dhabi is home to the world's largest investment fund. The biggest movie industry is in India, not Hollywood. New trade and political alliances are evolving between Asian, African, and Latin American nations. Global institutions are changing to accommodate the growing power and influence of non-Western economies, the rules by which all companies play. Products and services are being developed to meet the needs and preferences of a massive new global middle class, part of the two billion people from non-Western nations who have joined the global economic mainstream, and the billion more expected to do so in the coming decade.

Demographic trends underpin these tectonic shifts in power and demand. Many Western countries see population growth falling below replacement levels, with fewer young workers available to support older citizens. Meanwhile, less developed nations are expected to account for practically all of the additional 3 billion humans predicted to arrive by the time the global population peaks at 9.5 billion in 2050. Only fifty years ago, Europe contained a population two and a half times the size of Africa's. Today, Africa's population is larger, and by 2050 it will be two and a half times that of Europe.

Amid these shifts, leading companies in what were once emerging economies have made the transition from followers to innovators. Consider Indian car company Tata: its modular car called the Nano can be distributed in kit form and assembled at point of sale by local entrepreneurs for half the cost of its cheapest rival.

A CITY PLANET, WEIGHTED TO THE EAST AND SOUTH

The world is becoming a “city planet”. More than half of us now live in cities and every year another 70 million people migrate from rural to urban areas. The economic and social consequences are significant: historically, cities, with their population density and opportunities for specialization and growth of services have always generated economic activity, enfranchisement and innovation. Likewise, the “mega-cities” forming today will become increasingly critical as both markets and drivers of rapid growth. But, whereas in 1900 nine of the 10 largest cities in the world were in North America or Europe, within a couple of years only one — New York — will remain on the list.

Massive and with growing middle classes, megacities expanding in Shanghai, Dubai, Mumbai, Lagos, Sao Paulo and elsewhere are rising centers of innovation and commercial dynamism. These megacities concentrate a disproportionate economic influence over their regional landscape. Taken together, these cities will have a global impact. Their residents’ wants, needs, values, preferences and budgets will influence everything from the use of natural resources to market innovations in products, services, distribution and delivery.

WHERE SECTORS CONVERGE: A WEAVE OF PUBLIC, MORAL AND MARKET VALUES

In the past 30 years, the enterprise sector has enjoyed an unprecedented degree of autonomy. For the most part, its creative dynamism has served as a force for good in the world, creating and spreading wealth and meeting the needs of a growing proportion of humanity. But no sector of society can sustain such autonomy and power without becoming subject to checks and balances — and, indeed, the government and civic sectors are reasserting their influence and rising in prominence. In part, power is swinging in reaction to perceived excesses and failures of the enterprise sector itself, especially with regard to the management of risk in the financial sector. But there are also deeper and more permanent dynamics at play.

First, the role of government has always varied considerably in different regions of the world. As post-western globalization progresses, we

will see a much richer variety of relationships between sectors and different rules of engagement. In the U.S. and Europe, a more central role for government has been re-established in light of the financial crisis — and one that likely will grow to address the scale and urgency of required infrastructural investment. At the same time, the locus of governance is expanding beyond the traditional nation state: upward, to include regional (and likely global) institutions and downward to include the “city state,” which is an increasingly influential actor — witness the Global Alliance of City Mayors aspiring to set the next generation of sustainability policies and programs.

Driving all of these changes is a mounting awareness and concern about the scale, complexity, and interdependence of shared global challenges and a growing conviction that only collaborative efforts between the government, enterprise and civic sectors can address them.

This shift presents profound, long-term challenges and opportunities for each of the sectors. The enterprise sector can no longer assume “permission to play,” but must actively ensure it through meaningful cross-sector collaboration. The civic sector is moving to enable rather than disable wealth-generating economic activity, to forge productive alliances with those whose motives and aspirations are different, and to make practical its growing convening power. The government sector has to become more agile and flexible, to create and collaborate upon common ground with other entities, and to provide coherent leadership in tackling local, national and global challenges.

The leaders, organizations and regions that master these capabilities will shape our shared future—and those who do not will decline in influence and impact.

SUSTAINABILITY AND CLIMATE CHANGE: DEBATES GIVE WAY TO CONSENSUS AND ACTION

Until recently, three factors made climate change a relatively low-level priority for many organizations: First, the data on humanity’s ecological footprint and its impact upon the climate were incomplete and ambiguous. Second, the market-driven enterprise sector lacked mechanisms and incentives to incorporate environmental externalities. And third, the “Tragedy of the Commons”—a phenomenon in which individual people, organizations or groups do not recognize the imperative to protect shared resources until after those resources have been destroyed—was amplified by very low consumption rates in much of the world. All three of these barriers are falling.

After years of argument and debate, most scientific and governmental bodies are finally arriving at a data-driven consensus that our ecological

REBALANCED INFLUENCE, BLURRING BOUNDARIES

Not only are the enterprise, government and civic sectors rebalancing their influence, but the boundaries between their roles are blurring and their relationships are becoming increasingly co-operative and co-creative. Historically, governments have been driven primarily by values of public good; the civic sector by moral values, and the corporate sector by market values. Now every sector is being driven by a combination of all three. We see the evidence everywhere: Sovereign Wealth Funds investing for global capital gains and domestic development; governments setting extremely complex market mechanisms in place to resolve crises in the enterprise sector; major R&D for a malaria vaccine co-funded by GlaxoSmithKline and the Gates

Foundation (with United Nations involvement); an increasing reliance on the voluntary sector to provide public services; the emergence of entrepreneurial models of philanthropy; and more companies embracing the concept of social responsibility as a business fundamental rather than public relations gloss. Also consider: The U.S. forestry industry, once the scourge of environmentalists, now collaborates with green NGOs and includes players now hailed as models of natural asset management. And Coca-Cola, falsely accused of using polluted water in its products in India, earned legitimacy as a collaborator with NGOs and clean-water advocates in government halls for all of India’s citizens.

IT'S ONE SMALL WORLD AFTER ALL

Practically all climate scientists agree that climate change is real, serious and exacerbated by human behavior.

Current levels of human activity probably require about 1.5 planets. Rising global levels of prosperity have the potential to make the shortfall between consumption and carrying capacity much worse. If everyone living in the world now owned and drove cars at the same rate as the average American citizen, we would need a staggering eight planets to support humanity's resource consumption.

Rapid climate change will have broad implications for global food and water systems, human health, land and sea borders, and extreme weather events. As billions of people from the developing world reach for the unsustainable consumption patterns of Western nations, the implications of the Tragedy of the Commons comes into focus. When powerless parts of the world were being impacted by the early consequences of pollution, degradation and climate change, the international impetus for transformational change was limited. However, when a large proportion of the pollution experienced in Los Angeles can be traced to industrial activity in China, the equation changes markedly. As the sheer impossibility of Western consumption patterns on a global level becomes clearer, the imperative of a radical shift in our collective economic behavior becomes both obvious and ultimately inevitable.

footprint currently exceeds the carrying capacity of our planet.

As climate change and sustainability swiftly move from the arena of debate to the arena of action, people around the world will need to reinvent fundamental aspects of how we live, consume, do business, regulate and govern. Organizations and nations will respond with significant investments and innovations in the fields of energy, infrastructure, distribution and logistics that will prove highly disruptive to the current economic and business models of the enterprise sector. The governmental and civic sectors will reshape their agendas to focus on

social challenges related to water, food, health and migration that will be amplified by ecological degradation and climate change.

Most importantly, demand and consumption will evolve in new, less resource-intensive configurations. This is being driven by a variety of factors: growing global awareness; the convergence of religious/spiritual practices and environmental activism; the return to values of thrift in the West following the failures of credit-based consumption; the demonstrated ability of the less developed world to leapfrog the West as it moves up Maslow's hierarchy of needs; and the supply-side development (fueled in part by regulation and new incentives) of an increasing array of more sustainable options and choices in most product and service markets.

CONNECTIVE TECHNOLOGIES DELIVER LIBERATED NETWORKS OF CO-CREATION

The alarm that many organizations felt during the mid-1990s, when the first generation of Internet browsing technologies led to mainstream awareness of the transformative medium, has given way to a complacent belief that enterprises largely have absorbed the impact of the new technology.

Nothing could be further from the truth. We are still in the very earliest phase of creating the applications, improving the technologies, and grasping the possibilities of Internet-enabled connectivity. Even the earliest successful forms of Internet-enabled organizational models demonstrated a remarkable capability to liberate human energy in powerful new ways: eBay liberated entrepreneurship, Wikipedia liberated knowledge and Google liberated a collective spirit of inquiry.

But what we have witnessed so far is merely the start. With accelerating global profusion of Internet access, more and more actors are innovating faster and faster. As the Millennial generation—the first to be surrounded by and interacting with these technologies since birth—enters and assumes a more significant role in the workplace, companies should prepare to see even more radical change in the business environment in the next ten years than what they experienced during the tumult of the last ten. Organizational success will depend on identifying and capturing value in the new forms of relations, new models of organization and new types of value creation enabled by fast-evolving communications technologies.

Today's connective technologies are enabling more complex, iterative, agile and multi-layered sets of relationships amongst multiple actors that represent something more akin to "value webs." Rather than building an entire system around a single dominant player, participants in such value webs can readily be suppliers, partners and competitors to one another, depending on

context. Customers are frequently co-creators, helping forge the next generation of products and services. Innovation is as likely to spring from loose and open alliances as from in house R&D functions. In fact, the most agile companies create platforms for others to work upon. Apple, for example, will soon earn more revenue from its 30 percent share of the sale of iPhone applications (developed by others at zero cost to Apple) than from the sale of the phones themselves.

These four discontinuities already are defining a fundamentally altered world, in which the safe assumptions of the past are becoming increasingly risky bets, and the richest sources of future opportunity and paths to growth are unfamiliar and challenging.

IMPLICATIONS FOR THE FUTURE: NEW RELATIONSHIPS, EXPECTATIONS, OPPORTUNITIES

Taken together, these discontinuities are driving new priorities, challenges, and opportunities for organizations in every sector and region of the

MULTIPLYING THE WISDOM OF NETWORKED CROWDS

The ability of connective technologies to liberate human energy has spawned new movements, networks and political forces as the Internet has matured. Its impact has been felt in the enterprise sector across a wide range of new business applications—including things like digital advertising, e-commerce, sophisticated outsourcing models, cross-boundary collaboration, social networks, customer empowerment blogs and discussion boards, information transparency and complex database interactions. These new capabilities have all generated profound shifts in business models

and competitiveness. Internet-enabled open source collaboration has changed the software industry forever. Corporations are using new communications technologies to unleash the "wisdom of crowds" to identify and test new opportunities and make tough decisions. Small, previously isolated innovators are meeting the needs of large enterprises through Internet-based platforms like InnoCentive. User-generated ads are broadcast to 97 million Super Bowl viewers. The changes are pervasive and growing in frequency and magnitude.

world. The geometry of sustained advantage is being fundamentally altered as the business environment evolves. More than ever, the most successful and enduring organizations will be those best able to both anticipate and adapt to this changing world. In the midst of so much tumult, however, it is particularly challenging to identify and focus on the most critical, probable changes required for success. Nonetheless, by starting with key elements of the geometry of advantage, we can develop a clearer sense of the direction and trajectory of the journey that must be taken. The four most fundamental elements include:

- The roles, relationships, responsibilities, and expectations of enterprises within their social and civic context
- The nature of our customers and the ways we interact with them
- The requirements and processes that underpin our changing innovation agenda and priorities
- The nature of our organizations and the value creation system with which they continuously interact.

In each of these areas, the changes ahead will be profound, but they can be understood and anticipated.

1 A NEW “SOCIAL CONTRACT”: GROWING CIVIC EXPECTATIONS AND OBLIGATIONS

The pursuit of continuous economic growth remains a defining priority for almost all societies and governments. While models of enterprise-driven capitalism have varied meaningfully across cultures, countries and regions, market-

based economies are now almost ubiquitous. And this model has delivered handsomely: the world produced more economic output in the last century than in all of previous human history combined, and growth continues to accelerate in this new millennium.

The result has been an implicit social contract: the enterprise sector generates wealth and prosperity in exchange for a minimum level of intervention and constraint. Within this context, businesses have been able to concentrate on achieving continuous growth and satisfying the expectations of one primary constituency: the capital markets. (Just consider, for example, the level of executive bandwidth routinely dedicated to engaging with Wall Street through investor briefings and communications.) While this clarifying focus has empowered the enterprise sector to drive a clear growth agenda in return for extraordinary economic growth and prosperity, it has also had some unanticipated consequences: an overemphasis on short-term results over longer-term value creation; isolated occurrences of dubious business and accounting practices that have undermined civic confidence; and an overreliance on the judgment of capital markets.

And today, all four structural discontinuities are challenging this status quo. Connective technologies are amplifying and making more transparent the unintended consequences of rapid, enterprise-driven growth, including significant increases in wealth polarization; environmental degradation; negative impacts on human health; and social upheaval, friction, and insecurity. Sustainability concerns pressure businesses to attend seriously to environmental factors

previously treated as economic externalities. Post-Western globalization is likely to slow or even reverse the spread of the more laissez-faire Western capitalism. Blurring sectoral boundaries, more active governments, and a civic sector with increased voice and mobilizing capabilities will disrupt the relative autonomy of the enterprise sector.

Although the degree of change to the social contract remains uncertain, we can expect it to become more nuanced and complex as the world seeks to achieve “good growth” — a wider prosperity that produces fewer adverse environmental and social consequences. This re-examination will undoubtedly force businesses to navigate more challenging paths to their own continuous growth. But there are extremely rich opportunities as well, for those willing to take a bold and proactive stance.

RESPONSES

- **Revisit and make explicit the enterprise’s moral purpose.** It has long been demonstrated that every great, enduring business tends to have a powerful and resonant moral purpose: what it stands for in the world, the difference it aspires to make, the value it produces for people and for societies. This purpose consistently underpins choices, innovations, and actions as the enterprise seeks profit and sustained growth. In recent decades, during which shareholder value has been the goal, moral purpose has been underemphasized, displaced by the more muscular and quantitative language preferred by capital markets. In a world demanding “good growth,” there is a liberating opportunity (perhaps

imperative) to win the support of a broader set of stakeholders — civic society, governments, local communities, customers, and talent — by reemphasizing the foundational moral purpose upon which the business is built. Pursuing and adhering to a moral purpose is an important, though neglected, source of competitive advantage: It helps win the war for talent, save money (by economizing on supervision and control, and reducing operational risk), and earns the respect of external constituencies.



- **Shift from stakeholder management to constituency engagement.** Most businesses already have a clear understanding of the critical stakeholders that have direct power or strong influence on their industry and enterprise model, and explicit strategies and resources for lobbying, influencing, and otherwise “managing” them. Under the evolving social contract, this approach must advance toward a mutually beneficial and interactive relationship with a broader set of constituencies whose growing influence could help determine the ongoing “permission to

play” for the enterprise. This requires shifts both in attitude and action. Even the most “difficult” constituents will be better addressed in a spirit of partnership than of adversarial manipulation. And true engagement will entail an enhanced capacity to listen deeply, to empathize, to communicate transparently, to find common ground, to generate win-win solutions, and, of course, to adapt.

than in more traditional—and, of course, tangible—assets. This represents both a strategic weakness and a lost opportunity. By conducting a comprehensive audit of reputational assets and developing a strategy for protecting, developing and deploying them, most businesses can secure sustained and meaningful competitive and adaptive advantage.

2 PROFOUNDLY CHANGING CUSTOMERS — AND WAYS TO ENGAGE THEM.

Around the middle of the twentieth century, a radical shift occurred from a producer-driven economy to a consumer-driven economy. In the former state, producers determined allocation of resources and defined choices—a period summed up by the phrase often attributed to Henry Ford, “you can have it in any color, as long as it’s black.” The consumer-driven economy that began in 1950s America, by contrast, was distinguished by a plethora of choice, spreading affluence, and a vast increase in purchasing channels, all reinforced by a rapid rise in broadcast media and TV ownership. Together, these elements placed the demand side in the driving seat—an era encapsulated by the mantra, “the customer is king.”

This shift revolutionized the enterprise sector. Over time, considerable organizational power was transferred from manufacturing and engineering to marketing and sales functions. Brand power, customer loyalty, customer service and experience, total quality, and active differentiation all became enterprise priorities. Today, vir



- **Generate a clear strategy for protecting and enhancing reputational assets.** As relationships, trust, and confidence become increasingly critical underpinnings of enduring success, reputational assets have never been as vital. Nor, in the age of the Internet (once described as “a petri dish for conspiracy theories”) have they ever been as vulnerable. Both the importance and the vulnerability of these assets will continue to increase under the emergent social contract. Yet many enterprises have invested considerably less in the security and strengthening of this critical asset class

tually all successful businesses have embedded increasingly sophisticated methods for understanding, serving and occasionally delighting an increasingly demanding world of customers. But another profound shift is now upon us.

The rise of the consumer economy has demonstrated two critically important characteristics that are both now seriously challenged. First, almost every significant new product and service market created over the last fifty years has been initiated, defined and developed to address and satisfy the needs, wants, values, preferences and budgets of relatively homogenous western consumers. The customer base of the future, however, is far more diverse and dynamic. Given the realities of post-Western globalization, economic growth will increasingly come from new places and new sources. The middle classes outside the West—especially in Central and Southeast Asia, Russia, and Latin America— now exceed those of Europe, Japan, and the U.S., and serving their specific demands will require a different and more engaged model than the continuing roll-out of Western-derived goods and services. Meeting the currently unmet needs of the four billion people who have been chronically under-engaged in the global economy—and are even less likely to conform to typical Western demand patterns—represents extraordinary latent growth potential.

The second characteristic of the Western-led consumer economy has been a steady rise in the use of debt to fuel consumption. Average household debt in the U.S., for example, increased more than 25 percent in the last decade. It remains to be seen how the recent financial crisis

has permanently altered that dynamic—though the short term reversal has been clearly manifested. Moreover, the non-western economies have demonstrated a far lower willingness to embrace the debt-enabled path to consumption, and appear much less likely to do so now in light of recent events. This has potentially significant implications for future patterns of demand—and it is not the only driver of meaningful changes ahead. Increasing concerns about sustainability, coupled with generational shifts in expectation, behavior and consumption across the coming-of-age global Millennials, will also drive different and likely more fragmented, customer demand.

Equally important is the current transformation of the means of engaging with customers.

The co-evolution of marketing and new media is reaching a tipping point. Extraordinary growth in the reach and impact of social media is shifting influence over brand perception from marketers to millions of networked citizens. The ability for customers to customize products and services to their own unique tastes has spread across many industries—from automobiles through clothing to cell phones and laptops. Perhaps most significantly, businesses are productively engaging customers to co-create the markets and opportunity spaces of the future. These unstoppable and transformative forces demand significant adaptive responses from enterprises.

MEETING THE NEEDS OF FOUR BILLION PEOPLE IN EMERGING ECONOMIES, WHO ARE UNLIKELY TO CONFORM TO TYPICAL WESTERN DEMAND PATTERNS, REPRESENTS AN EXTRAORDINARY GROWTH OPPORTUNITY.

RESPONSES

- **Tap the tremendous growth potential of megacities.** These huge, fast growing and compact markets—along with smaller, rapidly expanding cities all over the world—are highly valuable, discrete profit pools with a distinctive mix of consumers, channels and ‘go to market’ economics that co-exist in relatively bounded geographies. As sources of a disproportionate amount of wealth and buying power, they offer unique potential to uncover new pockets of growth, opportunity, and profitability, based on the development of new or tailored brands, offerings, and programs. Succeeding will require deep insight into the needs, habits, and preferences of these local marketplaces. It will also mean replacing one-size-fits-all go-to-market models with approaches that are customized to the culture, economics, and infrastructure of the target market. For example, Asian telecommunications giant Bharti AirTel recently created an alliance with Mumbai’s unique Dabbawallahs network to raise awareness of their local telephony services, sell pre-paid cards, distribute materials and undertake similar business development activities. Enterprises that aggressively pursue megacity opportunities will enjoy first mover advantage, developing scalable, replicable platforms—and products—for the future.
- **Proactively explore co-creation opportunities with customers.** Throughout the past five decades or so of the consumer-driven economy, the ability to identify, assess, shape and respond to emergent and latent

customer demand became an increasingly critical capability. That capability is now being massively enhanced in many sectors by a far greater variety of means to actively engage customers in creating and defining future markets. Some of these are relatively incremental approaches. For example, many enterprises, most notably Starbucks, have created online communities of customers whose ideas and desires are actively solicited, while others, including L’Oreal, MasterCard and JetBlue, have launched competitions to access customer talent in the production of user-generated advertisements. More ambitiously, increasing numbers of businesses, including Nokia, are encouraging customers to participate actively in many phases of the offer design process, from identifying desired new characteristics to designing new products. Others, best exemplified by Best Buy, have created and mobilized local community networks to define the desired shopping experience. At perhaps the most revolutionary end of the spectrum, Lego has embraced users to help create an entire product range (Mindstorms NXT), while others are experimenting with “launches” of prototype products on virtual life sites such as Second Life. Given the ever-expanding universe of opportunity, nearly all enterprises would benefit from thoroughly reviewing the various ways in which they can deepen their customer interactions.

- **Create an explicit and dynamic engagement strategy, embracing social media,** which is aligned with your marketing, brand

and digital strategies. The rapid spread and impact of social media has attracted considerable attention recently—and rightly so, as it accelerates and multiplies the permanent changes in the relationships between producers and consumers. This poses real challenges—essentially related to a diminished level of enterprise control and influence over perceptions of their brands, products and services. For example, the massive scaling of what used to be termed “word of mouth” through easy access to ratings and reviews from fellow consumers plays an increasingly significant role in customer choice. YouTube videos of rats at play in a New York Taco Bell, or footage of dozens of customers at a Hertz center watching the only staff member leave the desk unattended as her shift ends, can seriously undermine the most skillful of advertising campaigns. But on the flip side, social media creates powerful new opportunities for appropriate and authentic customer engagement, and can dramatically improve the impact and cost effectiveness of the overall marketing mix. This requires a fundamental rethinking of when, where and how to engage, likely leading to a significant reallocation of resource and investment. For example, enabling customers’ self-directed research may prove more effective than traditional tactics of persuasion; pro-active participation in certain social networks can enable unfortunate mistakes to be turned into opportunities, rather than unfold as crises. Creating a new strategic theory of

engagement, which embraces social media and is linked to existing marketing strategies, will be an increasingly critical success factor for many enterprises.



3 THE INNOVATION IMPERATIVE: NEW DIRECTIONS, PRESSURES AND MEANS

Innovation has always been the primary fuel of economic growth and business success. It is axiomatic that as change accelerates, competitors proliferate, and customers express increasingly aspirational demands, the role and importance of innovation increases.

The conditions that have made innovation increasingly critical—collapsing product life cycles, increasing global competitiveness, and growing and spreading consumption—not only remain in play, they are now joined by new and powerful dynamics from the four global discontinuities. With emergent competitors around the world able to quickly follow established market leaders, commoditization pressures increase.

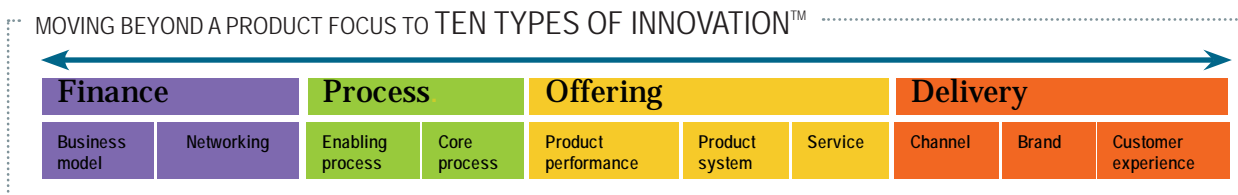
Post-western globalization is paradoxically both undermining the value available from innovation while also increasing its importance as a source of continuing advantage. Sustainability concerns are generating both pressures and potential solutions for moving rapidly toward more environmentally and socially benign economic activity—which must be anticipated as a major driver of innovation over the next decade. And new customers will have new and different demands that are likely to become a particularly important source of innovation.

These shifts will have an impact upon the nature of the innovations that will drive enterprise success in the near future. But there are also profound changes in the manner and type of innovations available. Connective technology enables approaches to innovation that extend far beyond the traditional R&D lab, and, indeed, beyond the boundaries of the enterprise. Co-creation with customers will lead to new models of open innovation. The success of the “open source”

through innovations in business models, channels and unique internal systems and processes.

- **Look beyond product and service**

innovation. A focus on improving current offers to customers is an intuitive starting point for many innovation efforts. However, detailed analysis of innovation investment and return reveals that this focus in aggregate attracts a substantially higher proportion of overall investment than its returns justify—and that very high returns can be generated from relatively modest innovation investment elsewhere in the value creation system. In particular, the last decade has seen a significant increase in the yield secured from innovations around business models, partnerships, process management, and the customer experience. These and other forms of innovation (See figure below, Ten Types of Innovation™) lend themselves to well established, disciplined and effective methods that can systematically drive growth



model in software over the last decade paved the way for a broader suite of more inclusive approaches to gathering the skills, capabilities and energies of broader networks of contributors. Moreover, while most innovations have been focused on products and services, connective technology and an increasingly knowledgeable, networked and interactive economy are also enabling very substantial value to be created

and profitability. Stretching the focus of the enterprise to prioritize these investments will be an increasingly essential dimension of the innovation imperative.

- **Embrace the discipline of open**

innovation: Open innovation occurs when an organization engages customers, suppliers, employees, and other parties in the collaborative development of a valuable

product, service, experience, or process. But despite lots of hype, open innovation has barely moved beyond ethereal debates or examples of a specific “tool.” That’s because it is neither a serendipitous or a one-off approach, but a purposeful, systematic quest for, and use of, new sources of innovation, based on clear principles, processes, and tools. It demands new skills and capabilities and often creates organizational challenges — especially in accessing inspiration and ideas from outside the company. That’s why open innovation requires a commitment from leadership and clear intent and focus. The success of open innovation depends upon identifying the most economically advantageous areas of the business where the impact will be greatest and then carefully designing experiments both to innovate and to evaluate and manage the cadence of change. Done right, open innovation enables lean organizations to find new opportunities rapidly with variable resources; reduces the risk required to place new innovation bets; cuts through organizational blinders to see disruptive threats and non-traditional sources of competition; provides an ability to lock up interested partners as sources of long-term value; and motivates employees and partners alike by creating powerful opportunities for differentiation and growth.

- **Clarify the innovation intent and align systems and adopt best technologies to fulfill it.** Despite the increasing priority it has been afforded over the last couple of decades, innovation remains a surprisingly hit-or-miss discipline. The yield loss from

innovation investments is too high, and would be unacceptable in any other mature field of business management and leadership. Why are so many organizations failing to capitalize on innovation? First, innovation in too many enterprises is a random cluster of good intentions, rather than a clear and explicit intent. Second, few organizations have aligned their most powerful systems and processes to encourage desired innovation, typically over-rewarding “exploitation of the old” over “discovery of the new”. Third, innovation is typically afforded a mysterious and unfathomable aura that denies the strides that have been made in our collective ability to identify what works, what doesn’t, and what management and leadership tools we can derive from it.

A short, twenty-five year old example illustrates how all of these points can be addressed. In 1985, the elderly Sochiro Honda assembled the senior leadership of Honda to focus on the firm’s future. He laid out a clear innovation intent: “six Hondas in every garage”. He declared how to get there: Honda engines in multiple tools for everyday life. He pointed to the essential system change: every high potential leader, to become a senior leader, must spend time working in the small engines division. He identified all Honda had learned about innovation to inform the management tools that must be adopted. Today, in blogs, U.S. citizens observe that while domestic auto manufacturers are producing TV ads mocking Honda for its strengths in lawnmowers, that company makes more profit from its small engines than any U.S. auto firm does from cars.

4 RAPID EVOLUTION OF ORGANIZATIONAL MODELS

How we organize has changed substantively in recent decades. We have collapsed hierarchical levels, dismantled internal silos, reengineered key processes, reconfigured from “multi-national” to “global”, and introduced greater levels of empowerment and autonomy. These shifts have been driven by broader social, technologi-



cal and economic trends that have required most organizations to move beyond the twentieth century imperatives for which they had been designed: managing scale, deploying specialization, achieving standardization, and exercising control in pursuit of efficiency. Increasingly, changes in the external and competitive environments, compounded by uncertainty and complexity, have demanded that organizations develop far greater speed, agility, alignment, and execution effectiveness. Today organizations face additional pressures stemming from the discontinuities set forth in previous sections: new social commitments and expectations, mounting

sustainability challenges, transformed relationships and engagement models with customers, and new opportunities for networked innovation. Taken together, it is clear that we are witnessing nothing less than the rapid emergence of a new global economic system that is more sophisticated, more interactive, and rich with opportunity.

The development of modern economies has long been characterized by a continuous increase in the density of relationships and interactions in the process of value creation. Over the last decade, this development has accelerated as more enterprises “virtualized” by focusing on their core competencies and outsourcing the rest. Traditional value chains are becoming less controllable value “webs”, in which our partners and even our customers are themselves continuously evolving their strategies, aspirations and capabilities. And, as connective technologies and more actors in the global economy generate opportunity for increasingly sophisticated interaction, systems for producing value (everything from innovation, assembly, packaging, distribution, marketing, sales and delivery) are becoming more complex and mutually interdependent. Success, therefore, comes increasingly from the ability to mobilize and deploy assets that we neither own nor control. This shift is so rapid and so profound that it represents a fundamental change in the structure and economics of the global enterprise sector. We have entered the era of the “co-creative” economy.

Success in this changing, networked, global environment requires more innovation in how organizations structure, mobilize, align and focus

key assets and relationships. Happily, these innovations, while challenging, are directionally very consistent with the journey of change already undertaken over recent decades. They will still be aimed at many of the goals already widely set: dismantling boundaries (internal and external) and making them more porous; removing impediments to nimbleness and flexibility, especially by devolving authority to the most appropriate levels; growing and enhancing critical and rare capabilities that can serve to differentiate; investing heavily in vital talent; enabling deeper and more complex collaborations through trust, authenticity and openness; establishing cultures of mutual respect and commitment; and aligning resources around seamless execution, in pursuit of a clear and compelling purpose.

Nonetheless, the journey of change over the coming decade will be even faster and more profound. As business models continue to evolve, they require equal innovation of supporting organizational models. The impact of connective technologies on how we organize is only relatively recently starting to become fully manifested; the first (global) generation raised with these technologies, the Millennials, is entering the workplace with different experiences, expectations and capabilities, and will aggressively push the envelope of possibility. And, perhaps most importantly, the smartest players in most industries will understand that in these tumultuous times their organizational model, rather than simply being designed to deliver against strategy, is actually *joining* strategy as the most critical source of advantage, differentiation and future, sustainable leadership.

RESPONSES

- **Master new, more engaging modalities of change to generate critical new capabilities.**

The oft-quoted mantra, “change is the only constant,” has never been more apt. Increasingly, organizational change and redesign must focus on the development and configuration of some fundamentally different capabilities required to win in the co-creative economy. These new capabilities demand a much more seamless integration of key assets, knowledge, people and activities than has been required historically and generating such capabilities is hard to achieve from standard top-down change processes alone. Other, far more inclusive and participative change modalities are increasingly important for the creation of complex and tightly integrated new capabilities, which inevitably requires greater input and commitment from a larger constituency. These new, more open modalities of change are harder to master and place additional pressures on senior leaders in the short term—but the approaches and best practices do exist, have been demonstrated to work, and result in more sustained and effective outcomes.

- **Reconfigure cost control in light of new business models and organization economics.** Most organizations today have been honed to run with far higher levels of efficiency than was true historically—a consequence of decades of re-engineering, process improvements and regular downsizing initiatives. Further efficiency gains will be harder to achieve from these

traditional approaches—in part because there are diminishing returns available, and also because, for many, there are now real risks of cutting into vital capacities. For example, outsourcing has allowed organizations to “virtualize” and reduce costs by focusing on their core competencies and delegating the rest to a third party. But there can be serious unintended consequences - British Airways, which made substantial savings by outsourcing its in-flight catering, also suffered devastating reputational damage when a labor dispute within its caterer grounded many flights for several days. New strategies for cost control must integrate three key dimensions. The first is a far clearer and more systemic understanding of activities and functions that fall into very different “asset classes.” For example, activities that serve as strategic enablers need to be treated very differently than those that serve as risk mitigators or those that serve as basic services. Second, this differentiation of asset classes must be dynamic and adaptive, recognizing the rapid evolution of new and far more interdependent and interactive business models designed to capture the multiple new growth opportunities offered by the changing global economy. Finally, cost control measures must aggressively exploit the transformative power of connective technologies, especially related to Web 2.0 and social media, to radically alter organizational economics by reducing transaction and co-ordination costs. Those organizations that continue only to deploy traditional approaches such

as “benchmarking” costs against current set of competitors will be significantly outperformed by those who embrace the opportunities and challenges posed by the emergence of new models, economics and innovative non-traditional competitors.

- **Develop existing and future executives to understand, create and lead new types of organization.** Leadership has never been easy or simple, but the challenges today are arguably more complex and daunting than they have ever been. Almost all current leaders have grown—and succeeded—within relatively similar models of organization: and these are now changing faster and more fundamentally than ever before. Tomorrow’s leaders must help create as well as lead far more empowered, nimble, porous and flexible organizations—and these will challenge much of what has been learned and feels comfortable. Rising to this will require a more aggressive stance towards learning about, experimenting with, understanding the key design principles that inform the new organizational models and opportunities. Leaders must also cope with a rapidly changing world—and therefore they must have a far higher level of contextual intelligence than previous generations. They must liberate, not simply harness, the energy of their people in pursuit of less clear-cut goals that was true historically—and therefore they have to learn to trust, and to earn trust, and to develop capacity in others, not dependency. Perhaps most importantly, in a dynamic and volatile world, leaders have

to master uncertainty. They cannot expect right and quantifiable answers to complex issues and problems, and therefore must increasingly exercise judgment—and have the courage to act on their informed convictions rather than their dangerous certainties. These are not trivial qualities—and they must be developed in addition to, not in place of, more traditional leadership attributes. The level and form of the investment that must be placed in leaders is increasing dramatically, and this will prove to be one of the most significant sources of adaptation and advantage for those who rise to the challenge.

BRINGING IT ALL TOGETHER — STRATEGIC RESILIENCE IN A WORLD OF NEW RISK AND OPPORTUNITY

Every organization, in every sector and region, will experience the shifts outlined in this article, and must select, sequence and configure their own specific responses in unique ways to meet them. **However, one emergent imperative is ubiquitous:** enterprise strategies must increasingly deliver not only differentiated competitive advantage, but also superior *resilience*. Many once-great organizations have perished over the last twenty years, and many more will follow them in the coming decade. Resilience—the ability to survive and thrive during the gales of change ahead—will above all else require deep understanding of and responsiveness to these seismic shifts to address the twin fundamentals of enterprise: **risk and opportunity**.

These have always been tightly intertwined. Considerable opportunity resides in addressing

risks others shy away from; while the pursuit of new opportunity invariably produces new risks. Yet in most organizations they are managed quite separately, with little constructive interaction between those holding leadership responsibility for each. This has been sub-optimal but generally not disastrous during periods of relative stability and clearly identifiable paths to growth. We do not live now in such times. The new geometry of advantage poses new risks to those who embrace change, and even greater risks to those who resist it. This need not be as daunting an undertaking as it may seem; it starts with a new and sustained strategic dialogue between those responsible for risk on the one hand and opportunity on the other hand. It requires upgrading traditional enterprise risk management systems, which are becoming too narrowly defined, too oblivious to new risks emerging from within changing business and organizational models, too dependent on quantitative models and too similar to those of competitors to provide advantage.

Shifting from a “risk management” to a “risk leadership” mindset also requires resolution of a paradox - in an increasingly transparent world rich in data, information and interpretation, we are confronted by greater levels of uncertainty than ever, and risk being overwhelmed into paralysis. The resolution is to adopt both an “inside-out” perspective that identifies the handful of most significant strategic vulnerabilities

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of the enterprise and its entire value creation system, and to couple this with an “outside-in” perspective that includes monitoring of those variables known to have a potential impact on our vulnerabilities, and broader scanning of anomalies that can reveal high impact shifts that are not currently on the radar screen. Both monitoring and scanning systems should ideally draw upon a combination of internal and external networks and open source data and information. Combined with greater and more sophisticated use of scenario planning and other simulation methodologies to “rehearse the future”, these “outside-in” and “inside-out” approaches will contribute substantially to the strategic resilience of those who adopt them aggressively.

The victories available to those organizations able to play effectively in an environment of discontinuity (including managing the fundamental shifts in mindset, behavior, capability and strategy) are extraordinary. Ambitious leaders have an opportunity today that is probably unprecedented—to actively exploit the radical changes in the geometry of advantage, and to refocus strategy on achieving resilience in a time of extreme turbulence. Those who succeed will not only claim the future for their organizations—but will also help define the future for us all. •

TAKING ADVANTAGE OF

Tumultuous Times

Taking Advantage of Tumultuous Times is a series of articles from Monitor offering insights into critical issues organizations face during this unprecedented period. Today's economic uncertainties, combined with multiple, significant and disruptive forces, change the nature of industries and competition across the globe. The articles explain how business leaders can seize opportunities during these times for lasting change and growth. Read more at www.monitor.com/tumultuoustimes.

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