Addressing the Innovator's Dilemma: How Chief Strategy Officers Can Spot & Respond to Existential Threats

At a glance

Even decades after the publishing of Clayton Christensen's *Innovator's Dilemma*, many organizations still wrestle with their efforts to nurture mainstream business lines and products while simultaneously preparing for future innovations and potential disruption. Most difficult is to distill and identify true external threats that are not yet fully mature amid the myriad overhyped changes in play.

This whitepaper summarizes key insights from a group of Chief Strategy Officers focused on addressing the Innovator's Dilemma – the challenge mature companies face in responding to disruptive innovations that threaten their core business model. Members of the Outthinker Strategy Network – a peer network focused on evolving the role of strategy and innovation in organizations – and thought leader David S. Duncan, former colleague and co-author of Christensen convened to discuss experiences and recommendations on how to identify, engage executive teams, boards, and entire organizations, and respond to disruptive threats. Following are the key insights business leaders should consider when seeking to achieve a balance between growing core products and services while keeping ahead of disruption from competitive threats.

Introduction

The Innovator's Dilemma, a concept first described by business theorist Clayton Christensen, refers to the difficulty well-run, successful companies have in responding to disruptive innovations - innovations that create new value networks and eventually disrupt existing markets. Successful companies can do everything "right" and still lose their market leadership, or even fail, as new and unexpected competitors rise and overtake the market.

Incumbent market leaders often struggle to embrace disruptive innovations because:

- Their existing customers don't need or want them initially - the innovations underperform existing solutions in the mainstream market
- The new innovations have unclear market demand and profits - so they don't get priority relative to sustaining innovations for current customers
- The innovations don't fit the company's existing processes, values, and business models

This makes it strategically challenging for market leaders to divert resources into disruptive innovations at the expense of their core business. By the time the disruptive innovation has improved enough to vie for mainstream customers, it's often too late for incumbents to catch up.

Christensen highlighted the disk drive industry as an example. Incumbents like Seagate focused on ever higher capacity drives for mainstream customers. Meanwhile, entrants like Quantum created smaller, lower-capacity, cheaper drives that were initially dismissed. But over time, the disruptive drives improved and eventually displaced incumbents by combining good enough capacity with cheaper prices.

Christensen's caution is still very real in organizations. Executive teams and boards, despite acknowledging the possibility of disruption, lag in putting in place an adequate approach to identifying, engaging, making decisions, and executing actions that can protect or even move the organization at the forefront of disruption. What is required is 1) a means to establish the right environment for discussion and engagement. 2) rigorous debate on key questions such as how to explore new opportunities while protecting the core business, how to anticipate and prepare for disruptive threats. Outthinker Networks CSOs working on this topic raised several key insights that worked for them in evolving how organizational leaders better approach the Innovator's Dilemma:

Identifying potential threats generates a sense of urgency

It is common for mature, successful companies to dismiss or minimize a potential disruptive threat. These threats typically do not meet the performance criteria of the incumbent products or services, or otherwise run counter to the current providers' values or precepts. Merely highlighting general statistical data related to the new threat is not likely to provoke action, for exactly the reasons they were dismissed or minimized initially. To provoke action and interest, a threat needs to be perceived viscerally, through areas that can touch closer to the reality and guts of decision-makers. Here are some suggestions given by the team:

Track Lost Clients

Nothing is more painful than finding out a client no longer wants our offers. However, tracking the reasons can show possibilities and trends that force important discussions. Analyzing lost accounts or having regular open loss-review meetings with clients can reveal where potential disruption is emerging. Asking clients who have recently left or who are reducing their business both: 1) why they are leaving or reducing and 2) what alternatives they are pursuing provides market intelligence that exit surveys alone cannot match. The segments most susceptible to disruption may appear more clearly through these conversations.

Leaders should ask: Are certain segments more prone to trying new solutions? What one-off losses signal a potential pattern? What jobs are departing customers hiring another firm to do? Which changes should we be paying attention to?

Look Beyond the Sector

Looking for threats only within industry boundaries constrains how companies think about innovations. Looking at solutions emerging in other or adjacent sectors provides fresh perspectives and foresight into disruption that may be just around the corner. For instance, what business model innovations are thriving in high-tech that could translate to retail? How are other business-to-business offerings leveraging technology?
Seeking innovation lessons from other industries can offer new insights. Broadening the aperture often reveals new models to consider that sector insiders would dismiss as irrelevant. It also highlights how other sectors are responding to the same underlying drivers of change.

Recognize the Lifecycles of Existing Businesses

Although a well-known concept, many companies still ignore business and product lifecycles. Mature companies may "ask" for disruptors. When disrupted, even dominant businesses and products will face declines as part of their lifecycle. Planning for this inevitability helps leaders make smart innovation decisions.

However, precipitating disruption may still be an extremely difficult and unpopular move. While such a decision may make rational sense, it cuts against many management ideals and training to avoid commoditization or cannibalization of their

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proven offerings. Once again, clear and convincing evidence that the business or offering at issue may be tapering must be coupled with visceral conviction before many companies will begin the journey of attempting to disrupt their own business or products.

Engaging the Organization

After acknowledging possible threat vectors, engaging the organization becomes the next big constraint – and not an easy one. Start early and gain alignment:

Involve Internal Stakeholders Early

Involving stakeholders from existing business lines early when exploring potentially disruptive innovations helps secure buy-in. Their input on whether a disruption is real and implications for the core business is invaluable. It also avoids "organizational organ rejection" of new ideas that may otherwise be seen as overhyped or irrelevant threats by others within the company. Well-coordinated committees that use time efficiently and create a sense of belonging for those that are focused on keeping profit centers running – they can help minimize the risk many may feel about the impact of disruption.

Get Alignment on Strategic Questions

The organization must align around a shared set of assumptions regarding future trends and their implications for the business model. Until the leadership team has "deep, visceral" alignment on a vision for the future, it's hard to commit to investments beyond the core business. Questions also drive the whole organization to get close to clients and real-world conditions to get answers.

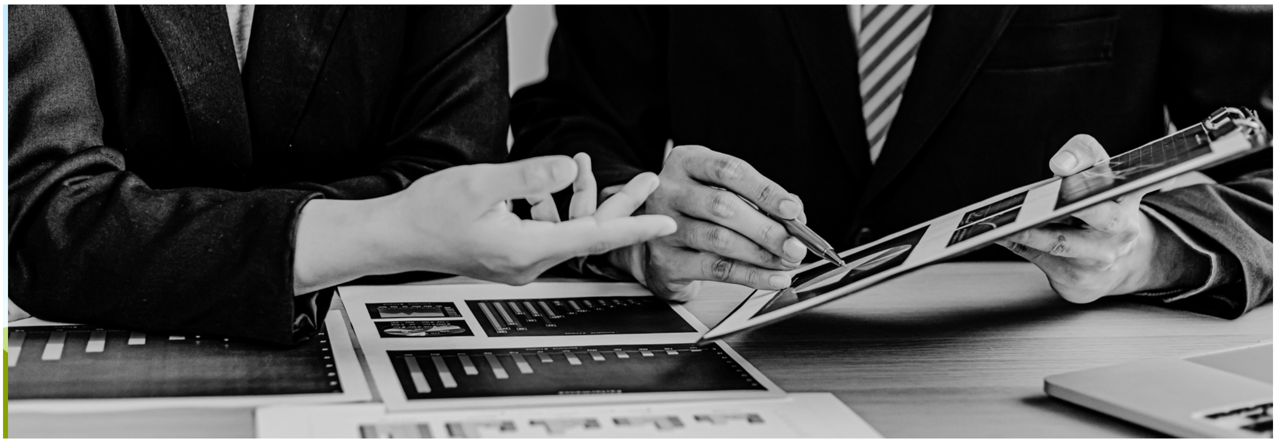
Potential questions to drive alignment include:

- Who will our future customers be and what problems will they need to solve?
- What types of solutions will they expect?
- How will our basis of competition shift?
- How robust will our core business be in that future environment?
- What is our desired scale/scope in that environment?
- What new offerings must we create to fill our strategic gap?
- How must our core business adapt?

Rather than general trends, strategy leaders should aim to develop specific quantifiable assumptions on the magnitude and timing of impacts. For example, how much market share will a new solution take and in what timeframe? What constitutes a ‘material’ threat – is it something that will impact the business in the next year, or will it manifest over the next decade? The answer to these questions can significantly influence the strategic approach a company takes.

As one CSO explained, “One of the dimensions we use in prioritizing is the imminence of a particular threat. We might ask ourselves, for example, what we think our industry will look like 10 years from now? That may be important. But if we think it’s going to look different in one year, we’d better be addressing it immediately.”

This alignment helps provide the strategic rationale for disruptive innovation investments and prevents defaulting to the status quo.



Set the foundations for execution

You can overcome the buy-in and engagement challenge, but if you don’t remove some common execution traps you risk the whole reputation of innovation in the organization.

Consider Organizational Structure and Governance Framework
A critical aspect to consider is the structure of the organization and how it interacts with lines of business. Does the responsibility of identifying and responding to material threats lie within the line of business? Or does a central function play a role in this process?
One CSO related, “We have a five phase-gate process: seed, develop, test, prove, and scale. When we scale or launch the business, it leaves the innovation group, and becomes its own P&L. We only want to launch things that we have high confidence will achieve sustainable profitability. This is a high bar.”
Disruptive opportunities and innovation can play an important, although not exclusive role in the intake process for an innovation program.

Test Innovations in Adjacent Markets First
Before threatening the core business, disruptive innovations can be tested in adjacent "fringe" markets. Once proven, the application to the core becomes evident. Incumbents worried about cannibalization often try protecting their core market first. But this restricts innovation to sustaining improvements for current customers versus Incumbents worried about cannibalization often try protecting their core market first. But this restricts innovation to sustaining improvements for current customers versus breakthroughs. New autonomous entities have the patience and objectivity to nurture innovations through market testing before broader launch.

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Conclusion

Addressing the Innovator's Dilemma is not a straightforward task. It requires accepting the reality and understanding of the business landscape, a willingness to question existing assumptions, and the courage to embrace the future. It also requires the challenging responsibility of aligning and engaging the rest of the management team. CSOs can play a critical role in confronting the challenge of protecting their companies from competitive disruption and keeping the organization well-positioned in an ever-changing competitive landscape.

Some key implications and actions for strategy leaders include:

- Recognizing that CSOs play a key role in helping companies avoid being disrupted
- Looking for strong evidence of where it hurts you the most: Tracking lost clients reveals where disruption can start in the market. Also, looking beyond the sector for threats avoids missing innovations emerging in adjacent industries.
- Involving stakeholders from core businesses early on increases buy-in for disruptive concepts
- Aligning leadership on assumptions of how the business will need to evolve is critical before considering potentially disruptive innovations
- Recognizing the lifecycle of current businesses helps frame appropriate innovation responses
- Having the proper structure in place for the different innovation life-cycle stages.
- Testing disruptive innovations in fringe markets first reduces risk to the core business

By putting in place these experience-backed recommendations from Outthinker Network heads of strategy, CSOs can help their organizations to address if not overcome the Innovator's Dilemma. Taking proactive steps to identify and respond to disruptive threats is key to sustained competitive performance. Maintaining this organizational commitment to self-disruption ensures companies can compete both today and in the future.

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