Innovation in a crisis. Why it is more critical than ever.

McKinsey & Company

By Jordan Bar Am, Laura Furstenthal, Felicitas Jorge, and Erik Roth

DOWNLOADS

Article (PDF-794KB)

John F. Kennedy once observed that the word "crisis" in Chinese is composed of two characters—one representing danger, the other opportunity. He may not have been entirely correct on the linguistics, but the sentiment is true enough: a crisis presents a choice. This is particularly true today.

The COVID-19 pandemic has upended nearly every aspect of life, from the personal (how people live and work) to the professional (how companies interact with their customers, how customers choose and purchase products and services, how supply chains deliver them). In our recent survey of more than 200 organizations across industries, more than 90 percent of executives said they expect the fallout from COVID-19 to fundamentally change the way they do business over the next five years, with almost as many asserting that the crisis will have a lasting impact on their customers' needs (Exhibit 1).

Exhibit 1

The COVID-19 crisis presents an opportunity that few feel equipped to pursue.

Although most executives agree that innovating the business will be critical …

90% believe that the COVID-19 crisis will fundamentally change the way they do business over the next 5 years

85% are concerned that the COVID-19 crisis will have a lasting impact on their customers' needs and wants over the next 5 years

… few feel equipped to face the challenge.

21% have the expertise, resources, and commitment to pursue new growth successfully

2/3 believe that this will be the most challenging moment in their executive career

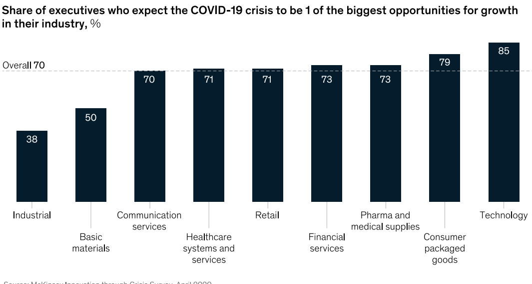
McKinsey & Company

However, more than three-quarters also agreed that the crisis will create significant new opportunities for growth, although this varies significantly by industry (Exhibit 2).

Exhibit 2

Nearly three of four executives agree that changes brought about by COVID-19 will be a big opportunity for growth, with variation across industries.

Share of executives who expect the COVID-19 crisis to be 1 of the biggest opportunities for growth in their industry, %



Source: McKinsey Innovation through Crisis Survey, April 2020

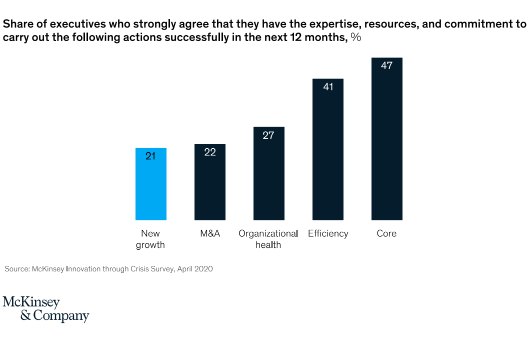
McKinsey & Company

Of course, seeing the opportunities emerging from this crisis is not the same as being able to seize them. Fewer than 30 percent of these same executives feel confident that they are prepared to address the changes they see coming. The area in which they feel the most challenged is delivering net new growth opportunities (Exhibit 3).

Exhibit 3

Few executives feel confident that they are prepared to capture new growth opportunities.

Share of executives who strongly agree that they have the expertise, resources, and commitment to carry out the following actions successfully in the next 12 months, %



Source: McKinsey Innovation through Crisis Survey, April 2020

McKinsey & Company

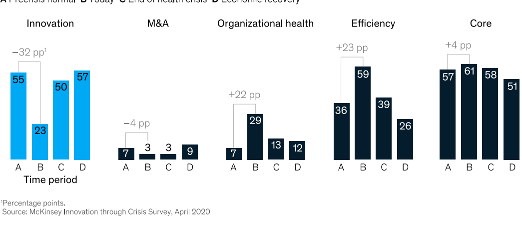
How are executives responding? As might be expected, they are largely focusing on maintaining business continuity, especially in their core. Executives must weigh cutting costs, driving productivity, and implementing safety measures against supporting innovation-led growth. Unsurprisingly, investments in innovation are suffering. The executives in our survey strongly believe that they will return to innovation-related initiatives once the world has stabilized, the core business is secure, and the path forward is clearer. However, only a quarter reported that capturing new growth was a top priority (first- or second-order) today, compared to roughly 60 percent before the crisis hit (Exhibit 4).

Exhibit 4

Commitment to innovation has decreased as companies work through the COVID-19 crisis and focus on short-term issues.

Share of executives who list each action as the No. 1 or No. 2 priority precrisis vs today, %

A Precrisis normal **B** Today **C** End of health crisis **D** Economic recovery



[1]Percentage points.
Source: McKinsey Innovation through Crisis Survey, April 2020

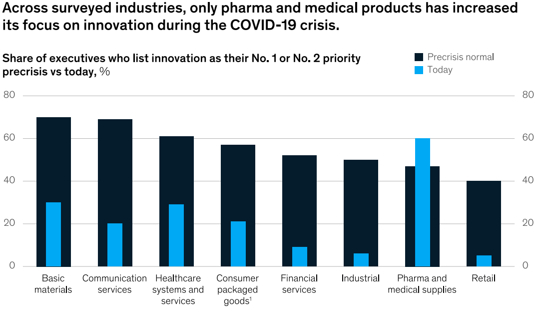
McKinsey & Company

This decline in focus on innovation is evident across every industry we surveyed; the sole exception is pharmaceuticals and medical products, where we see an almost 30-percent increase in the immediate focus on innovation (Exhibit 5).

Exhibit 5

Across surveyed industries, only pharma and medical products has increased its focus on innovation during the COVID-19 crisis.

Share of executives who list innovation as their No. 1 or No. 2 priority precrisis vs today, %



[1]Includes grocery-retail businesses.
Source: McKinsey Innovation through Crisis Survey, April 2020

McKinsey & Company

Leaders face an important choice around supporting innovation-led growth in the short term, one that may have lasting consequences for their companies' ability to grow in the years to come. Our research suggests that playing it safe may be a shortsighted decision right now.

The case for innovation

Our survey and subsequent interviews with business leaders tell us that many companies are deprioritizing innovation to concentrate on four things: shoring up their core business, pursuing known opportunity spaces, conserving cash and minimizing risk, and waiting until "there is more clarity." However, we believe that, particularly in times of crisis more urgent actions to take include:

- adapting the core to meet shifting customer needs
- identifying and quickly addressing new opportunity areas being created by the changing landscape
- reevaluating the innovation initiative portfolio and ensuring resources are allocated appropriately
- building the foundation for postcrisis growth in order to remain competitive in the recovery period

Many businesses simply cannot operate as they have in the past. What made a company successful historically may no longer be possible during or after the crisis. Customers may struggle to pay. Channels may have radically shifted to accommodate new needs or work around new constraints. A stable regulatory context may have changed, potentially creating opportunities that never existed before. The assumptions that supported years of stable, predictable growth may no longer be valid.

Explore the collection

Competitive advantages shift dynamically as business models adapt to new market realities, and the core capabilities that made an organization distinctive may suddenly be less differentiating. While the rise of digital has been mounting similar pressures for more than a decade, the current crisis has significantly exacerbated and accelerated its disruptive force. Sudden pivots observed during the COVID-19 pandemic include:

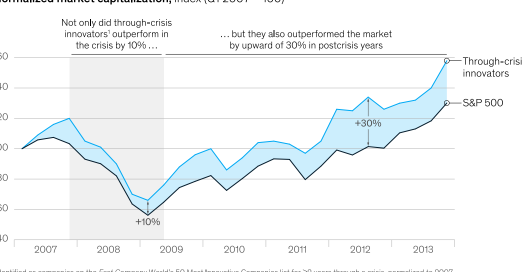
- *Changes to sales models.* Firms with significant field forces can no longer rely on in-person coverage to outcompete. According to McKinsey's B2B Decision-Maker Pulse survey, 96 percent of businesses have changed their go-to-market model since the pandemic hit, with the overwhelming majority turning to multiple forms of digital engagement with customers. Sales coverage has been completely redefined as companies discover that virtual technology allows them to do things that were nearly impossible previously, such as assembling the "perfect team" of experts for every sales pitch. In this digital sales sphere, smaller firms can often "match up" to even their biggest competitors.
- *Need for new offerings.* Food distributors that traditionally supplied restaurants are setting up digital direct-to-consumer channels as the crisis decimated their core restaurant sales. Similarly, the entertainment industry is generating new content (for example, sports retrospectives) to fill the void in programming created by the suspension in sports leagues. Even museums are creating and streaming digital content to enable people to enjoy their offerings from the comfort and safety of home (for instance, Getty's "life Imitating art" challenge).
- *Rapid changes in customer behavior.* For years, videoconferencing providers enjoyed steady growth by focusing on corporate customers. This market typically required expensive deployments, often involving the physical installation of specialized equipment and training to ensure high-quality connections. Now Zoom, with its simple setup and almost viral connectivity, has become the "Kleenex" of the videoconference world. Practically overnight, the world has grown accustomed to "zooming" for myriad purposes, including the arts, religion, fitness, and social connections with colleagues, friends, and family.
- *Influx of competitors from different industries.* Medical-device firms that historically had a narrow competitive set and were insulated by a complex and highly technical regulatory approval process are facing competition from previously unimagined new entrants such as home appliance manufacturers and automakers, as regulations are relaxed to meet critical needs. Who could have predicted the rapid approval and success of GM and Dyson as ventilator manufacturers?

Businesses can gain long-term advantages by understanding such shifts and the opportunities they present. In past crises, companies that invested in innovation delivered superior growth and performance postcrisis. Organizations that maintained their innovation focus through the 2009 financial crisis, for example, emerged stronger, outperforming the market average by more than 30 percent and continuing to deliver accelerated growth over the subsequent three to five years (Exhibit 6).

Exhibit 6

History suggests that companies that invest in innovation through a crisis outperform peers during the recovery.

Normalized market capitalization, index (Q1 2007 = 100)



[1]Identified as companies on the *Fast Company* World's 50 Most Innovative Companies list for ≥2 years through a crisis, normalized to 2007.

McKinsey & Company

Crises, especially the one we are experiencing now, have a significant financial and human toll, stranding assets and human capital and causing significant social and economic dislocation. However, many of these dynamics are ingredients for disruption from which new business models emerge. For example, the sharing economy rose out of the 2009 financial crisis as technology enabled the creation of marketplaces for underutilized assets just as people were seeking much-needed new sources of income, catching incumbents unprepared. The SARS epidemic that ravaged Asia in 2002 and led its citizens to shelter in place was the impetus for growth and widespread adoption of e-commerce in that region, making China the epicenter of innovation around social commerce. The more recent focus on the climate change crisis has driven significant growth in solar equipment and electric cars, as well as innovation around more "earth-friendly" foods such plant-based meat substitutes.

How should companies that believe in the innovation imperative pivot to pursue it today? What follows are our recommendations for ways to approach the recovery from this crisis that can significantly increase the value captured from innovation-led growth.

The recipe for emerging as an innovation leader

In earlier research, we introduced the Eight Essentials of Innovation—the critical practices that have the greatest impact on innovation success. We subsequently showed that mastering the Eight Essentials leads to significantly higher performance, with organizations that excel at most of these practices delivering 2.4 times higher economic profit. Mastering these innovation essentials is even more important now, as companies prepare to return to growth coming out of the crisis. The immediate challenge is motivating teams to bring intense focus, speed, and agility to delivering new sources of value. Crises are like adrenaline for innovation, causing barriers that once took years to overcome to evaporate in a matter of days. Entrenched orthodoxies on "the way things are done" are replaced with "the new way we do things" almost overnight.

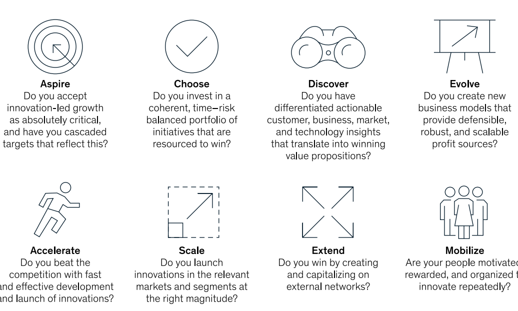
MOST POPULAR INSIGHTS

1. COVID-19: Implications for business
2. Reimagining the office and work life after COVID-19
3. 'True Gen': Generation Z and its implications for companies
4. The future of work in Europe
5. How centered leaders achieve extraordinary results

To emerge as leaders from this crisis, companies can rely on the Eight Essentials of Innovation as a formula and a road map for success. While all of the Eight Essentials matter, our earlier research has shown that in times of broad economic stability, two of them—*Aspire* and *Choose*—are most important for generating immediate outsized impact. In times of crisis, however, we observe that other essentials take on greater significance, suggesting a different order of action (Exhibit 7). We recommend prioritizing *Discover, Evolve,* and *Choose*; these three will guide an organization in reorienting its focus, as needed. Then leaders can address *Aspire* to reset their guiding "North Star," *Accelerate* and *Scale* to invest at the right levels and speed given potential changes in end markets, *Extend* to develop new types of ecosystems, and finally *Mobilize* to put in place the appropriate talent and incentives to activate the innovation plans.

Exhibit 7

The Eight Essentials of Innovation serve as an important guidepost for navigating the COVID-19 crisis.



McKinsey & Company

Discover. The market context during a crisis is dynamic, with little certainty about what will define the world when things stabilize. Having a powerful approach to analyzing this type of landscape requires the ability to *Discover*. It is critical for companies to overinvest in rediscovering what matters to customers now and understanding the impact those changing needs will have on their business. As Henry Ford once remarked, "If I had asked people what they wanted, they would have said 'faster horses.'"

Crises tend to reshape spending patterns, which in turn change how attractive an end market may be. For example, many consumer-facing companies must now contend with the likelihood that brick-and-mortar retail may never return to its glory days, as many stores become mini-distribution hubs for e-commerce. Whereas the commercial real estate market used to place a premium on the highest floors of office buildings, concerns about confined crowds in elevators and high-density work spaces may now flip these valuations on their heads.

Collecting and synthesizing market insights should not be a siloed task left to a dedicated function or agency. Entire organizations, from sales and customer service to marketing and operations, can be activated to monitor change and interpret its impact. Every customer touchpoint is a new opportunity to learn. Having the ability to rapidly synthesize the many signals coming into an organization, recognize new patterns of customer behavior, and take action quickly can give companies a head start in the innovation race.

Organizing this information so that it can be rapidly converted into new products, services, customer experiences, and business models is critical. First, it means having a way to clearly define and prioritize valuable problems to solve for customers. To identify a valuable problem, companies need to determine a clear "who" (a specific customer description), develop a fact-based understanding of the burning challenge this customer faces, and specify the outcome they hope to achieve by solving it. This strict definition helps to separate fuzzy and unhelpful questions from clear customer needs for which a solution can be precisely assessed.

Sidebar

Concept-generation tools

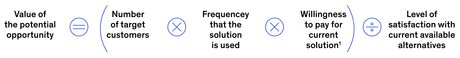
Businesses can further prioritize among various valuable problems to solve using an equation that factors in the size of the potential market, the value that customers place on a solution, and the relative satisfaction of alternatives to the proposed solution (Exhibit 8). Once businesses have identified the most valuable and relevant problems to solve, they can use concept-generation approaches to arrive at

hundreds of ideas within a day (see sidebar, "Concept-generation tools."). Leaders can then leverage rapid formats such as pitch panels to further prioritize and refine the concepts. As American chemist Linus Pauling advised, "The way to get to good ideas is to get lots of ideas and throw the bad ones away."

Exhibit 8

What makes something a good idea?

Equation to use with valuable problems to solve



[1]Willingness to pay is a proxy for customer ascribing meaningful value. Whether companies choose to charge and who pays is a business-model decision.

McKinsey & Company

Evolve. Today, countless companies are seeing dramatic shifts in their profit pools and the economics that support their operations. Crises like the one we are living through today are watershed moments for companies to *Evolve*. Successfully managing a business model shift first requires determining which aspects of the model have been impaired and are unlikely to return. If a company derived an advantage from a field sales force that can no longer call on customers or brick-and-mortar storefronts that now have reduced foot traffic, for example, it will need to pivot to develop a digital approach. While some of these challenges may ease as lockdowns are lifted, other market dynamics and ways of working may be permanently altered. As recent research shows, Chinese consumers' offline consumption dropped almost 70 percent with shelter in place restrictions and only half of that volume returned after the lockdown was lifted; likewise, consumer adoption of telemedicine appears to be sticking. That, in turn, will have implications for an organization's assets, tools, and capabilities.

Experimenting with alternative business models—by asking, for instance, "What if we were acquired by organization X today?"—can be a great way to test what an organization could accomplish by evolving its business model. Removing constraints and questioning previous assumptions about what will generate the most value are powerful ways to conceive new business and economic models.

Choose. So, how does one fund the innovation required to make this kind of pivot? Revisit the innovation pipeline with fresh eyes and reprioritize resourcing. Challenging the core assumptions that support each initiative can determine which initiatives to continue, pivot, or cut. One of the biggest mistakes an organization can make is to let assumptions become assertions. The value, timing, and risk of initiatives will likely change in the "next normal" as market dynamics evolve and customers rethink their needs and associated spending.

Reconstructing the innovation portfolio based on what will drive the most value enables leaders to reallocate resources toward the best "next normal" opportunities and away from opportunities for which previous assumptions no longer apply. As an example, a consumer-packaged-goods company that planned to launch a product line centered around health enthusiasts in gyms may decide to shift resources toward building its direct-to-consumer e-commerce business that had been sidelined previously because of historic beliefs that demand was too small and customer adoption of virtual channels too limited. Today those beliefs may have reversed.

Aspire. Setting a new aspiration should act as a North Star that defines a combination of capabilities and strengths that will persist in the post-pandemic world. To do that, leaders may need to reframe their business and challenge orthodoxies that shaped the previous aspiration. As an example, the work-from-home technology platforms that once saw themselves as compliments to an office-based model could now envision their business as competition for the likes of WeWork and the biggest commercial real estate firms. They could also position themselves to become the platforms of choice for older generations of consumers, now savvier in the use of digital technology, to communicate with family and friends.

Accelerate and Scale. The global pandemic has significantly accelerated the pace at which companies are bringing new ideas to market, including massively expediting some regulatory processes and applying pressure on industry ecosystems to deliver scarce products and services in new ways. In a matter of weeks, some companies pivoted their existing manufacturing to support COVID-19 response: industrial companies are producing ventilators and hygienic masks, luxury brands are making hand sanitizer, and distilleries are producing disinfectant alcohol. Given the accelerated pace at which products and services are launched directly into market, it is critically important to ensure that supply chains and other enablers of scale keep pace to meet demand.

Extend and Mobilize. In some cases, businesses can leverage external partnerships to *Extend* their organization's reach and, in so doing, realize a higher return on innovation investment, mitigate risk, and help shape regulatory policies. One of the major early lessons of the COVID-19 crisis is that competitors and firms from completely different industries can suddenly become allies. We have seen this in the more than 15 pharmaceutical companies that agreed to share compound libraries in the search for a coronavirus therapy, and in the public-private partnerships created to help flatten the infection curve and prepare for the reopening of economies.

To enable such extensions, organizations will benefit from instilling an agile culture and working model that help *Mobilize* innovation. Speed is an important driver of innovation success, as is the ability to persist despite the hardships that a crisis imposes.

The essential practices underpinning distinctive innovation have not changed in this time of crisis, but the relative emphasis and urgency of where businesses should focus has. Whereas in our 2019 article "The innovation commitment" we highlighted *Aspire* and *Choose* as disproportionately important during times of stable economic growth, we believe the uncertainty and severity of the current crisis requires leaders, first and foremost, to re-*Discover* customer needs and *Evolve* their business models to meet those needs.

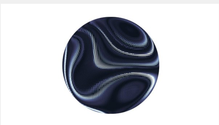
Above all, organizations need to realize that innovation, now more than ever, is a choice. Regardless of the relative emphasis and order, we believe that the Eight Essentials of Innovation, which for years have helped leading innovators more than double the total returns to shareholders compared to laggards, will continue to be critical in navigating and emerging even stronger from this crisis.

About the author(s)

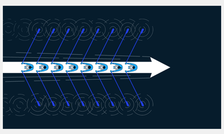
Jordan Bar Am is an associate partner in McKinsey's New Jersey office, where **Felicitas Jorge** is a consultant; **Laura Furstenthal** is a senior partner in the San Francisco office, and **Erik Roth** is a senior partner in the Stamford office.

The authors wish to thank Matt Banholzer, Katie Kroeger-Davis, Katie Lelarge, Olivia Papa, Lakshmi Prakash, Brian Quinn, and Henrik Sachs for their contributions to this article.

RELATED ARTICLES



Article
The COVID-19 recovery will be digital: A plan for the first 90 days



Article - *McKinsey Quarterly*
The innovation commitment

Article - *McKinsey Quarterly*
The eight essentials of innovation

McKinsey & Company

SUBSCRIBE TO OUR LATEST INSIGHTS

Email address

Contact us FAQ Privacy policy Cookie policy Terms of use Local language information Accessibility statement

McKinsey Insights - Get our latest thinking on your iPhone, iPad, or Android device.

Download on the App Store GET IT ON Google Play

© 1996-2020 McKinsey & Company